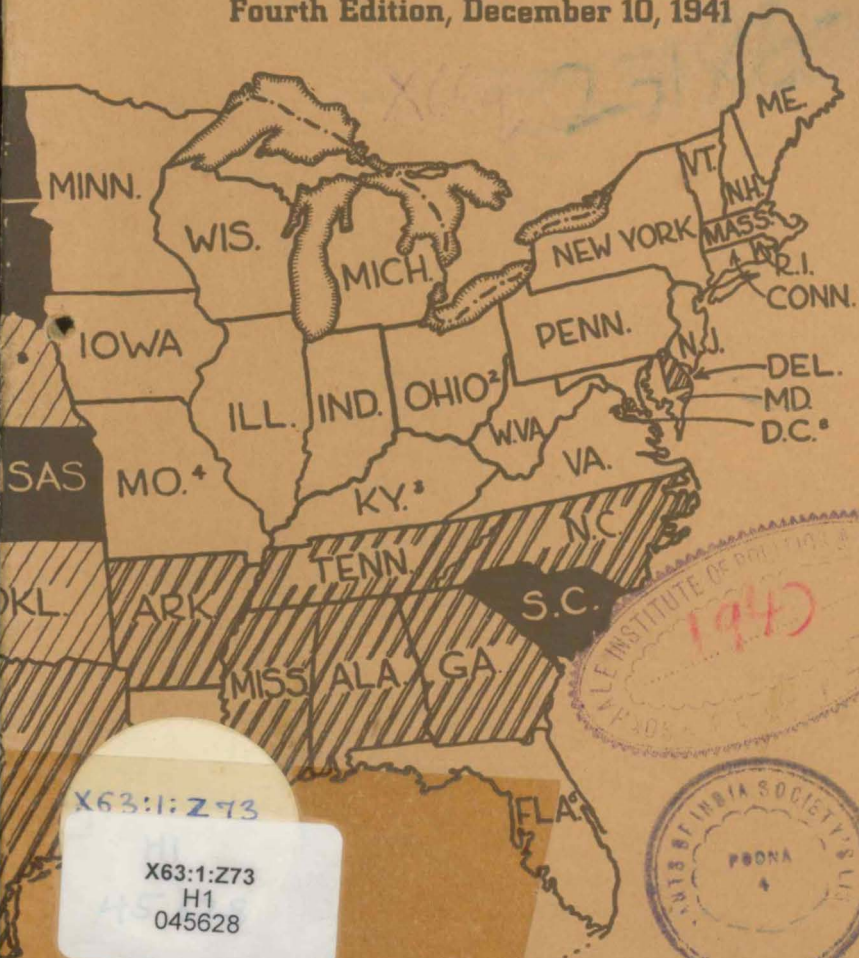


# SMALL LOAN LAWS OF THE UNITED STATES

Fourth Edition, December 10, 1941



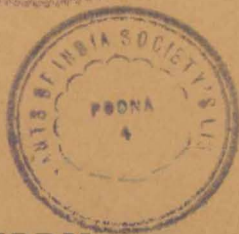
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**POLLAK FOUNDATION  
FOR ECONOMIC RESEARCH  
NEWTON, MASSACHUSETTS**



## POLLAK PAMPHLET 37

*First edition, March 10, 1939*

*Second edition, April 20, 1939*

*Third edition, May 20, 1940*

*Third edition, reprinted, March 10, 1941*

*Fourth edition, December 10, 1941*

### ACKNOWLEDGMENT

*The aid is hereby gratefully acknowledged of Rolf Nugent and John E. Hamm, of the Russell Sage Foundation, who furnished valuable materials and read both the manuscript and the proofs of this pamphlet.*

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## Small Loan Laws of the United States

**T**HE great majority of consumers must satisfy most of their material wants by the use of money. At times their needs can be supplied from current income. But when their needs temporarily exceed their incomes and cash reserves are lacking, they want to borrow. Indeed, in many cases, they must borrow or suffer intolerable hardships. The result is a demand for small loans which exists whether or not a means is provided to satisfy that demand within the law.

As a rule, anyone may make small consumer loans without obtaining a state license and submitting to regulation, provided that interest does not exceed certain legal maximums. These maximums, which vary from state to state, range from 6% to 12% per annum. In most states, the maximums are set by the general interest or usury laws; in a few states, by other laws.<sup>1</sup>

Even when usury laws are interpreted strictly by the courts, evasion devices are numerous; and penalties for infractions generally are too mild to discourage determined violators. As a rule, it is the small loan law, rather than the usury law, which blocks evasions and provides effective penalties.

The consumer demand for small loans cannot be met at

<sup>1</sup> Colorado, Maine, Massachusetts and New Hampshire have no usury laws, and Rhode Island's general interest limits are too high to be restrictive. In these five states, effective limits on loans of \$300 or less are set in the small loan laws, which prohibit the taking of interest greater than 6% to 12% per annum except by licensees.

For an up-to-date discussion and a complete chart of general usury statutes, see "*A Survey of the General Usury Laws*," by Benj. S. Horack, in *Law and Contemporary Problems*, Vol. VIII, No. 1, Duke University, N. C., 1941.

rates of 6% to 12% per annum. At 12%, the interest on a \$50 loan, repaid in 10 monthly instalments, is \$2.75. It costs a commercial agency nearly that much to investigate applicants and close the loan, to say nothing of bookkeeping costs, collection costs, bad debt losses and return on the investment. Banks, lending comparatively large amounts on preferred security, at less expense per dollar and at less risk, can and do lend to consumers at 12%, or at an even lower rate. Credit Unions, with the help of numerous expense short-cuts, make even small loans at 1% a month. But these agencies fall far short of meeting the entire demand.

If the state decides to make loans available to nearly all employed workers, it must sanction charges which cover the necessarily high expenses of this kind of business. And if it wishes to prevent evasions and exploitation, it must provide for effective regulation and supervision. These are objectives of the small loan laws.

#### “SMALL LOAN LAWS” DESCRIBED

The statutes known as “small loan laws” govern the specialized business of lending small sums, usually defined as \$300 or less. Typically, such laws (1) permit lenders who obtain licenses to charge rates higher than those allowed by the general usury laws but no more than specified maximums; (2) establish standards for licensing; (3) prescribe certain practices and prohibit others; (4) establish a regulatory body, often empowered to make rules and regulations; and (5) impose severe penalties for violations. The laws generally do not apply to certain lenders such as national and state banks, building and loan associations, credit unions, industrial banks and pawnbrokers. Usually these lenders are subject to special laws.

Most small loan laws conform in chief respects to the Uniform Small Loan Law, a model act framed and recommended by the Russell Sage Foundation for the social purpose of eliminating illegal, high-rate lenders, and for the

purpose of providing a carefully-regulated source of credit to meet the demand for small loans. For this reason, the model law is used as a standard in describing the laws of the individual states.

Table I classifies the laws of the 48 states, the District of Columbia and the Territory of Hawaii, according to their effectiveness in placing the small loan business under social control. Because laws and economic conditions of the

TABLE I

Summary of Small Loan Laws <sup>1</sup>

(Abbreviations: USLL: Uniform Small Loan Law. Approx.: Approximate. Dr.: Draft. The Uniform Small Loan Law has been revised five times since first drafted in 1916. Since publishing the Sixth Draft in 1935, the Russell Sage Foundation has informally recommended certain improvements as to details and has the Seventh Draft in preparation. Compared to the refined and efficacious Sixth Draft, early drafts, tho advanced for their time, were crude and inadequate.)

Name of State	Relation to USLL	Maximum Rate <sup>2</sup>
Arizona	Early dr.; material variations	3½%
California	Two acts, taken together, approx. 6th dr.	2½-2% at \$100; flat 2% if security insured.
Connecticut	Approx. 6th dr.; differs in form	3-2% at \$100
Florida	7th dr. features; material variations	3½%
Hawaii	Approx. 6th dr.	3½-2½% at \$100
Illinois	Approx. 6th dr.	3-2½% at \$150
Indiana	Approx. 5th dr.; administrative rate control	3-1½% at \$150; 5¢ fee on some loans

<sup>1</sup> Particulars are taken from "Annotations on Small Loan Laws," by F. B. Hubachek, "Regulation of the Small Loan Business," by Robinson and Nugent, and other sources. (See list on p. 23.)

Canada enacted a Dominion small loan law, effective January 1, 1940, which provides a maximum charge of 2% per month, computed on unpaid balances.

<sup>2</sup> Rate per month on unpaid principal balances, unless otherwise indicated. Where more than one rate is given, the rate is a graduated rate; that is, the first rate is charged on a part of the balance up to a certain amount, and the second rate on the remainder. Thus, in Connecticut, the maximum charge for a month during which the balance is \$140 is 3% of \$100 plus 2% of \$40, or \$3.80.

Name of State	Relation to USLL	Maximum Rate
<b>Effective Regulation</b>		
Iowa	Approx. 6th dr.; administrative rate control	3-2% at \$150
Kentucky	Approx. 6th dr.; differs in form	3½-2½% at \$150
Louisiana	Approx. 4th dr.	3%
Maine	Early dr.; later features	3-2½% at \$150; 25¢ min. chg.
Maryland	Early dr.; by amendment approaches 4th dr.	3½%
Massachusetts	Prior to USLL; approx. early drs. in substance; administrative rate control	3-2½% at \$150 on unsecured loans; 3-2% at \$150 on chattels and endorsed notes; other rates
Michigan	Approx. 6th dr.	3-2½% at \$100
Minnesota	Approx. 6th dr.	3%
Missouri	Resembles 4th dr.	3-2½% at \$100 <sup>3</sup>
New Hampshire	Early dr.; amended to resemble 4th dr.	2%; fees, in advance, of \$1 on loans up to \$50, \$2 on larger loans up to \$300 <sup>3</sup>
New Jersey	Approx. 5th dr.	2½%
New York	Approx. 5th dr.	2½-2% at \$100
Ohio	Prior to USLL; approx. early drs.; added features	3% on first \$300 \$1 fee on \$50 or less
Oregon	Like 4th dr.; material variations; auto loans separately regulated	3% <sup>3</sup>
Pennsylvania	Resembles 6th dr.; differs in form; lacks some features	3-2% at \$150; 6% per an. after 18 mos.
Rhode Island	Approx. 6th dr.	3%
Utah	Early dr.; minor differences	3%
Vermont	Approx. 6th dr.	2½-2½% at \$125
Virginia	Early dr.; amended to resemble 4th dr.	3½%
Washington	Approx. 6th dr. with variations	3% to \$300; 1% to \$500; \$1 minimum
West Virginia	Like 4th and 5th drs.	3½-2½% at \$150
Wisconsin	Approx. 5th dr.; differs in form; administrative rate control	2½-2-1% at \$100 and \$200

<sup>3</sup> Step rate, i.e., maximum on loan over \$100 is 2½% a month throughout its life, and on loan of \$100 or less is 3% throughout. Above details and classification reflect amendments to the Missouri law enacted in 1939.

Because of the limited area, population and market of New Hampshire, and because legal small loan offices are available in three adjacent states, valid generalization as to adequate rates for other states cannot be deduced from the experience of New Hampshire.

Name of State	Relation to USLL	Maximum Rate
<b>Partially effective Regulation</b>		
Colorado	Differs greatly; permits fees and extra charges	10% a year; other chgs. <sup>4</sup>
Nebraska	Differs greatly; but has important USLL features	9% a year; plus fee of $\frac{1}{2}$ % of loan <sup>5</sup>
New Mexico	Differs greatly; permits fees and extra charges	10% a year; fee of $\frac{1}{2}$ % of loan; other chgs. <sup>6</sup>
Oklahoma	6th dr.; material variations	10% a year; plus fees
<b>Largely or Wholly Inoperative Laws</b>		
Alabama	Resembles 4th dr.	8% a year
Arkansas	Many features of USLL; no rate provision	10% per an. (usury law)
Dist. of Col.	Inadequate law; \$500 license fee	1% a month
Delaware	Inadequate law; supervision insufficient; suited to commercial and industrial banks	8% discount, including fee computed on original amount of loan
Georgia	Early dr. of USLL	1 $\frac{1}{2}$ % a month
Mississippi	Crude and confused; excessive fees; those charging more than 20% per an. (a violation of law) to pay privilege tax of \$2000; ineffective supervision	10% per an.; fees
No. Carolina	Inadequate law	6% a year
Tennessee	Resembles 4th dr.; material variations	6% a year; fee of not exceeding 1% a month
Texas	Very crude law; no size limit; no supervision	10% per an. (usury law)
Wyoming	Crude law	10% a year <sup>7</sup>
<b>No Special Small Loan Laws</b>		
Idaho, Kansas, Montana, Nevada, North Dakota, South Carolina, South Dakota		

<sup>4</sup> 10% per annum, plus fee of  $\frac{1}{2}$ % of amount actually loaned chargeable not more than twice in any calendar year, plus insurance charge, on auto loans, of \$5 for each \$100 or fraction thereof loaned. Special charges for loans of \$50 or less.

<sup>5</sup> The service charge probably can be repeated every 12 months, but on periods of less than 12 months, it must be prorated. In case of prepayment, unearned service charge must be cancelled.

<sup>6</sup> Footnote 4 applies, except that on auto loans lender may charge, for his own single interest protection, 5¢ for each \$10 of the amount loaned, and in addition may collect for other insurance of the security.

<sup>7</sup> Wyoming limits the contract rate of interest to 10%, and in addition makes it a misdemeanor to charge more than 25% per annum on sums less than \$200.

TABLE II

Summary of Small Loan Laws by Type of Law\*

- A. LAWS OF THE UNIFORM SMALL LOAN LAW TYPE . . . . .** 32 states  
 In 28 states of this group — the first 28 states in Table I — the small loan business has been brought under effective regulation. Operating under the Vermont law of 1939 (2½%-2¼% at \$125) are 13 licensees; and under the New Hampshire law of 1933 (2% a month, plus inspection fees) there are 21 licensees in 10 cities. Lending under the law in Georgia and Tennessee has dwindled to the vanishing point. The Alabama and Arkansas laws are dead letters, insofar as regulated licensed lending is concerned, because the permitted rates do not enable legal lenders to do business.
- B. LAWS OF OTHER TYPES . . . . .** 9 states  
 Colorado has adopted a system of interest plus fees that permits very high rates on the smaller loans; with the complexity of fees and the lack of regular reports from licensees, supervision is difficult. The Oklahoma law of 1941 is described on page 14. New Mexico's law, enacted in 1939, closely follows Colorado's. Nebraska's law limits interest and fees more effectively, but lacks important regulatory features. Mississippi's laws are confused and inadequate; illegal lending is widespread. Inadequate rates and other regulatory features render small loan laws of the following ineffective or inoperative: Delaware, North Carolina, Texas, and Wyoming.
- C. NO SMALL LOAN LAWS . . . . .** 7 states  
 Idaho, Kansas, Montana, Nevada, North Dakota, South Carolina, South Dakota.  
 The laws of North Carolina and Wyoming are so fragmentary and futile that these two states are regarded by some authorities as having no small loan laws.

\* Hawaii also belongs in Group A and District of Columbia also belongs in Group B.



states vary in many aspects, no classification is entirely satisfactory. As used below, "effective regulation" means that the small loan demand is supplied under exacting state supervision and that there is sufficient authority to stop illegal lending. However, in Ohio and some of the other states listed as having "effective regulation," there are objectionable features in the laws. "Partially effective" laws are those which promote lending but fail to provide adequate borrower protection. "Largely or wholly inoperative laws" are those under which few, if any, loans are made by lenders who obey those laws.

TABLE III

SUMMARY OF MAXIMUM RATES  
in States with Operative Small Loan Laws

<i>Maximum Rate*</i>	<i>States</i>
3½% a month	5 (Ariz., Fla., La., Md., Va.)
3½% a month on smaller balances, lower rates on larger	3 (Hawaii, Ky., W. Va.)
3% a month (plus in Ohio \$1 fee on loans of \$50 or less)	6 (Minn., Ohio, Ore., R. I., Utah, Wash.)
3% a month on smaller balances, lower rates on larger (plus certain fees in Ind.). Mo. has step-rate	9 (Conn., Ill., Ind., Ia., Mass., Me., Mich., Mo., Pa.)
2½% a month	1 (N. J.)
2½% a month on smaller balances, lower rates on larger	4 (Calif., N. Y., Vt., Wis.)
2% a month, plus fees	1 (N. H.)
9% per annum, plus charges	1 (Neb.)
10% per annum, plus service charges	2 (Colo., N. Mex.)
10% per annum, an initial charge of 5%, monthly charge of approx. 2%, with maximum of \$2	1 (Okla.)

\* See Table I for explanation of rates and details. These rates apply only to loans of \$300 or less.

## HIGHLIGHTS ON CERTAIN STATES

The following state-by-state comments give added details of the laws and observations on their workings in practice. The states selected are those which illustrate significant departures from the model Uniform Small Loan Law, as to maximum charges, or size of loans, or other regulatory provisions. This group occupies a position in-between the states with clearly adequate rates and effective supervision, and the states which outlaw the small loans business or ignore its existence.

### *Alabama*

Alabama's law, which on the surface resembles the fourth draft of the Uniform Small Loan Law, differs from that draft in important particulars. The Alabama law applies only to Jefferson County, one county out of sixty-seven, thereby excluding many communities large enough to have a small loans problem; the law applies only to loans of \$100 or less, a size class which includes only part of the demand for small loans; and the interest rate is set at "\$8 upon each \$100 for one year," which is the maximum contract rate of the usury laws. This means that, for the privilege of engaging in an unprofitable business, licensees must pay \$100 a year, file a \$1000 bond, and submit to regulation. In consequence, the law is a dead letter.

Lending of small sums is open and widespread, but it is high-rate lending, unsupervised and unregulated. Investigations have disclosed a common rate of 240% a year, with a rate of 432% a year not uncommon for negro borrowers.

### *California*

Until 1939, the money-lending laws of California were in a chaotic condition. There was great uncertainty, in many situations, as to what law applied.

In 1939, adequate small loan regulation was provided, patterned after the latest draft of the Uniform Small Loan

Law. This legislation, submitted to the electorate by reference, was approved by a vote of about two and one-half to one.

An act passed in 1941 apparently permits insurance companies to make loans without licenses, and to make the maximum charges allowed under the Small Loan Act and the Personal Property Broker's Act.

### *Colorado and New Mexico*

The Colorado small loan law of 1935 and the New Mexico law of 1939 depart from the usual practice of stating maximum rate limitations in terms of all-inclusive percentages computed on unpaid balances. Both laws subdivide the charges in detailed schedules.

In Colorado maximum charges are 10% per annum on unpaid balances, plus a service fee of not more than one-tenth of the amount actually loaned (to be charged not more than twice in any calendar year), plus an insurance charge on auto loans of \$5 on each \$100 or fraction thereof, which charge may be levied whether or not the insurance is placed with an insurance company. On loans of \$50 or less, the limit is a flat charge of one-tenth of the amount loaned on loans maturing in 61 days or less, and a flat one-fifth on loans maturing in 62 to 120 days. The over-all cost, not including insurance charge, is equivalent on loans repaid in 12 monthly instalments to roughly 3% a month on unpaid balances. On short-term loans of \$50 or less, lenders may charge the equivalent of 10% to 16% a month, and on a one-week loan may charge 10% a week (520% a year). These very high charges on very small loans encourage just that type of anti-social lending which most small loan laws are designed to obliterate.

In both Colorado and New Mexico, the rate section alone, with its complex provision for fees and insurance charges as well as interest, facilitates evasion and makes supervision difficult. In addition, the laws are weak in regulatory and supervisory features.

### *District of Columbia*

The law, adopted in 1913, limits loans to \$200 and the rate to 1% a month on unpaid balances. The license fee of \$500 is five times as high as the usual fee. The law is largely prohibitory in effect.

District of Columbia borrowers in large numbers go to Maryland and Virginia, where small loan laws are in active operation. Other borrowers patronize illegal lenders within the District who charge extremely high rates.

Conditions in the District are more favorable to low-cost lending than in any one of the 48 states; but because Congress has failed to pass a law that works, borrowers who obtain loans must pay either the rates of Maryland and Virginia or the extortionate rates of local, illegal lenders.

### *Florida*

A device used in many states to evade usury laws is called "salary-buying." The lender claims that he does not make loans, but purchases his customers' wages at a discount. The Uniform Small Loan Law defines such transactions as loans. Until 1941, Florida's law did not, with the result that Florida had numerous high-rate, unregulated "salary buyers." The new law covers salary buying, applies the original act to the entire state, and embodies many provisions of the latest drafts of the Uniform Small Loan Law.

### *Missouri*

Missouri's small loan law conforms rather closely to the fourth draft of the model act. In years past, however, regulatory authorities have been troubled by two important differences: first, the maximum rate has been 2½% a month, which has restricted the supply of smaller-sized loans; second, the section which declares wage assignments and sales to be loans has been inoperative.

Missouri borrowers who wanted loans from \$100 to \$300 were well served, apparently, by licensed lenders; but

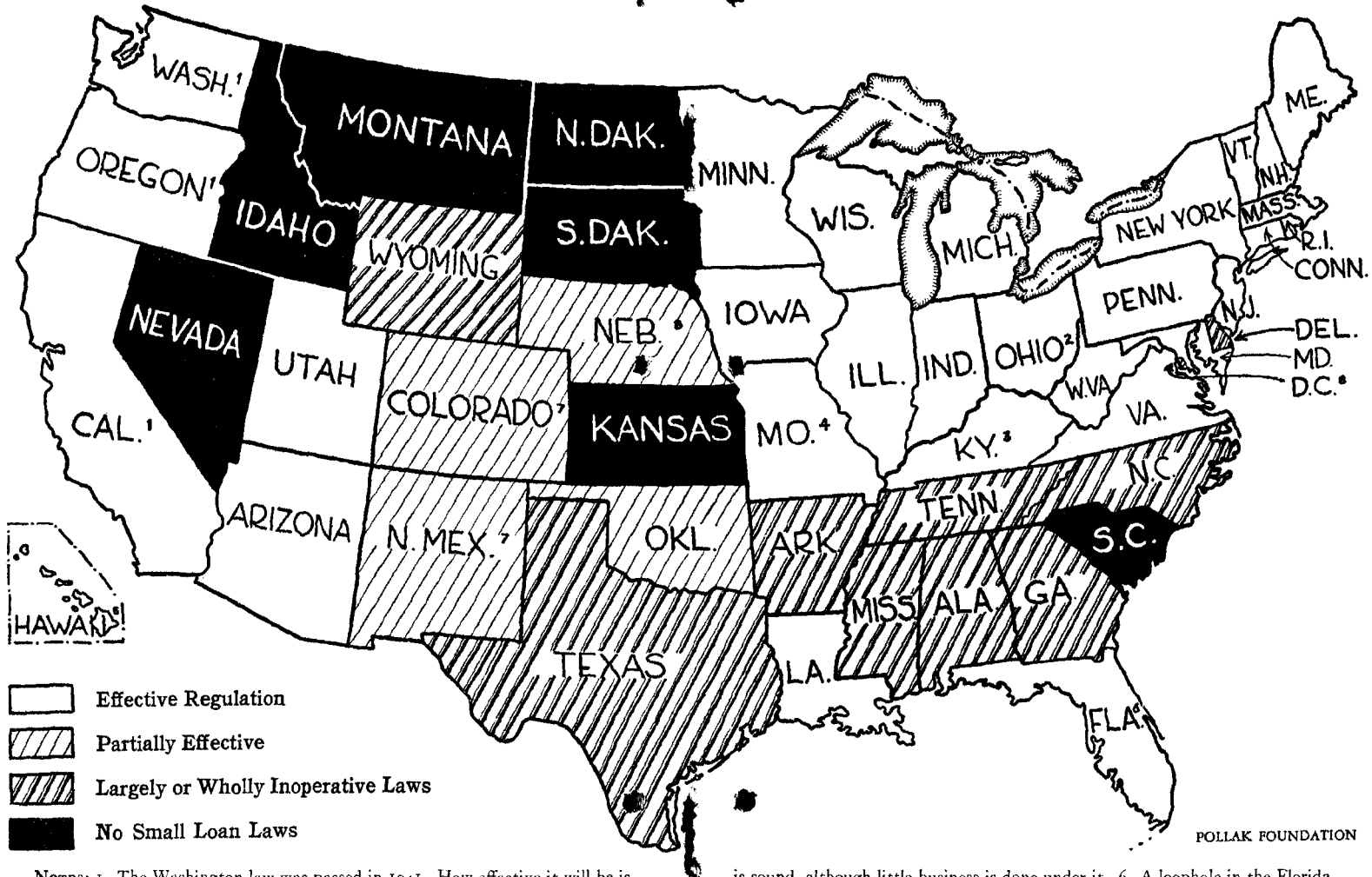
many borrowers who wanted smaller loans patronized illegal "salary buyers." A Kansas City investigation, conducted in 1936 by committees of the Better Business Bureau and the Bar Association, disclosed an estimated 10,000 high-rate borrowers, who with their families accounted for one-tenth of the city's population. The victims were steadily employed by well-known business firms, including railroads, meat packers, hotels, auto assembly plants and public utilities. The twelve salary buyers, all lending on wage assignments, were charging from 120% to 540% a year. Instalment payments on principal were not permitted, with the result that \$10, \$20 and \$30 loans, which might well have been liquidated in a few weeks, were outstanding years on end.

Closure of loopholes in the law and adoption of the 3% a month rate on loans of \$100 or less have greatly reduced illegal lending. However, many former salary buyers have used the loophole provided by the confused state of the Loan and Investment Companies Act.

### *Nebraska*

In 1941, the Nebraska Legislature repealed the 1915 Small Loan Law and enacted an entirely new law. The new law embodies some of the regulatory features of the latest drafts of the Uniform Small Loan Law. It differs from those drafts, however, in important respects. First, the new law purports to apply to all lenders, including banks, credit unions, and building and loan associations, who charge more than 9% per annum and to all loans, regardless of size or security. Second, the rate section provides for 9% per annum interest on unpaid balances, plus a service charge, on balances of less than \$1,000, of one-tenth of the amount of the loan. The right to collect the full amount of the service charge is restricted to an actuarial basis, which appears to be complicated. The new law differs in several other respects from the latest draft of the Uniform Small Loan Law.

# SMALL LOAN LAWS OF THE UNITED STATES



POLLAK FOUNDATION

NOTES: 1. The Washington law was passed in 1941. How effective it will be is not yet clear. The minimum charge of \$1 (abolished by Oregon in 1941) encourages lenders to make \$10 loans at very high rates. 2. Failure of the Ohio law to give the supervising officer enough power and failure to restrict the licensees to small loans cause trouble. 3. Exemption of loans on the sole security of motor vehicles has facilitated evasion in Kentucky. 4. Missouri has some high rate lending under a law which permits lenders to make hazard charges on automobile loans without issuing insurance policies. 5. The Hawaiian law

is sound, although little business is done under it. 6. A loophole in the Florida law which permitted a large volume of high rate lending by salary buyers was closed in 1941. 7. Rate regulations in Colorado and New Mexico differ from those of other states which have adopted drafts of the Uniform Small Loan Law. Some high rate lending is permitted under these laws, and regulation is ineffective. 8. The Nebraska and Oklahoma laws of 1941 are described in the text. It is too early to tell how effective regulation will be under these laws.

## *New Jersey*

From 1914 to 1929, under a rate of 3% a month, a broad small loan service was developed. Following a reduction in 1930 to 1½%, the legal business shrank to the point of extinction and illegal lending became widespread. In 1932, the legislature raised the rate to the present level of 2½% a month.

In November, 1929, there were 415 licensed small loan offices. In 1932, there were but 83, most of which were liquidating. In 1940, there were 117 licensees, with loan balances of about 20 million dollars. There now appear to be a sufficient number of lenders.

Conditions in New Jersey are particularly favorable to low-cost lending. Incomes are comparatively high; population is dense. Partly for this reason, partly as a result of vigorous law enforcement, lending is kept under state control and licensees' capital is available in adequate amount.

## *Oklahoma*

Until 1941, Oklahoma had no small loan law. Like Alabama, Texas, and several other states which have no laws or laws that fail to operate, Oklahoma was ridden with illegal lenders. The state is useful for illustration because a study in 1938 by Findley Weaver, Director of the Bureau of Business Research at the University of Oklahoma's Business School, and a study in 1940-'41 by the Junior Bar Conference, of the American Bar Association, provide illuminating data.

Analysis of 520 loans made by unregulated lenders shows that interest rates ranged from an average of 325% per annum on loans of \$10 or less, to an average of 56% per annum on loans over \$150. On loans of \$11 to \$20, repayable in four weekly instalments, rates averaged 600%. At the other extreme, the average rate on four of the larger loans was 29%, and the rate on one loan was 26%.

The average loan of the unregulated lenders was \$22.76, compared to \$121.60 for Oklahoma credit unions, which

lend to substantially the same kind of borrowers. For personal loan departments of commercial banks, which lend to more carefully selected risks, the average was \$218.82. Of the unregulated loans, 93% were for amounts of \$50 or less, and 96% matured within 6 months. For the credit unions, the corresponding percentages were 27% and 24%. In short, the unregulated lender makes a type of loan peculiarly his own — the small, exceedingly high-rate, quick-maturing loan.

This does not mean that consumers limited themselves to small total indebtedness; commonly, borrowers were in debt to six or eight lenders at once. Nor does the fact that over 80% of the loans were payable in three months or less mean that loans were in fact quickly paid. Because interest payments were so large, debtors had great difficulty in paying anything toward reduction of principal. On due dates, they usually renewed or shifted to other lenders. Rates were very high, but so were costs. Very small loans are expensive to make, particularly under the small-scale, inefficient organization which characterizes this illegal business.

In 1941, Oklahoma adopted a law which may put an end to most of the old-type illegal lending. However, the constitutional limit of interest to 10% per annum remains. In addition to the 10%, the law purports to allow an initial service and expense charge not to exceed 5% and a monthly charge of approximately 2%, with a maximum of \$2. The law has been in effect too short a time to enable anyone to tell how it will work, nor does anyone know what the courts will decree concerning the validity of the service and expense charges. On a small loan, paid in 3 months, an effective annual rate of 65% appears to be authorized by the new law.

### *South Carolina*

The plight of needy borrowers in South Carolina is what may be expected in every state which relies for the pro-



tection of poor people upon the general usury law. In South Carolina, the *permitted* rate on loans is 6 per cent per year, or 7 per cent in written contracts. The rate which borrowers *actually* pay to unregulated lenders in that state is revealed in "The Small Loan Problem in South Carolina," a study by William Hays Simpson of Duke University, published in 1940, and in a later study by the Junior Bar Conference of the American Bar Association.

In connection with the study by Dr. Simpson, 1,042 borrowers were interviewed in fourteen cities and towns in the state. Of these borrowers, the largest group, 262 white and 96 colored, paid interest at rates between 200 per cent per year and 300 per cent per year. The average rate ranged from 97.3 per cent on loans above \$50.00 to 462.7 per cent on loans of \$10.00 and less. Dr. Simpson concludes that the question in South Carolina is not whether small loans are to be made at rates permitted by the usury law: they are not made at those rates and will not be made. The question is, he concludes, whether lenders will be permitted, under a new law, to charge rates from 2½ to 3½ per cent per month, or whether hard-pressed citizens of the state will continue to borrow of illegal lenders at rates six to ten times as high. To date all efforts to relieve the plight of borrowers have failed. Relief may be obtained, the author concludes, only by passing a modern draft of the Uniform Small Loan Law.

### *Tennessee*

The State Constitution empowers the Legislature to "provide for a conventional (interest) rate, not to exceed ten per cent per annum." The Legislature has set the maximum contract rate at 6% per annum.

With this limitation in mind, the Legislature in 1925 passed a law, similar in form to the fourth draft of the Uniform Small Loan Law, which limited charges to interest of 6% per annum, plus fees not to exceed 3% a month on unpaid balances — an over-all maximum of 3½% a month.

The fees must not be arbitrary, the courts have ruled, but on each loan must be justified by specified services rendered and expenses incurred.

The Tennessee law has not accomplished its purpose. Supervision has been wanting and enforcement lax. Even under the adequate rates in force between 1925 and 1937, illegal lending was widespread. A 1936 drive in Memphis disclosed numerous unlicensed lenders who were charging 120% to 600% a year. The loans were small, typically \$5 to \$20, many borrowers were in debt on several separate loans. Some had loans with legal and illegal companies at the same time. Similar conditions were disclosed in Knoxville, Chattanooga and Nashville. Indignant, the legislature reduced the fee rate to 1% a month and the law became inoperative.

Possibly the law itself, framed to take account of the constitutional usury limit, afforded a shaky foundation on which to build a permanent legal business. Possibly the banking department correctly explained the difficulty when it stated that it did not have a staff sufficient for enforcement. The law itself falls short of the best; it does not require regular accounting reports and does not grant supervisory officials the right to establish rules and regulations. Whatever the cause, supervision was ineffective and prosecution was confined to infrequent drives by the Attorney General. Evidently the small loan law does not enforce itself.

In 1936 there were 56 licensees, and no doubt many borrowers obtained loans at legal rates. Under the present 1½% total charge, only six companies are qualified as small loan lenders.

### *Texas*

The under-cover nature of illegal lending prevents the collection of complete statistics. Enough is known, however, to give Texas first place among the loan shark states. A year or two ago, California or Florida or Washington

might have questioned the claim of Texas to such distinction; a year or two before that, Minnesota; and before that, Kentucky; but, year by year, some of the chief markets of illegal lenders have been all but banished by the passage and enforcement of adequate small loan laws.

Today, according to the findings of Rolf Nugent of the Russell Sage Foundation, Texas has a volume of illegal lending far larger than that of any other state. Of the total loan balance of loan sharks in the United States, the largest part, 35.1 millions of dollars, is in 10 states which have either no small loan laws, or largely or wholly inoperative laws.\* Of these 35.1 millions, 9 states, combined, have about one-third, and the other state, Texas, has the remaining two-thirds. Much of the other loan shark business is in the District of Columbia and in the 6 states of Alabama, Arkansas, Delaware, Georgia, Mississippi, and Tennessee. In these 7 jurisdictions combined, however, the loan shark balance is only 12 millions, compared with 23 millions in Texas, alone.

Other states, even some of those which are mainly agricultural, have large industrial centers in which the loan shark business is comparable to that of certain sections of Texas; but some of these states have small populations. For example, the 5 unregulated mountain states and west north central states, combined, have little more than 2% of the population of the United States, whereas Texas alone has nearly 5%.

In 1939, the Better Business Bureau of Dallas, Inc., published statistics of the first 1,000 complaints made to the Anti-Usury Committee, during the first ten weeks of the Committee's activities. These 1,000 complaints involved 2,554 separate loans made with 72 lending companies. The lowest rate charged was 120% per year; the

\* These 10 states are Idaho, Kansas, Montana, Nevada, North Carolina, North Dakota, South Carolina, South Dakota, Texas, and Wyoming. The estimates are from Rolf Nugent, *The Loan Shark Problem, Law and Contemporary Problems*, Vol. VIII, No. 1, pp. 7-9; Duke University, N. C., 1941.

highest was 1131.4%; and the average was 271.68%. The Committee estimates that illegal lenders annually collect from Dallas citizens, in usurious interest, about one and a quarter million dollars.

Unfortunately, Texas still relies, for the protection of its necessitous borrowers, on the inadequate provision in the Constitution which forbids lenders from charging interest at a higher rate than 10% per year.

### A SOUTHERN STATE TRIES REGULATION

Prior to 1934, Kentucky was known as "The Loan Shark State." The other states also had rights to that title, Kentucky did serve as headquarters for a large high-rate illegal concern lending across state lines, and her own people were sorely exploited by numerous illegal lenders. The wage-earner bankruptcy rate was eight times the national average. According to one estimate, illegal lenders in Kentucky, with more than 70,000 accounts, exacted an annual total of \$5,000,000 in charges. A common charge was 10% for two weeks, equal to 260% a year. Worse still, many borrowers were not allowed to pay in instalments what they had borrowed, and so remained in debt year after year.

In 1934, however, Kentucky passed a thoro-going regulatory law. During 1937, the third full year of operation, licensed lenders had on their books an average of 30,550 accounts and collected total charges of \$1,053,417. Some illegal lending persisted, but most of the 20-per-cent-per-month illegal lenders had been driven out. Exemption of loans on the sole security of motor vehicles has facilitated evasion, but this has been overcome, for the most part, by vigorous enforcement. The fact that the average loan, \$102, was appreciably smaller than in northern states suggests that Kentucky's rate of 3½% on the first \$150 and 2½% on the remainder may be made to work even in states with scattered population and relatively low incomes.

## THE MASSACHUSETTS SMALL LOAN LAW

Massachusetts was one of the first states to enact a law of the type now on the statutes of 33 states. This law, which was passed in 1911, was thoroly revised in 1916 to do away with the charging of fees, which had resulted in excessive charges on the smaller loans. The 1916 law, with minor changes, is the law of today. It resembles the first draft of the Uniform Small Loan Act, but differs markedly in form and wording. Many of the detailed features of the more modern drafts are absent.

Nevertheless, the law accomplishes its purpose. In 1934, when proposals for drastic reduction of rates were before the legislature, officers of 49 leading Massachusetts social agencies asked that the law be retained without change. There is little illegal lending and borrowers' complaints are negligible.

The law works well, even without detailed proscriptions, partly because wide powers are vested in the supervisory authorities, and partly because these authorities have been able, intelligent and active. Administrative orders, used flexibly to correct faults as they develop, have the force of law. Moreover, licensees, before taking legal action against delinquent borrowers, report their intentions to the Small Loans Supervisor, who examines the circumstances with a view to forestalling harsh actions. Rarely are household goods in use by borrowers taken in satisfaction of lenders' claims. Under less efficient supervision, however, the imperfections in the law might cause much trouble.

Massachusetts has administrative rate control; the Commissioner of Banks, with due regard for the amount, security and time of loans, may set rates lower than the 3% a month maximum written into the small loan law. An additional reduction became effective on October 1, 1937. The rate on by far the largest class of loans — those secured by chattel mortgages, endorsers or co-makers — was set at 3% a month on the first \$150 of the loan balance,

and 2% a month on any excess. For unsecured loans, the rate is 3% a month on the first \$150 and 2½% on any excess; for real estate loans, 2% a month; and for loans secured by bank books, insurance policies, stocks and bonds, 1% a month.

An act passed in 1941 makes the small loan law inapplicable to sales finance transactions.

#### SUMMARY

Since May 20, 1940, when the third edition of this pamphlet was published, far-reaching changes have been made in the small loan laws of several states. These changes are reflected in the map on pages 12-13. Florida and Washington have been added to the first group; Oklahoma has been added to the second group; Florida has been dropped from the second group; Oklahoma and Washington have been dropped from the fourth group.

Nine states and the District of Columbia still have largely or wholly inoperative laws. The laws of Alabama, Arkansas, Georgia, Tennessee, Texas, and the District of Columbia embody important parts of certain drafts of the Uniform Small Loan Law, but these laws are ineffective because under the permitted rates commercial lenders of small sums cannot do business; while the laws of Delaware, Mississippi, North Carolina, and Wyoming are too fragmentary and weak to be operative.

There are still 7 states, the black ones on the map (Idaho, Kansas, Montana, Nevada, North Dakota, South Carolina, and South Dakota) which have no special small loan laws, and two states (North Carolina and Wyoming) with laws which, for practical purposes, might be called "no small loan laws."

#### URBAN POPULATIONS SERVED UNDER SMALL LOAN LAWS

However, the number of states with small loan legislation is less significant than the number of individuals to

whom a regulated loan service is available. The demand for small loans is chiefly among city dwellers who must pay money for nearly everything they use, and who are able to meet instalment payments from their regular pay envelopes. Farmers, in contrast, who have irregular incomes, and are widely served by private, cooperative and governmental loan institutions, seldom patronize small loan companies.

Table IV shows that about 84.4% of the urban population of continental United States now resides in states with fully effective small loan regulation, compared with 75.1% before California, Florida, and Washington improved their laws.

TABLE IV  
POPULATION OF STATES WITH VARIOUS TYPES OF  
SMALL LOAN REGULATION

	Number of States*	% of Total U.S. Popula- tion in Group	% of U.S. Urban Popu- lation in Group
Effective Regulation . . . . .	28	72.8	84.4
Partially Effective . . . . .	4	4.1	2.8
Largely or Wholly Inoperative Laws . . . . .	9	18.1	10.4
No Small Loan Laws . . . . .	<u>7</u>	<u>5.0</u>	<u>2.4</u>
TOTAL, CONTINENTAL UNITED STATES . . . . .	48	100.0	100.0

\* The District of Columbia is included, but not the Territory of Hawaii.

Most of the states which have not yet enacted effective laws are mainly agricultural. However, the District of Columbia is 100% urban, and Colorado and Texas are more than 40% urban.

The total urban population of the states which have partially effective laws, inoperative laws, or no laws, is under 11,000,000. Yet even those states which are chiefly rural, such as Alabama, Arkansas, Georgia, Mississippi, North Carolina, and Tennessee, have large population centers with an active, continuous demand for small loans. In all such states, this endless demand creates an inescapable and pressing social problem.

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