Report of

Interim Committee

OF THE

House of Representatives

STATE OF MINNESOTA

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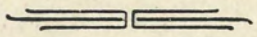

SMALL LOAN LEGISLATION

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REPORT OF THE INTERIM COMMITTEE OF THE MINNESOTA HOUSE OF REPRESENTATIVES

To the House of Representatives of the Forty-sixth Session of the Legislature of the State of Minnesota:

The undersigned members of the House of Representatives of the Forty-fifth Session 1927 were appointed as members of a committee, to make a study of the conditions and practices in connection with the making of small loans and report its findings and recommendations in connection therewith to the Legislature at the commencement of its session in 1929, pursuant to the following resolution adopted by vote of the House on April 21, 1927, to-wit:

WHEREAS, serious evils exist in connection with the making of small loans within the State; and

WHEREAS, numerous bills were introduced in the 1927 Session of the Legislature, none of which met with the approval of either the House or Senate; and

WHEREAS, it is desirable that the remedial legislation be framed and presented to the Legislature at the commencement of its Session in 1929, to correct the evils conceded to exist.

THEREFORE, BE IT RESOLVED, that the Speaker be, and he is hereby authorized and directed to appoint a committee of five (5) members of the House, whose duty it shall be to make a study of the conditions and practices in connection with the making of small loans and report its findings and recommendations in connection therewith, to the Legislature at the commencement of its Session in 1929.

BE IT FURTHER RESOLVED, that the members of such committee shall receive their actual expenses paid and incurred for hotel and travel in the performance of their duties, to be paid out of the Legislative Expense Fund, by the filing by the members of such committee with the State Auditor a verified statement showing the amount of such expenses.

The State Auditor shall audit such claims and issue his warrant upon the State Treasurer to be paid out of the Legislative Expense Fund.

BE IT FURTHER RESOLVED, that before entering upon the performance of their duties the members of the committee so appointed shall make and file written acceptance of their appointment with the Secretary of State.

AND BE IT FURTHER RESOLVED, that the committee shall have authority to employ such necessary help and assistance as it shall deem necessary, so as to better expedite the business of the committee.

I.

INTRODUCTORY

As expressed in the foregoing resolution, the creation of this committee was an outgrowth of efforts made in the House and Senate of the Legislative Session of 1927, to enact legislation to deal effectively with certain serious evils admittedly existing in the making of small loans in Minnesota. In fact the background of this committee antedates the Session of 1927. In previous sessions bills directed at the evils existing in the small loan business were introduced and considered. Interest has centered in the princi-

ples embodied in the Uniform Small Loan Law, because this is the type of legislation which has been enacted in those states which have sought to solve the problem. In the 1923 Session this bill received the approval of the House, but met defeat in the Senate. No attempt was made to revive it in 1925 largely perhaps because in that Session there was no change in the personnel of the Senate which had disapproved the bill. In 1927, the friends of this bill renewed their efforts to secure its passage, and it was introduced in the Senate as Senate File No. 61 and in the House as House File No. 63. Another bill seeking to remedy the same evils was likewise introduced in the House as H. F. No. 89 and in the Senate as S. F. No. 1150. Following the defeat of H. F. No. 63 and as a result of the discussion upon that bill, a drastic measure, H. F. No. 470, proposing to make usury a felony, was introduced. This bill was referred to the Committee which had under consideration the other small loan bills, and it remained there without futher action. After defeating H. F. No. 63, the Uniform Small Loan Bill, the House voted favorably on a motion to reconsider the same, and the bill was re-referred to the committee which had recommended its passage. The defeat of the companion bill S. F. No. 61, however, convinced the proponents of this legislation in the House that the chances of enacting such legislation at the 1927 Session were slight. However, the friends of this bill, although defeated, were encouraged by the fact that the existence of these evils was disputed at no time in the discussion upon these bills. The only question raised was that of the proper type of legislation for eradicating the loan shark and at the same time avoiding any evils which might be incidental to the solution of this old problem. The gravity of the situation and the apparent determination on the part of the members to eliminate the loan shark, prompted the introduction of the foregoing resolution. The authors were convinced that further study was necessary to determine and formulate proper legislation, and that this could best be done by an interim committee devoting the necessary time to the study of this problem.

II.

INVESTIGATION

At the outset the committee found that the burden of its duty was considerably lightened by reason of the fact that there was no lack of evidence that grave evils existed in our State in the business of making small loans. The existing conditions revealed in the hearings before the committees of both House and Senate, and admitted in argument by opponents of the bill in both bodies, left no room for doubt that the burden of this committee's duty lay not in the matter of investigating and proving the existence of the evil, but rather in determining the proper remedy. Although admitted, the loan shark evil, as it exists in this State and elsewhere and as it has existed elsewhere in the past until curbed by proper and effective legislation, is discussed in this report for the purpose of clarifying the issue, and as a foundation for the findings and recommendations made by this committee.

The storm center of the loan shark question in the Session of 1927 was the so-called Uniform Small Loan Law, introduced as S. F. No. 61 and H. F. No. 63. Because of this fact and also because of the fact that laws embodying the principles of the Uniform Small Loan Law have already been enacted in twenty-four states, the committee adopted this as a starting point.

In this way an opportunity was afforded to study the practices of the loan shark in these states before such laws were enacted, and the effect which the administration of these laws has had on the practices of the loan sharks, as well as its effect upon the small loan business in general.

After some consideration as to the course of study and investigation to be followed, the committee decided to visit several states in which the law had been enacted and in operation for a period of time sufficient to give it a fair test. Time and expense were important considerations, as well as information and results to be obtained. And upon all these considerations, the committee determined upon visiting the States of Illinois, Indiana, Pennsylvania, New Jersey, New York, Connecticut and Massachusetts, all of which states contain many industrial centers, the field in which the small loan business is conducted, and all of which states have adopted remedial legislation dealing with this subject. In these states interviews were had with state officials charged with the administration of these laws, lenders operating under the law, borrowers, employers of labor, and representatives of various social welfare organizations. Some idea of the extent of these investigations may be gained from the following list of persons interviewed by the committee:

Chicago, Illinois:

Charles R. Napier, of the Chicago Bar, attorney for the Illinois Lenders' Association.

Joel D. Hunter, General Superintendent, United Charities of Chicago.

Irene V. McCormick, Chicago Legal Aid Bureau.

Marvin Poole, of Butler Brothers.

N. Y. Fowler, Attorney, Chicago Northwestern Railway Company.

Mrs. E. Pearl Warwick, Small Loan Examiner, Department of Trade and Commerce of Illinois.

Mr. Walling, President, Morris Plan Bank, Chicago.

Fred B. Snite, Albert Snite, Mr. Turginson and J. C. Houck, Lenders.

Indianapolis, Indiana:

Elmer Johnson, Supervisor, Industrial Loan Department.

F. L. Thompson, Chairman, American Industrial Lender Association.

J. H. Aufderheide, President, Metro and Commonwealth Loan Companies

A. C. Broughman, Legal Loan Company.

William R. Teel, Capitol Loan Company.

C. H. Stratton.

Judge James W. Collins.

Judge John Holtzman.

S. E. Foster, Director of Indianapolis Charities.

Harrisburg, Pennsylvania:

George H. Orth, Chief, Bureau of Private Banks.

Peter G. Cameron, Secretary of Banking.

Mr. Kerr, a lender.

Philadelphia, Pensylvania:

Charles G. Mueller, President, Community Finance Service.

Romain Hassrick, Secretary, Philadelphia Legal Aid Society.

Dr. Lewis N. Robinson, Swarthmore College.

Trenton, New Jersey:

J. F. Hammond, Deputy Commissioner, Bureau of Banking.

Col. Buckney, Mr. Watson, Mr. Smith, Lenders.

Vernon L. Buckman, Secretary, New Jersey Industrial Lenders' Association.

New York City:

John M. Glenn, General Director, Russel Sage Foundation.

Leon Henderson, Director, Department of Remedial Loans, Russell Sage Foundation.

Arthur H. Ham, Vice-President, Loan Society, and formerly Director Department of Remedial Loans, Russell Sage Foundation.

Walter S. Hilborn, formerly Acting Director, Division of Remedial Loans, Russell Sage Fundation.

Rolf Nugent, Assistant Director, Department of Remedial Loans.

Lawson Purdy, New York Charity Organization.

Dr. Franklin Ryan, Author of "Usury and Usury Laws", Instructor of Banking, Harvard Business School.

Hartford, Connecticut:

L. E. Shippee, Deputy Commissioner, Banking Department.

John F. Dianno, Banking Department.

Mr. East, Lender.

Boston, Massachusetts:

Earl E. Davidson, Supervisor of Small Loan Agencies.

George W. Wightman, of Hale and Dorr, Attorneys for Beneficial Loan Society.

Lawrence E. Green, of Hale and Dorr, Attorneys for Beneficial Loan Society.

Herbert Wheeler, Treasurer, Boston and Main Railroad.

J. F. Turner, Auditor of Revenue, Boston and Main Railroad.

Miss Caroline Cook, Chief Supervisor of Incorporated Charities.

Richard D. Hall, Attorney for Boston and Main Railroad.

L. A. Barthelmus, Chairman of Legislative Committee of Brotherhood of Locomotive Engineers for Massachusetts.

Also a number of Massachusetts Lenders.

A voluminous record of these personal interviews has been kept and the committee hopes that it will be found possible to make this record available to the members of the Legislature.

These interviews have been supplemented by a considerable volume of documentary evidence which has been gathered, by study and investigation of certain phases of the question by individual members of the committee and by discussion of the whole problem in its various phases by the entire committee. Based upon these studies and investigations the committee makes the following as its findings, relative to the small loan business, its evils and the proper remedy therefor.

III.

FINDINGS

1. That all classes of people, rich and poor alike, from time to time have not sufficient money to meet their immediate needs and must therefore resort to borrowing.

We commence with the basic proposition that the borrowing of money is a practice which is not limited to any one class or to any certain classes of people. The lending of money is a legitimate business, long recognized as such, and occupies an important place in modern society. No great advancement in production can take place without capital. If every person were limited in his operations to the use merely of what he could obtain by his two hands, if he were limited to that which he could produce and enjoy only by his own unaided efforts, day by day, and were not able to discount the future by borrowing against it, it would not be long before the comforts that all classes now enjoy would vanish. The purposes for which money is borrowed and the conditions which create the need for borrowing money vary. A large corporation may borrow several million dollars through the medium of a bond issue for the purpose of extending its field of operations. The merchant of our smaller communities may borrow several thousand dollars to finance the purchase of a stock of goods. The small manufacturer may borrow from time to time to meet his pay roll or other immediate and pressing obligations of his business. Loans such as these are known as productive loans, the proceeds of the loan being used in further production.

As the great mass of borrowing transactions with which most persons are familiar are those which take place between the comparatively well-to-do, it has largely escaped observation that those besides the well-to-do must borrow. The manufacturer, merchant and farmer must borrow to carry on their legitimate operations. But there is another class of persons whose reason for borrowing is more imperative than that of the well-to-do. That reason is the need of food, clothing, shelter and other necessities of life. A wage earner is out of employment for a period of several weeks or months. His needs and the needs of his family continue and must be provided for. He seeks to borrow money as the only way to tide over this unemployment period. Or perhaps his wife or a child is ill for some time. He carries the added burden of doctor and hospital bills, besides employing help to care for his family. Perhaps this added expense approaches or even exceeds his income, yet the expense must be met and can be met only by borrowing. Or sometimes death in the family creates the immediate demand for money, which frequently cannot be supplied from the resources at hand. Borrowing is resorted to as the only way in which such an emergency can be met. These and other conditions create the need for borrowing money to provide the necessities of life. Loans of this type are known as consumptive loans, because as distinguished from productive loans, the proceeds are not used in further production, but are consumed by the borrower in providing life's necessities for himself and family. Specific instances may be cited of consumptive loans unwisely made, cases in which the borrower should not borrow. Still the demand for consumptive loans is as genuine and legitimate a demand as that for productive loans and therefore a demand for which provision should be made.

2. That for the purpose of protecting the borrower against extortionate rates of interest, laws have been enacted limiting the rate of interest which the lender may charge and receive.

Society has long recognized the weakness of the borrower's position as compared with that occupied by the lender, and the need of protecting the borrower against the avarice of the lender. To give this protection, laws

were at one time enacted in the countries of Europe, prohibiting the charging of interest. One fundamental fact was not taken into account, i. e.: that unless a lender is compensated in some manner he will not part with his money to make a loan. Since people found it necessary to borrow, these laws were evaded. Loans were made and interest was charged. The pressure of rising commercial and industrial interests increased the need of borrowing and finally the necessity of recognizing what was actually taking place in business resulted in the modification of these prohibitory laws, and the laws prohibiting interest were replaced by laws prescribing a maximum rate of interest which might be charged for any loan. Such laws are commonly known as usury laws.

All of our states except six have usury laws upon their statute books. Six of our states fix no maximum limit and permit the charging of any rate of interest. The other forty-two states fix maximum rates of interest, varying from six to twelve per cent per annum. In most cases these usury laws provide penalties for charging a rate of interest in excess of the maximum rate. In some states the penalty is forfeiture of excess interest, which clearly is no penalty at all. Some statutes provide for forfeiture of all interest. Others prescribe as a penalty the forfeiture of both principal and interest.

In Minnesota usury consists of charging a rate of interest in excess of eight per cent per annum, and our statute provides a penalty of loss of both principal and interest for violation of this maximum limit fixed by law. Contrary to the opinion of some, however, usury is not a criminal offense and no criminal prosecution can be had, regardless of the rate of interest which the lender charges.

3. That the general usury laws of this state and of other states are such as to render it impossible for the average consumptive borrower to obtain money at a rate of interest within the limit fixed by law.

It is difficult, if not impossible, to ascertain with any degree of accuracy the percentage of the people of the country who are so situated as to be able to borrow at banks or elsewhere at rates within the maximum rates fixed by law. Some authorities assert that only about fifteen per cent are capable of borrowing at banks or elsewhere at the normal contract rate of interest, leaving about eighty-five per cent who must borrow, if at all, from other sources and at higher rates, whenever the necessity for borrowing exists. These percentages will, of course, vary between states and between different localities within the same state. In the smaller cities and villages where the people are better acquainted and where the extremes of wealth and poverty are not so great, the percentage of those who can borrow at legal rates will be found higher. In the large centers of population, however, as in the three large cities of Minnesota, the percentage capable of obtaining money at banks or elsewhere within the legal interest limit is relatively small.

As a general proposition banks are not interested in making personal loans for consumptive purposes. The borrower has not sufficient security to meet the demands of the banks, and if he had, the expense of making the small loan is so great that it is not regarded as profitable or desirable. Clearly a bank prefers to make one loan of $5,000 rather than to make one hundred loans of $50.00 each, or twenty-five loans of $200.00. The

result is that in the average large city, the man who seeks to borrow for consumptive purposes finds that banks are not at all interested in his needs nor is anyone else interested in supplying the money at a rate within our eight per cent maximum.

4. That the Necessitous borrower, unable to borrow at banks or elsewhere at legal interest rates, will and does borrow from other sources at higher rates.

The fact that a necessitous borrower in desperate need of funds to provide life's necessities for himself and family, is unable to borrow money at an interest rate of eight per cent per annum does not mean that he will not borrow. If he can obtain the money which he needs at a higher rate of interest, he will gladly pay it, and he will pay whatever interest rate is necessary to obtain the loan. The rate may be such as to shock the conscience and intelligence of one who does not occupy the position of borrower, but to the borrower the immediate need is larger and more important than the more remote day of reckoning. Somehow, if he looks into the future at all to consider the matter of repayment, he hopes for the best, but the circumstances which make the loan necessary must be met at any cost. The borrower is willing to pay a higher rate; if he can find someone who will loan him the money he will contract to pay any rate of interest demanded of him.

5. That to meet the needs of this large class of borrowers who cannot obtain money at legal rates of interest the loan shark has appeared, supplying the need, but at unreasonable and extortionate rates of interest.

As might reasonably be expected where such an insistent demand exists, there will be a supply to meet and satisfy the demand. Those furnishing the supply may assume great risk in doing so, but the magnitude of the risk is offset by the compensation which is demanded and received.

The needs of this large class who cannot borrow money at legal rates are supplied by lenders commonly known as loan sharks, who make a business of lending money in small sums at illegal rates of interest. It is to the loan shark that the necessitous borrower turns for relief. Obviously this class of lenders assumes a great risk. They cannot lend money in small sums at legal rates and make a profit. As a business proposition, no one can make small loans on uncertain security, assume the risk of loss involved, pay overhead, cost of investigation and cost of collection and still make a profit. Under the general usury law of this State, if the lender charges more than that, the borrower is not obligated to pay anything in return, either interest or principal. But the loan shark charges more than the legal rate, because he cannot profitably make a loan within the limit fixed by law, and he charges an exorbitant rate because of the risk he assumes and because the borrower, unable to obtain a loan elsewhere at better rates, must and will pay almost any rate demanded. The interest rates charged by these lenders range from 120 to 400 per cent per annum and higher. The borrowers contract to pay these rates for one reason alone: their needs are so pressing that they must agree to these rates if they are to find any relief. Thus because of the urgent needs of the borrower

the loan shark is able to carry on his operations and contract for and collect unreasonable and extortionate rates of interest, in spite of our usury law with the drastic penalty which it prescribes.

6. That in the large industrial centers of Minnesota, as in similar centers of population in other states where effective legislation has not been enacted, loan sharks do a thriving business based upon rates of interest which range from 120 to 400 per cent per annum and higher.

The loan shark is not found in the smaller centers of population. The problem is an urban problem. If there are any necessitous borrowers in the smaller communities their numbers are small. The business of the loan shark must have volume. This volume can be had only in the large cities, with their large industrial population. In all these centers the loan sharks have made their appearance and here they continue to do business unless, as in many states, their activities have been curbed by proper legislation.

In the three large industrial centers of Minnesota, Minneapolis, St. Paul and Duluth, loan sharks are found in abundance. Accurate figures as to the number of these high rate lenders are not available, because of the fact that they are not subject to license, regulation or inspection, and are engaged in an outlaw business. However, a glance at the classified pages of the telephone directories of these cities will give some idea of the number of lenders engaged in business. The Minneapolis classified business directory, under the head "Loan Companies", contained eighty-five names, more than fifty of which are known to be loan sharks. The classified or ad section of one Minneapolis newspaper, under the head "Money to Loan," carries daily more than one full column of loan shark ads. These advertisements figured at minimum yearly contract rates aggregate a cost of more than $25,000 per year. Surely a business which can bear an advertising expense of this amount is not conducted on a small scale. It is estimated that the number of loan sharks operating in this State alone at the present time exceeds one hundred.

The actual volume of business done by these lenders cannot be ascertained. Their business is not subject to inspection by state authority and it naturally keeps itself under cover so far as possible. Perhaps the best estimate is that based upon a newspaper campaign against loan sharks, conducted by a Minneapolis newspaper in 1926. This paper invited all persons who were victimized by loan sharks to present themselves at the newspaper's offices, and make their troubles known. The offices were overrun by the numbers responding to the invitation. A volunteer group of twelve lawyers undertook to adjust the troubles of these numerous borrowers and contributed their services without charge. The task was so great that the number of lawyers was increased until forty were devoting a considerable part of their time to this work. The attempt to solve the loan shark problem in this manner was never completed. Similar newspaper drives against loan sharks have been inaugurated elsewhere, but all have led to the same conclusion that the problem is too far-reaching to be dealt with in that manner. Those who took an active part in this campaign concluded that there were no less than twenty thousand loan shark victims in the City of Mineapolis alone, and that three million dollars is a conserva-

tive estimate of the amount invested in this business in the three large cities of the State.

The most extraordinary case discovered was that of a borrower, who had been in the clutches of the same loan shark for a period of seventeen years. His transactions originated with a loan of $150.00, and he testified that he had paid almost $2,500 and still owed the lender about $175.00. We do not consider it necessary to go into further detail as to the prevalance of the loan shark evil in aggravated form in Minnesota. Its existence and activities have been denied by no one, and the admission of these conditions is contained in the resolution by which this committee was created.

The rates of interest charged by these Minneapolis loan sharks range from 120 to 400 per cent per annum. The same is true elsewhere, wherever loan sharks carry on their trade. On the following page there are a few cases picked at random from the files of the Minneapolis Legal Aid Society.

THE FOLLOWING ARE ACTUAL CASES HANDLED BY THE LEGAL AID SOCIETY OF MINNEAPOLIS DURING THE TIME M. U. S. KJORLAUG WAS ITS ACTIVE ATTORNEY

Our File Number	Loan Company	Amount of Loan	Payments	Time	Average Time of Loan	Gross Profit	Rate of Interest Per Year	Rate of Interest Per Month
13209	Ready Cash Loan Co.	$35.00	$6.45 semi mo.	3 mo.	1¼ mo.	$3.70	100%	8 1/3%
13209	Reliable Loan Co.	20.00	4.40 semi mo.	3 mo.	1¼ mo.	6.40	300%	20%
13209	City Loan Co	40.00	16.75 per mo.	3 mo.	1¼ mo.	10.25	246%	20½%
13209	Patterson Loan Co.	20.00	4.60 semi mo.	3 mo.	1¼ mo.	7.60	360%	30%
13209	F. C. Augustine	35.00	14.00 per mo.	3 mo.	1¼ mo.	7.00	192%	16%
5706	Minneapolis Loan Co.	25.00	6.50 per mo.	6 mo.	1¾ mo.	14.00	384%	32%
8315	Minneapolis Loan Co.	90.00	8.95 per mo.	9 mo.	2½ mo.	30.55	290%	24%
11042	Union Loan Co	30.00	8.00 per mo.	6 mo.	1¾ mo.	18.00	400%	33%
10310	Eagle Loan Company	50.00	22.00 per mo.	3 mo.	1¼ mo.	16.00	370%	31%
12404	City Loan Company	55.00	12.50 per mo.	6 mo.	2¼ mo.	20.00	250%	21%
10875	Minn. Mtg. Loan Co.	25.00	4.30 per mo.	9 mo.	2½ mo.	13.70	230%	20%
10867	Minn. Mtg. Loan Co.	60.00	7.70 per mo	10 mo.	3¼ mo.	27.00	200%	16%
14021	Minneapolis Loan Co.	60.00	8.30 per mo.	10 mo.	3½ mo.	23.00	130%	11%
10694	Minneapolis Loan Co.	75.00	9.75 per mo.	12 mo.	3¾ mo.	42.00	180%	15%
10161	Mpls. Credit Bureau	60.00	12.00 per mo.	6 mo.	2½ mo.	12.00	96%	8%
17619	Park Loan Company	15 00	.....	1 mo.	.....	3.50	280%	23 1/3%
17103	N. W. Loan Company	40.00	10.25 per mo.	6 mo.	3½ mo.	21.80	180%	16%
16891	Mutual Credit Co.	10.00	2.25 semi mo.	3 mo.	1¼ mo.	3.50	336%	28%
16891	Minn. Mtg. Loan Co.	40.00	3.10 semi mo.	10 mo.	6 mo.	22.00	108%	9%
16891	National Loan Co.	30.00	3 75 semi mo.	6 mo.	3½ mo.	15.00	168%	14%
16891	Local Loan Company	35.00	3.86 semi mo.	6 mo.	3¼ mo.	11.20	108%	9%
16891	Ready Cash Loan Co.	25.00	3.20 semi mo.	6 mo.	3 mo.	13.40	168%	14%
16891	City Loan Co.	15.00	3.50 semi mo.	3 mo.	1¼ mo.	6.00	384%	32%
16891	F. C. Augustine	50.00	6.50 semi mo	6 mo.	3 mo.	28.00	222%	18½%
16891	Carroll Loan Co.	40.00	6.30 semi mo.	5 mo.	3 mo.	23.00	240%	20%
16891	State Loan Company	75.00	5.00 semi mo.	10½ mo.	6 mo.	45.00	120%	10%
16891	Patterson Loan Co.	20.00	4.60 semi mo.	3 mo.	1¼ mo.	7.60	360%	30%
17343	F. C. Augustine	75 00	10.00 semi mo.	6 mo.	3 mo.	45.00	240%	20%
17085	Fidelity Loan Co.	50.00	12.75 per mo.	6 mo.	3 mo.	26.50	210%	17½%

7. That the loan shark by threats and intimidation preys upon the weakness and ignorance of the borrower with whom he deals.

Viewed in the light of calm reason and with knowledge of the usury law and its drastic provisions, it is sometimes difficult to appreciate the circumstances which enable the loan shark to carry on his business. The law is all against him. He risks the loss of every cent which he lends at usurious rates, but while the law is against him the facts are all in his favor. The borrower who deals with him is driven by necessity. The urgent nature of the borrower's necessity is what makes the usurious bargain possible. The terms of the bargain are dictated by the lender, not by the borrower. The borrower, in his necessitous circumstances, must accept the terms given him or go without the loan. He has no power to drive a bargain of his own. The lender scrupulously avoids giving the borrower a copy of the agreement entered into. Perhaps, as is often the case the borrower signs two or three notes for one loan, not knowing the nature of the instruments which he signs. Another common practice is to have the borrower sign a note in blank, an amount being inserted afterward by the lender. Thus it is possible to give the transaction every appearance of validity. The borrower as a rule is unable to state just what his agreement was or just what papers he signed. The loan is made in currency, thus avoiding any record of the amount of money delivered by the lender. No receipts are given for the payments made by the borrower. When the loan is paid in full no papers are delivered to him, lest he seek to recover what he has paid. In short the borrower is kept as much as possible in the dark concerning the entire transaction from beginning to end. Nothing is gained by saying that the borrower should not be a party to such a transaction. Surely a man versed in business dealings would not do so. But these borrowers are not of that class. Uppermost in their minds is the thought of obtaining the money which they need so badly, and the business side of the deal is left entirely to the lender, who is only too ready to relieve the borrower of the annoyance of such petty details, thereby impressing him with the courteous manner of the lender and the ease with which he can make a loan.

When the borrower delays or defaults in payment, he obtains a decidedly different view of the nature of the lender. The lender has a large assortment of tricks for dealing with the defaulting borrower and he employs them time and again. Frequently a man borrows money without the knowledge of his wife not wishing to trouble her with the knowledge of his embarrassed condition. In fact many loan sharks encourage him to borrow in secret and advertise the fact that here is an opportunity to obtain money without the wife's knowledge. Some borrowers do not need such encouragement. The loan shark knows that the man who borrows in secret fears publicity. In his effort to collect he approaches the borrower with the threat that unless he makes his payments as agreed, his wife will be informed of the loan. The threat proves quite effective. Again the average borrower wishes to conceal from his employer the fact that he has borrowed money. The loan shark is aware of this. He threatens to notify the employer or to levy garnishment of wages. Railroad employees in particular fear garnishment, for the reason that three garnishments will result in discharge from employment. The threat of informing the employer by notice or garnishment is a very effective club in dealing with defaulting borrowers. ,

The law being all in favor of the borrower in these usurious transactions, it is difficult perhaps to understand why the borrower does not assert his legal rights. The answer is that legal rights can be determined only in court, and court means publicity, which the borrower fears. Rarely does the loan shark resort to the courts to enforce his usurious transactions, because his threats accomplish their purpose in most instances. But in those rare cases where suit is brought, the amount involved is insufficient to warrant the expense of a defense on the part of the borrower, and he is unable to bear the cost which he would incur in asserting his rights. If he does assert his rights, the loan shark appears in court well fortified, perhaps with a note valid to all appearances, signed by the borrower, or with a record of payments made. The borrower is without a record or receipt of any kind to show the amount received or payments made, other than those admitted by the lender.

In short the loan shark is able to carry on his business because the borrower enters the transaction in ignorance, is kept in ignorance from beginning to end, and is held to the hard bargain by his own necessitous condition and the threats of the loan shark.

8. That laws such as the general usury law of this State are ineffective in curbing the loan shark evil, because they are arbitrary and unsound in principle in that they do not make proper allowance for the various types of loans, the difference in credit and security possessed by borrowers and the elements of expense involved in the making of loans.

In fairness to the loan shark it must be admitted that these small consumptive loans cannot be made at legal rates without financial loss to the lender. This fact constitutes the loan shark's justification. The general usury law of Minnesota and of all states is unscientific in principle, because it fails to take into consideration several of the basic elements which go to make up a loan charge.

There are elements other than pure interest which comprise the charge made for any loan of money. There are perhaps no cases where a loan charge contains nothing but pure interest. The charge on a loan such as those made to the United States Government, where all risks and other elements are reduced to a minimum, is the nearest approach to a loan charge consisting entirely of pure interest. In such a loan the other elements are relatively negligible. In the case of a large productive loan made to an industrial corporation, where the element of risk is small, the pure interest element in the loan charge is relatively high, but not to the same extent as it is in the case of a loan to the Government. In the case of smaller loans made to individuals upon good security, the elements of the loan charge, other than pure interest, are relatively higher than in the Government loan or large productive loan. In the case of the small consumptive loan, however, the type of loans with which we are concerned in this report, the pure interest element in the loan charge is relatively small and the greater part of the charge consists of elements other than pure interest.

Mention is made of these various elements of a loan charge in the several types of loans because it is only when these are kept clearly in mind that the arbitrary nature of our general usury law is apparent. To express the same thought in more concrete terms, let us consider for a moment a sum of $50,000.00 placed on interest. If this amount is loaned

in one lump sum at eight per cent per annum it will, of course, yield $4,000.00 per year, with little if any expense or effort on the part of the lender. Assume, however, that this same sum of $50,000.00 is the working capital of a small lender, and instead of being loaned in one lump sum or in several large sums, upon good security, it is loaned in sums averaging $50.00 each. If the lender succeeds in keeping this full amount on interest all of the time, which is a practical impossibility, and charges eight per cent interest, he would be receiving $4,000.00 per year in interest. But clearly a great deal of time, effort and expense is involved in attending to one thousand loans of $50.00 each, or even to five hundred loans of $100.00 each. In either case the lender will need a bookkeeper, a stenographer, an investigator and a collector. He himself can serve as office manager. Out of the $4,000.00 income from his $50,000.00 capital he must pay the salaries of these employees, including his own, and must pay his rent, light, telephone, advertising and other incidental expenses of his offiice. Also he must bear any losses which he may sustain by reason of poor loans. Obviously this expense will exceed $4,000.00 and his business will be conducted at a loss, which means that an eight per cent usury law is not such as to permit the conduct of a business of making small loans.

The difficulty lies in the fact that when the rate of interest has from time to time been fixed by usury laws, account has been taken only of those transactions which are generally in the public mind: the ordinary loans by banks and individuals to those who have good security to offer, or who have sufficient property so that they are entitled to credit without security. Apparently no consideration has been given by the framers of these laws to the undeniable fact that a large class of necessitous borrowers cannot obtain a loan at that rate and must therefore borrow at a higher, although illegal rate of interest.

9. That in theory there are four possible methods of dealing with the loan shark evil:

(a) To repeal our general usury law, thereby lessening to some extent the risk assumed by the lender, and leaving the matter of interest rates to unrestricted competition.

(b) To make the eight per cent usury law more effective by prescribing that violation thereof shall constitute a criminal offense, punishable by imprisonment and by rigidly enforcing such a law.

(c) To provide for the making of small loans as a semi-philanthropic, non-commercial enterprise.

(d) To legalize commercial lending of small sums at prescribed rates in excess of the general maximum interest rate, fair both to lender and borrower, with provision for State licensing, inspection and supervision.

10. The first method above suggested, i. e.: The repeal of our general usury law, is impractical and would prove ineffective in operation.

The repeal of our general usury law can scarcely be considered at this time, because whether or not this law is serving any useful purpose public opinion is overwhelmingly in its favor. Economists maintain that these

general usury laws are unavailing in controlling interest rates and they present a strong line of argument in support of this assertion. Be that as it may, our general usury law will doubtless stand for a long time to come and we need not be concerned with the advisability of its repeal, because however little good it may accomplish it does not appear that it is causing any disturbance. We are concerned only with the matter of driving out the loan shark, and the repeal of our general usury law would not accomplish this. Maine, Massachusetts and New Hampshire have no general usury laws, and yet the loan shark flourished in those states until exterminated by effective legislation.

11. The second method above suggested, i. e.: That of attaching a criminal penalty to our general usury law, is inexpedient.

(a) Because a criminal penalty, if not rigidly enforced, provides no remedy, but would rather tend to increase the rate charged by the loan shark, because of the greater risk which he would then assume. The effectiveness of any law depends upon the extent to which it is enforced. The difficulty of enforcing a law making usury a felony is so obvious as to require no argument.

(b) Because if effectively enforced, it would deprive necessitous borrowers of a source of funds to tide them over periods of emergency and thus throw them on charity for relief. Leaving out of consideration the practical impossibility of enforcing such a law, let us assume that it could and would be enforced to the extent of exterminating the loan shark. It would not eliminate the borrowers who have dealt and would deal with him. Their need of money would continue to exist. They would still be unable to borrow at rates within our general usury rate. In dealing with the problem of driving out the loan shark, it must be remmembered that he is filling a place in the economic and social field, however improperly, and that in exterminating him we must also provide a proper substitute, as a source from which necessitous borrowers can obtain the needed funds. It may be well to emphasize in this connection that the problem which confronts us is of a two-fold nature: we must drive out the loan shark, and at the same time we must provide a proper substitute. These two phases are so closely related as to be inseparable. We cannot accomplish the eradication of the loan shark without providing some agency to take his place. Therefore, increasing the penalty for usury, whether enforced or not, offers no solution for this problem.

12. That the third method suggested, i. e.: Lending by semi-philanthropic and non-commercial agencies has been tried and found inadequate.

This proposal has been tested in this State and elsewhere and it has been found, without exception, that the funds provided therby have been insufficient to meet the demand, with the result that the loan shark has continued to thrive. Nearly twenty years ago when the evils of the small loan business were first recognized, an attempt was made to deal with the problem through the medium of "Remedial" or "Provident" loan associations. The Russel Sage Foundation was instrumental in establishing from twenty to thirty such associations in many large cities. These ossocia-

tions were formed for the sole purpose of alleviating the credit conditions of distressed persons who were being compelled to pay exorbitant interest rates on loans. It was the purpose of the founders to eliminate the loan shark by competition, through lending money in small sums at a very much lower rate than was exacted by commercial loan companies. As a rule all of the officers and directors of these associations, except the active manager, served without salary. Regardless of the existence of remedial loan associations, people still went to the professional money lenders. There was nowhere near enough benevolent money to meet the demand, hence the loan shark continued to flourish. The remedial associations did not solve the problem. We have had such associations in Minnesota for a period of about fifteen years, and the fact that the loan shark is still decidedly with us is ample proof of the failure of this method of combating his activity. The experience of other states has been identical.

13. That the fourth method suggested, i. e.: To legalize the lending of small sums of money at prescribed rates in excess of the general maximum interest rate, fair both to lender and borrower, with provision for State licensing, inspection and supervision of the lender, offers the only practical method of exterminating the loan shark.

We have found that there is a legitimate demand for loans in small sums for consumptive purposes. We have further found that loans of this type cannot be made profitably as a business proposition at a rate of eight per cent per annum. In fact the making of loans of this character at that rate can bring only loss to the lender.

Since a genuine and legitimate demand for such loans exists, and since the demand cannot be met at rates within the limits of our general usury law, the only logical and practical solution which can be found is to legalize, upon loans of this type, a rate sufficiently high to attract adequate legitimate capital to meet the demand and yet not so high as to place an undue burden upon the borrower. Nothing is accomplished by theorizing upon the proposition that the poor man, who borrows $50.00 to buy food for his family, should pay no higher rate than is paid by the railway company, which borrows a million dollars to extend its lines. This is a condition which, however desirable it might be, is impossible, because of the basic differences in these two types of loans which have been already noted. While we are thus indulging in sentiment and theory, thousands of our fellow citizens are in the grasp of the loan shark, paying rates of from 120 to 400 per cent and higher. It is this condition which confronts us.

But the legalizing of a higher rate of interest upon loans of this type will not in itself solve the problem. Just as there are loan sharks who violate our eight per cent usury law, there would doubtless be loan sharks who would violate the law if a higher rate were permitted, without adequate safeguards. The position of the necessitous borrower is necessarily weak and he is in need of and entitled to the power of the state to offset the advantage possessed by the lender. Provision must be made that loans of this type, at a higher rate of interest, can be made only by those persons licensed for that purpose by the State, and these licensees must be subject to the careful inspection and supervision by State authority, to insure that

the rights of the borrower be given adequate protection. The details of this State supervision will be discussed later in this report in connection with the proposed bill.

14. That the necessity of allowing upon small loans a rate of interest in excess of the general maximum rate has been recognized in this state and provision therefore made by statute.

The proposal for a higher rate of interest upon small loans is not without legislative recognition and sanction in Minnesota. In the past we have recognized the impossibility of the making of small consumptive loans at a rate within that fixed by our general usury law. By Section 7042 and 7043, General Statutes 1923, we authorized the making of salary and chattel mortgage loans in sums not exceeding $200.00 and provided that the lender might charge therefore a rate of one per cent per month, with a fee in addition thereto, according to a graduated scale of fees, set forth in that Act. Again by Chapter 206 Laws of 1925, providing for the organization of credit unions, we have recognized the need of a higher rate of interest than that permitted by the general usury law, and have authorized a charge of one per cent per month, on loans made by such associations.

Under this latter Act about twenty-five associations or unions have been formed in a period of about three years. These are capable of rendering a valuable service to their members within their limited field of operation. Credit union organization is limited, and necessarily so, to groups having a common bond of occupation or association, or to groups within a well defined rural district. They are able to make loans at a rate of one per cent per month only because their field is limited in this manner, and also because of the fact that their officers and directors serve without pay. In Minnesota the law specifically provides that the directors and committee members shall not be compensated. The fact that the loan shark has continued to flourish during the fifteen years since our first statue allowing a higher rate was enacted, is ample proof that the provisions of that law are insufficient to solve the problem. Furthermore, a credit union, while contributing toward this end, is not adequate in itself, for the reason that its field of activity is and always must be limited. Neither of these laws is sufficient to drive out the loan shark, nor can both together accomplish that end.

15. That a rate of three and one half per cent per month on upaid balances to cover interest and expenses, with no fees in addition thereto, on loans of $300.00 or less, offers the only practicable solution of this problem.

Since the principle of authorizing a higher rate of interest on small loans has already been recognized in this State, we may now view the problem in a businesslike way, free from sentiment and prejudice against the making of any discrimination in rates between different types of loans and different classes of borrowers. We are justified in believing that a rate should be auuthorized upon loans which will be sufficient to attract adequate capital to meet the needs of these borrowers, and yet a rate which will be fair to the borrower. How can we determine such a rate?

A number of years ago the Russell Sage Foundation, an endowed philanthropy of New York City for improvement of social and living conditions, began to study this matter of lending money to needy borrowers, with a view to putting it on a scientific basis and correcting the existing abuses. This organization made careful investigation of the small loan business in all its varieties and in all parts of the United States. It discovered a great many fundamental facts in regard to the making of consumptive loans. Upon the basis of these findings a Uniform Small Loan was prepared and recommended to the legislatures of the various states. With only slight variations, the law has been adopted in Maine, Connecticut, Rode Island, Pennsylvania, Maryland, Virginia, Georgia, Illinois, Indiana, Iowa, Arizona, West Virginia, Florida, Missouri, Wisconsin and Louisiana. Furthermore, the following states operate under laws which are the same in principle as the Uniform Law, with slightly different rates of interest: New Hampshire, Massachusetts, New Jersey, Ohio, Michigan, Utah, Oregon and Tennessee.

The chief feature of this law is that it fixes a special maximum of three and one half per cent per month on unpaid balances for this type of loan, the amount of the loan being limited to sums of $300.00 or less. The Foundation discovered that the cost and risk of the business were so high that such a rate would have to be legalized, not only to get lenders to go into the business, but also to get legitimate capital to go in it at all. It is true that in few instances these laws limit the rate of interest to three per cent per month, usually however, with a small fee in addition. During the early stages of the studies made by the Foundation it was thought that three per cent per month was a reasonable maximum limit for such loans, but as more figures were obtained later, it was found that three and one half per cent per month, with all fees eliminated, was a better basis.

The rate of three and one-half per cent per month on unpaid balances is sufficiently high to allow a fair and reasonable return, which will attract adequate capital to meet the demands. Concerns which have large capital and efficient organization may make more at this rate than would strike the average man as proper. A small lender will have to struggle to make a living at this rate. The highest net earnings which we have found to be made by any lender are seventeen or eighteen per cent per annum, this being exceptionally high, and from this we go down the scale until we find lenders forced out of business because of their inability to make a profit at that rate. It is perhaps fair to say that the average net earnings of the lenders, operating under such laws, is about ten per cent per annum. The struggling small lender with limited capital, is no more an argument for increasing the rate than the success of the large and well organized lender is an argument for reducing the rate.

It is conceivable that the time may come when efficient organization and competition for the better class of small loans may result in a reduction of the rates charged by at least some of the lenders. Thus far, however, we have learned of no instance in which this has been done.

This is indicated by the fact that within the last few months one large company engaged in the making of small loans has voluntarily reduced its rate. Whether it will be able to conduct its business at the lower rate is uncertain, but the experiment is significant.

To judge the fairness to the borrower of this rate of interest it must be remembered that the borrowers who will pay this rate are those who are unable to borrow at more favorable rates. It is not the man who can borrow

at six per cent or eight per cent per annum who will pay three and one-half per cent per month. It is the borrower who is now forced to deal with the loan shark and pay from 120 to 400 per cent per annum who will borrow from the licensed lender at three and one-half per cent per month. Furthermore, it must be remembered that no interest is collected in advance. That these small loans are repaid in regular installments and interest is always computed on the unpaid balance. It is usual for those not acquainted with the small loan business to assume that because the interest rate charged is three and one-half per cent per month, the borrower must pay to the lender forty-two per cent of the amount borrowed in addition to the principal. It does not work out this way in practice. If a loan of $60.00 is repaid in six equal monthly installments, the amount of interest paid is $7.35 or 12.25 per cent of the principal. If a loan of $100.00 is repaid in twelve equal monthly installments, the total amount of interest paid is $22.75, or 22.75 per cent of the principal. It is submitted that these charges will bear comparison with the cases cited by the Minneapolis Legal Aid Society, of charges made by loan sharks, where for example, $20.00 interest was paid on a loan of $55.00 for a period of six months, this being a charge of twenty-one per cent per month, as compared with the proposed charge of three and one-half per cent per month.

The uniform law fixes a maximum limit of $300.00 for loans on which this rate may be charged. Obviously, some limit as to the amount of the loan must be fixed. It has been found that $300.00 is a limit sufficiently high so as to take care of the needs of the class of borrowers affected. It is argued by some that the maximum should be lower. Fifteen years ago we enacted a law allowing an extra rate of loans of $200.00 or less. Taking into consideration the increased cost of living at this time, it would not seem that a limit of $300.00 is disproportionate. It is perhaps true that on a loan of $250.00 or $300.00 this rate may allow more than a necessary return to the lender. It is no less true that this rate does not allow an adequate return to the lender on loans of $50.00 or less. Suggestions for a sliding scale providing for a higher rate of interest on the smaller loans and a gradually decreasing rate as the amount of the loan increases, have been considered and found inadvisable for at least two reasons. In the first place, a sliding scale of rates renders inspection and supervision of the business difficult, if not impossible. Secondly, such an arrangement is an invitation to the lender to split the loans in order to avail himself of the higher rate allowed on the smaller loans. It appears that the only practicable method is to fix one rate of interest for all loans within the amount on which this extra rate is to be permitted.

16. In addition to the authorization of this higher rate upon loans of this type, adequate provision must be made for state supervision of the business and adequate penalties must be provided to make the enforcement of this law effective.

We would certainly fail to accomplish our purpose if we were to confine ourselves to enacting a law which would authorize a rate of three and one-half per cent per month. It has been suggested in an earlier finding that adequate safeguards must be provided to protect the borrower under the three and one-half per cent law. Chief among these safeguards are the following:

(a) The right to loan money at rates of three and one-half per cent per month must be limited to those who have obtained licenses for that purpose

from the state. The limiting of such rates to licensees is necessary to enable the state to inspect and supervise the conduct of such business. If all were permitted to lend at that rate, it would be impossible to ascertain who was engaged in the business and therefore impossible to inspect and supervise the same. Furthermore, the officer charged with administering the law must be authorized to revoke the license of any lender. This provision is obviously necessary in order that the officer may be able to discipline the licensee.

(b) The licensee should be required to furnish a satisfactory bond in sufficient amount to insure his financial responsibility and to protect any borrower who may have a cause of action against him as such.

(c) The commissioner should be authorized to make examination of the loans and business of every licensee and of every person by whom such a loan shall be made as licensee or otherwise. He should be required to make such examination at least annually. To facilitate this work, licensees should be required to keep such books and records of their business as may be prescribed by the commissioner. This provision for examination of the lender's business is one of great importance. We have seen that the borrower is in need of and is entitled to the power of the state to offset the bargaining advantage possessed by the lender. If the state is to confine its activity to the issuing of licenses, then it is left to the borrower to protect himself and obviously he is unable to do this. The state, therefore, should keep careful watch of the activities of the lenders to determine whether or not they are complying with the law in all respects, and to compel obedience whenever violations are discovered.

(d) The law should carry a criminal penalty for any person who engages in this business without a license or for any licensee who in any manner charges a rate exceeding the limit prescribed by law. While a criminal penalty would be of little effect without state supervision, it has been found that with state supervision the criminal penalty is very effective, because of the fact that the lender knows that prosecution of any violation of the law will not be left to the borrower, who is unlikely to prosecute, but will be in the hands of the commissioner, whose duty it is to see that the law is complied with and who will prosecute violators of the law.

(e) There are a number of restrictive provisions which should be incorporated in such a law and which are explained hereafter in connection with each section of the proposed law, where they can be more readily understood.

17. That the enactment of legislation allowing a charge of three and one-half per cent per month, with proper safeguards to the borrower, has brought legitimate capital to the small loan business and has elevated this business to a plane of decency and respectability where it properly belongs.

The business of a loan shark is undeniably a bootleg business, because, operating outside of the law, decent legitimate capital will not enter this field. Yet here is a field where the demand for money is as genuine and legitimate as the demand in any other field. The demand is being met only by those who are willing to defy the law and exact an exorbitant profit for so doing.

The demand for small consumptive loans should be supplied by legitimate capital. Legitimate capital will enter this field if proper provision is made by law.

This is not a matter of compromising with evil. The small loan business is not wrong in itself. It is wrong only in the manner and to the extent in

which it is carried on by the loan shark. Our existing law has made it possible to carry on the business in this manner at great profit to the lender and has made it impossible for legitimate capital to enter and engage in this business.

States which have enacted legislation along the lines recommended have found that it has resulted in the extermination of the loan shark and the entry of legitimate capital into this small loan field. Under the operation of these laws, the small loan business has come into the open. The offices look much like small banks. Corporations to do small loan business are now organized. While previously the goal was to make a fortune through the sharpest methods conceivable, the aim of the new type of man engaged in the business is to make a profit by financial service and at reasonable cost to the borrower.

The lenders have formed national and state organizations that hold public conventions, which are addressed by prominent men. Various phases of the business are discussed openly in these meetings and the public has an opportunity to acquaint itself with its nature. Everywhere state officials charged with the administration of this law testify that the lenders' organizations are the greatest factor in policing the business. They refuse to tolerate improper practices of licensees and others, and give invaluable assistance to these officers in the enforcement of the law in all its phases. As Dr. Lewis N. Robinson of Swarthmore College, a man who has made an exhaustive study of small loans, declares, "The making of small loans was always a necessary business, but because it had no proper legal setting, it was carried on outside the law. The Uniform Law has made it a legal business and by bringing it into the open, has raised its standards with its status."

18. That while it is probably true that the average loan of the licensed lender is larger than the average loan of the loan shark, this does not indicate that the licensed lender will not make the small loans.

The charge is sometimes made that the licensed lender will not make small loans of $10.00, $15.00 or $20.00 because they cannot be made profitably. Those making this assertion attempt to prove it by pointing out that the average loan made by the licensee is considerably higher than the average loan made by the loan shark. Authentic figures as to the average amount of the loans made by the loan shark are not available because of the cover under which this business is necessarily conducted. But it is doubtless true that the average loan of the licensee is higher than that of the loan shark. It does not follow from this that the licensed lender will not make small loans. There are a number of reasons which account for the higher average loan of the licensee.

In the first place, the loan shark, being an outlaw, does not dare make the larger loans of $200.00 or $300.00. He has no standing before the law and if he makes one of these larger loans, the borrower may find it to his advantage to contest payment in court, rather than yield to the demands and threats of the loan shark. This is not true of the smaller loans, and the loan shark feels that he should confine himself to comparatively safe ground. Therefore he limits himself to the smaller loans, which can be repaid for less than the cost and trouble of contesting payment in court.

Secondly, under the three and one-half per cent rate, borrowers know that they can borrow more at less cost. Frequently a borrower who actually needs $100.00 and who could borrow $100.00 from a licensed lender at three and one-

half per cent, will not be considered by a loan shark for more than $50.00, or if he could get more than that he does not feel that he can afford it at the high rate which the loan shark demands.

Thirdly, since the loan shark will not make a large loan, the borrower frequently finds it necessary to make two or more loans, and thereby deals with several loan sharks at the same time. There is evidence of collusion between loan sharks, whereby when one lender has made as large a loan or as many loans to one borrower as he desires to make, he will send the borrower to another loan shark for an additional loan. Thus, in the Minneapolis newspaper drive against loan sharks, seven hundred borrowers were found who had 1338 loans, an average of about two loans each. One borrower had seven loans, aggregating $120.00; another had six loans, aggregating $105.00. Obviously splitting $120.00 into seven loans of less than $20.00 each, will maintain a low average. But does a low average maintained by the splitting of loans, as compared with the higher average loan of the licensed lender, indicate that the licensed lender will not make the smaller loans?

The answer to this charge is that the records of the licensed lenders indicate that they will and do make the smaller loans. They readily admit that they cannot make a profit on the smaller loans and that some of them are made at a loss in that they do not bear their proportionate share of the expense of the business. However, the lenders justify the making of these smaller loans upon the theory that in proper cases they regard it as a matter of duty, and further that they regard it as a matter of good business practice. They regard it as a matter of duty in that they feel that since they are licensed by the state to make loans to necessitous borrowers, they should not hesitate to make a proper loan solely because the amount is so small that no profit is involved. They regard it as a matter of good business practice, upon the theory that by refusing to make a small loan they incur the displeasure of the prospective borrower, whereas, by making the loan they secure his good will and at some future time, he or some relative or friend may be in need of a loan of sufficient size to bring profit to the lender. There is nothing unusual in this view which the lender takes of making the smaller loans, even though without profit. As a parallel, it might be suggested that lawyers frequently perform services for needy clients, either because of what they regard as their duty as officers of the court, or because of the good will which such service brings to them with possible future business of a profitable nature. And so it is with the licensed lender.

19. That the legalization of a rate of three and one-half per cent per month on loans of $300.00 or less does not interfere with or jeopardize the borrower who now is capable of obtaining a loan at a bank or elsewhere at banking rates of interest.

It has been urged that the legalization of a rate of three and one-half per cent per month on small loans will force certain borrowers, who now can borrow at banking rates, to pay the higher rate. The argument appears absurd on its face, because the borrower, whose credit and security is sufficient to enable him to obtain a loan at eight per cent per annum or less, could obtain a loan at that rate from the same source even if licensed lenders were authorized to charge the higher rate. However absurd the argument may appear, it has been urged with such apparent sincerity as to warrant consideration.

The proponents of this view argue that the farmer who now borrows at a bank at eight per cent per annum or less, will be victimized by the lender and forced to pay three and one-half per cent per month. It must be remembered in this connection that only licensed lenders are to be permitted to charge this higher rate. It must also be kept in mind that any person, co-partnership or member thereof, or corporation or officer or director thereof, doing business under any law of this state or of the United States relating to banks, trust companies and building and loan associations, is specifically excluded from the provisions of this Act. In short, these persons cannot secure a license and therefore cannot charge a rate of three and one-half per cent per month on small loans.

The Uniform Law excepts any person, co-partnership or corporation, doing business under any law of this state or of the United States, relating to banks, trust companies or building and loan associations. It has been urged, however, that while a bank or trust company, as such, could not become a licensee, the officers and directors would circumvent the spirit of the law by obtaining a license in the name of an individual officer. Officials administering these laws in other states testify that they know of no case in which this has been done. To those acquainted with the dependence of the small town banker upon favorable public opinion, and the condemnation which would be the lot of one who placed himself in this position, the argument is of little force. Bankers could not afford to become licensees and force the farmers, whose credit is sufficient for a bank loan, to pay the higher rate. But to make assurance doubly sure, the committee in the recommended bill has amended the Uniform Law by excepting not only banks, trust companies and building and loan associations, but also the officers and directors thereof. It is difficult to see how, with this restriction, a bank could engage directly or indirectly as a licensee, and it is likewise difficult to see how the farmer, or anyone else who has sufficient credit to borrow at a bank, could be forced or induced to borrow money at the higher rate from a licensee.

We find that in other agricultural states farmers are sometimes found among those borrowing from the licensed lenders. However, state officials testify that these farmers are in most instances found to be tenant farmers, who never could borrow at a bank, but who are now availing themselves of the opportunity to make a start by borrowing from the licensed lenders. No farmer, tenant or otherwise, who has the security which a bank will recognize, finds it necessary to pay the higher rate in order to obtain money.

Few would deny the friendship of Ex-Governor Frank O. Lowden toward the cause of the farmer. Governor Lowden states, with reference to the small loan law, "The problem is not a rural one. I do not know of any instance where the privileges given by the law are being abused by bankers in either the large or small cities. I know of no instance in which licensees under this law have had any transactions with farmers." This statement was made after the law had been upon the statute books of Illinois for a period of ten years.

20. That legislation of the character embodied in the uniform law has received the approval and endorsement everywhere of organizations and individuals who have given the matter consideration.

Opposition to this legislation comes from two groups of people: From the uninformed, who do not understand why more than the maximum rate fixed by the general usury law should be charged on small loans; and from the

interested, who do not want their illegitimate business, in which they charge from ten per cent per month and up, to be affected. It is easy to understand and excuse the uninformed; it is likewise easy to understand the interested.

However, those who have become informed on the small loan problem and who have studied the operation and effects of this law and who have no personal interest in the matter, have given this legislation their sanction and endorsement. The Minnesota State Conference of Social Work, composed of more than sixty charitable and welfare organizations, has approved this legislation, and many of these organizations have given it their separate, individual endorsement. The Legal Aid Society of Minneapolis, which, because of the nature of its work, is particularly well informed on the small loan question, has not only endorsed the Uniform Law, but has been active in urging its passage.

The Baltimore Legal Aid Bureau, the Cincinnati Legal Aid Society, the Cleveland Associated Charities, the Cleveland Legal Aid Society, the Grand Rapids Legal Aid Bureau, the Milwaukee Legal Aid Society, are among those of other states giving their approval. Irene V. McCormick of the Chicago Legal Aid Bureau, S. E. Foster of the Indianapolis Charities; Romain Hassrick, of the Philadelphia Legal Aid Society, appeared before the committee and expressed their unqualified approval of these laws.

State officials who administer these laws endorse them in the highest terms, and testify to the benefits which they have brought to the class of borrowers affected, the generally high type of lenders engaged in the business, and the great improvement effected in the business of making small loans. Among those appearing before the committee and endorsing the law were: Mrs. E. Pearl Warwick, Small Loan Examiner, Department of Trade and Commerce of Illinois; Elmer Johnson, Supervisor, Industrial Loan Department of Indiana; George H. Orth, Bureau of Private Banks and Peter G. Cameron, Secretary of Banking, of Pennsylvania; J. F. Hammond, Deputy Commissioner, Bureau of Banking of New Jersey; L. E. Shippee, Deputy Commissioner, Banking Department of Connecticut; Earle E. Davidson, Supervisor of Small Loan Agencies of Massachusetts.

Perhaps it may be granted that William Green, President of the American Federation of Labor, is as well informed and sympathetic a friend of the wage earner as may be found. He endorses the small loan law of Ohio in these terms: "This law has operated to the great advantage of the mass of people, those who have been compelled to borrow in small sums, and who have been required to pay very large interest charges. The Lloyd Act marks a great step forward in this character of legislation. Public sentiment in Ohio will not permit it to be weakened or repealed."

These endorsements are typical of the views of those who have studied the small loan problem and who have had opportunity to observe the operation of these laws.

IV.

RECOMMENDATIONS

Upon the foregoing findings the committee submits the following recommendations:

1. That the extension of credit unions as authorized by Chapter 206, Laws of 1925 should be encouraged.

As hereinbefore stated, the committee finds that credit unions are capable of rendering valuable assistance in the small loan field. Adequate provision for the organization of such unions having been made by statute, there is no further legislation which we can recommend along this line. Our existing credit union law has the approval and endorsement of the committee.

Some progress in the development of credit unions has been made in Minnesota. In the three years since the enactment of the statute about thirty-eight such organizations have been formed. Doubtless many more will be formed, and this movement should be encouraged in every possible manner. Groups eligible under the law should be fully advised as to the manner of organization and the conduct of the business. The Russell Sage Foundation has made an extensive study of credit unions and is prepared to give full information regarding their establishment and operation.

The credit union being a co-operative, rather than a commercial enterprise, and the overhead expense being relatively small, these organizations are able to lend money to members at a rate of one per cent per month. Certainly a man who can obtain a loan at that rate should not pay three and one-half per cent per month. However extensive may be the development of the credit union idea, there will always be borrowers who cannot or will not become members of any credit union. For this class the only source of borrowing will be the commercial agency, with its higher rate. But the credit union can take care of many who would otherwise find it necessary to pay the higher rate necessarily charged by the commercial lender.

In just what manner the development of credit unions can be furthered in this state the committee is not at this time prepared to say. However, it is our opinion that welfare organizations can accomplish a great deal of good by obtaining and disseminating such information among those groups which are eligible under the law to form credit unions. Perhaps also provision can be made whereby the state will likewise assist in furthering the establishment of credit unions by giving publicity to the possibilities of this form of organization.

2. That the bill hereinafter set forth, being the uniform small loan law with slight modifications, be enacted by the legislature of the State of Minnesota:

A BILL

For an Act to license and regulate the business of making loans in the amount or of the value of $300.00 or less, secured or unsecured, at a greater rate of interest than eight percentum per annum, prescribing the rate of interest and charge therefor and penalties for the violation thereof and regulating the assignment of wages or salaries earned or to be earned when given as security for any such loan or as consideration for a payment of $300.00 or less, and to repeal Sections 7042 and 7043, General Statutes 1923, and all Acts and parts of Acts inconsistent with the provisions of this Act.

Be It Enacted by the Legislature of the State of Minnesota:

Section 1. License. That no person, co-partnership or corporation shall engage in the business of making loans of money, credit or things in action in the amount or of the value of $300.00 or less and charge, contract for or receive a greater rate of interest than eight percentum per annum therefor,

except as authorized by this Act and without first obtaining a license from the Commissioner of Banks, hereinafter called the Commissioner.

Section 2. Application and Fee. Application for such license shall be in writing and shall contain the full name and address, both of the residence and place of business of the applicant, and if the applicant is a co-partnership of every member thereof, or if a corporation of each officer and director thereof, also the county and municipality, with street and number, if any, where the business is to be conducted, and such further information as the Commissioner may require. Such applicant at the time of making such application shall pay to the Commissioner the sum of $100.00 as an annual license fee and in full payment of all expenses for examinations under and for administration of this Act, provided that if the license is issued for a period of less than twelve months the license fee shall be pro rated according to the number of months that said license shall run.

All license fees received by the Commissioner shall be paid into the State Treasury and shall be credited to the funds, otherwise appropriated for the maintenance of the Banking Division of the Department of Commerce, and may be used for the employment of such additional assistants as the Commissioner may deem necessary for the administration of the provisions of this Act by said Division.

Section 3. Bond. The applicant shall also at the same time file with the Commissioner a bond in which the applicant shall be the obligor in the sum of $1,000.00, with one or more sureties whose liability as sureties shall not exceed the sum of $1,000.00 in the aggregate, to be approved by the Commissioner, and said bond shall run to the State of Minnesota, for the use of the State and of any person or persons who may have a cause of action against the obligor of said bond, under the provisions of this Act. Such bond shall be conditioned that said obligor will conform to and abide by each and every provision of this Act and will pay to the State and to any such person or persons any and all monies that may become due or owing to the State or to such person or persons from said obligor under and by virtue of the provisions of this Act.

Section 4. License to Issue. Upon the filing of such application and the approval of said bond and the payment of said fee, the licensing official shall issue a license to the applicant to make loans in accordance with provisions of this Act for a period which shall expire the first day of January next following the date of its issuance. Such license shall not be assignable.

Section 5. Additional Bond. If in the opinion of the Commissioner the bond shall at any time appear to be insecure or exhausted or otherwise doubtful, an additional bond in the sum of not more than $1,000.00, satisfactory to the Commissioner, shall be filed within ten days after notice to the licensee, and upon failure of the obligor to file such additional bond, the license shall be revoked by the Commissioner.

Section 6. Revoking License. The Commissioner may upon notice to the licensee and reasonable opportunity to be heard revoke such license if the licensee has violated any provision of this Act, and in case the licensee shall be convicted by a court a second time for the violation of Section 13 of this Act,

the Commissioner shall revoke such license, provided that the second offense shall have occurred after a prior conviction, and thereafter no license shall be issued to such licensee nor to the husband or wife of the licensee, nor to any co-partnership of which he is a member, nor to any corporation of which he is an officer or director.

Section 7. Posting. The license shall be kept conspicuously posted in the place of business of the licensee.

Section 8. No person, co-partnership or corporation so licensed shall make any loan provided for by this Act under any other name or at any other place of business than that named in the license. Not more than one place of business shall be maintained under the same license, but the Commissioner shall issue more than one license to the same licensee upon the payment of an additional license fee and the filing of an additional bond for such license.

Section 9. Whenever the licensee shall change his place of business he shall at once give written notice thereof to the Commissioner, who shall attach to the license his approval in writing of the change.

Section 10. Examinations. The Commissioner for the purpose of discovering violations of this Act, may either personally or by any person designated by him, at any time or as often as hemay desire, but at least once each year, investigate the loans and business of every licensee and of every person, co-partnership and corporation by whom or by which any such loan shall be made, whether such person, co-partnership or corporation shall act or claim to act as principal, agent or broker thereunder, or without the authority of this Act; and for that purpose he shall have free access to the office or place of business, books, papers, records, safes and vaults of all such persons, co-partnerships and corporations. He shall also have authority to examine under oath, all persons whomsoever, whose testimony he may require relative to such loans or business.

Section 11. Books and Records. The licensee shall keep such books and records in his place of business as in the opinion of the Commissioner will enable him to determine whether the provisions of this Act are being observed. Every such licensee shall preserve the records of final entry used in such business, including cards used in the card system, if any, for a period of at least three years after the making of any loan recorded therein.

Section 12. Misleading Advertising. No licensee or other person, co-partnership or corporation shall print, publish or distribute or cause to be printed, published or distributed in any manner whatsoever, any written or printed statement with regard to the rates, terms or conditions for the lending of any credit, consideration or things in action, in amounts of $300.00 or less, which is false or calculated to deceive.

Section 13. Rate of Interest. Every co-partnership and corporation licensed hereunder may loan any sum of money, not exceeding in amount the sum of $300.00, and may charge, contract for and receive thereon as interest and expenses a rate not to exceed three and one-half percentum per month. Interest shall not be payable in advance or compounded and shall be computed on unpaid balances. In addition to the interest herein provided for no

further or other charge or amount whatsoever for any examination, service, brokerage commission or other thing or otherwise shall be directly or indirectly charged, contracted for or received, except the lawful fees, if any, actually and necessarily paid out by the licensee to any public officer for filing or recording or releasing in any public office any instrument securing the loan, which fees may be collected when the loan is made or at any time thereafter.

Section 14. Requirements on Making and Payment of Loans. Every licensee shall:

Deliver to the borrower, at the time a loan is made, a statement in the English language, showing in clear and distinct terms the amount and date of the loan and of its maturity, the nature of the security, if any, for the loan, and the name and address of the borrower and of the licensee and the rate of interest charged. Upon such statement there shall be printed in English a copy of Section 13 of this Act;

Give to the borrower a plain and complete receipt for all payments made on account of any such loan at the time such payments are made;

Permit payment of the loan in whole or in part prior to its maturity, with interest on such payment to the date thereof;

Upon repayment of the loan in full, mark indelibly every paper signed by the borrower with the word "Paid" or "Cancelled", and release any mortgage, restore any pledge, cancel and return any note and cancel and return any assignment given by the borrower as security.

Section 15. No Confessions, Powers, Etc. No licensee shall take any confession of judgment or any power of attorney, nor shall he take any note, promise to pay or security that does not state the actual amount of the loan, the time for which it is made, and the rate of interest charged, nor any instrument in which blanks are left to be filled in after execution.

Section 16. Wage Assignments. The payment of $300.00 or less in money, credit, goods or things in action, as consideration for any sale, assignment or order for the payment of wages, salary, commission or other compensation for services, whether earned or to be earned, shall be deemed a loan within the provisions of this Act, secured by such assignment; and the amount by which such assigned compensation exceeds such payment shall be deemed interest upon such loan from the date of such payment to the date such compensation is payable. Such loan and such assignment shall be governed by and subject to the provisions of this Act.

Section 17. Validity and Payment of Wage Assignments. No assignment or order for payment of any salary, wages, commissions or other compensation for services earned or to be earned, given to secure any such loan, shall be valid unless the amount of such loan is paid to the borrower simultaneously with its execution; nor shall any such assignment or order or any chattel mortgage or other lien on household furniture then in the possession and use of the borrower, be valid unless it be in writing, signed in person by the borrower; nor if the borrower is married unless it is signed in person by both husband and wife; provided that written assent of a spouse shall not be required when husband and wife have been living separate and apart for a period of at least five months prior to such assignment, order, mortgage or lien.

Under any such assignment or order for the payment of future salary, wages, commissions or other compensations for services given for security for a loan made under this Act, a sum equal to ten percentum of the borrower's salary, wages, commissions or other compensation for services shall be collect-

able from the employer of the borrower by the licensee at the time of each payment of salary, wages, commissions or other compensation for services from the time that a copy of such assignment, verified by the oath of the licensee or his agent, together with a similarly verified statement of the amount unpaid upon such loan, is served upon the employer.

Provided, that no such assignment of or order for the payment of any salary, wages, commissions or other compensation for services earned or to be earned shall be enforceable during such time as payments are being made by the employer upon a prior assignment or order made by such borrower to the same or to another licensee.

Section 18. Prohibitions. No person, co-partnership or corporation, except as authorized by this Act, shall directly or indirectly charge, contract for or receive any interest or consideration greater than eight percentum per annum upon the loan, use or forbearance of money, goods or things in action, or upon the loan, use or sale or credit of the amount or value of $300.00 or less.

The foregoing prohibition shall apply to any person who as security for any such loan, use or forbearance of money, goods or things in action or for such loan, use or sale or credit, makes a pretended purchase of property from any person and permits the owner or pledgor to retain the possession thereof, or who by any devise or pretense of charging for his services, or otherwise, seeks to obtain a greater compensation than is authorized by this Act.

No loan of the amount or of the value of $300.00 or less, for which a greater rate of interest or charge than is allowed by this Act, has been contracted for or received, wherever made, shall be enforced in this State, and every person in anywise participating therein in this State shall be subject to the provisions of this Act.

Section 19. Any person, co-partnership or corporation and the several officers and employees thereof, who shall violate any of the provisions of Sections 1, 8, 12, 13 or 18 of this Act, shall be guilty of a gross misdemeanor, and upon conviction thereof shall be punished by a fine of not more than $500.00, or by imprisonment for not more than six months, or by both such fine and imprisonment, in the discretion of the court.

Section 20. This Act shall not apply to any person, co-partnership or member thereof, or corporation or officer or director thereof, doing business under any law of this State or of the United States, relating to banks, trust companies and building and loan associations, or licensed pawnbrokers.

Section 21. The enforcement of this Act shall be entrusted to the Commissioner of Banks, and he is hereby authorized and empowered to make the rules and regulations necessary, in his judgment, for the conduct of such business and the enforcement of this Act, in addition hereto and not inconsistent herewith.

Section 22. Sections 7042 and 7043, General Statutes 1923, and all acts and parts in or for as the same may be inconsistent with the provisions of this Act, are hereby repealed.

Sections 23. This Act shall take effect and be in force from and after June 1, 1929.

V.

EXPLANATION OF BILL

Section 1. The purpose and effect of this section is to prohibit the charging of a rate of interest in excess of eight per cent on loans of $300.00 or less by any person except those licensed therefor by the Commissioner of Banks.

Section 2. This section provides the procedure by which application shall be made for such license and prescribes the license fee of $100.00.

Section 3. This section provides for a bond of $1,000.00 to be furnished by each licensee, the purpose of the bond being to insure the financial responsibility of the lender in order that a borrower may be able to recover any damages sustained by reason of any transaction with such lender.

Section 4. This section provides for the issuance of the license upon compliance by the applicant of the foregoing provisions. It also provides for the term during which the license shall operate and prohibits its assignment.

Section 5. This section authorizes the Commissioner to require an additional bond whenever he deems the existing bond insecure, exhausted or otherwise doubtful.

Section 6. This section authorizes the Commissioner to revoke the license for any violation of this Act and requires that he revoke the license of any lender who shall be twice convicted for charging interest in excess of three and one-half per cent per month, provided that the second offense shall have occurred after a prior conviction. It further provides that no license shall be issued to such licensee nor to the husband or wife of such licensee, nor to any co-partnership of which he is a member, nor to any corporation of which he is an officer or director.

Section 7. This section is self-explanatory.

Section 8. The purpose of this section is to prevent evasion of the law by compelling licensees to do business only in the name under which the license is issued.

Section 9. The purpose of this section is to enable the Commissioner to locate all licensed lenders without difficulty.

Section 10. This section authorizes the Commissioner to make examinations at any time, and requires him to make such examinations at least once each year.

Section 11. This section authorizes the Commissioner to prescribe the books and records to be kept by each licensee. This is for the purpose of simplifying the making of examinations.

Section 12. The purpose of this section is clear and requires no further explanation.

Section 13. This section authorizes licensees to charge a rate of three and one-half per cent per month on loans of $300.00 or less. It prohibits the charging of interest in advance or the compounding of interest, and provides that interest shall be computed on unpaid balances only. It further prohibits the charging of any fee except the lawful fees paid to any public officer for filing, recording or releasing any instrument securing a loan.

Section 14. This section requires the licensee to deliver to the borrower a statement of the terms, the amount, the date of the loan and of its maturity, the nature of the security for the loan, the name and address of the borrower and of the lender, and the rate of interest charged. It further requires that the lender give the borrower a receipt for all payments made on any loan, and that he permit the payment of the loan in whole or in part at any time before its maturity, with interest to the date of such payment. It requires that upon payment of the loan in full the lender shall deliver to the borrower every paper signed by the borrower, marked "Paid" or "Cancelled," and that he release any mortgage and restore any pledge of property given as security for the loan.

Section 15. This section prohibits the licensee from taking any confession of judgment or any power of attorney, and requires that any note, promise to pay or security shall state the actual amount of the loan, the time for which it is made, and the rate of interest charged, and that no blanks shall be left to be filled after execution.

Section 16. This section defines what shall constitute an assignment of wages. It is directed at the so-called salary buyers. The devise employed by the salary buyers has been developed for the purpose of evading the small loan law. They have claimed that they are not makers of loans, but buyers of salaries or wages, and therefore not subject to the provisions of this law. This section therefore specifies that such transactions shall be deemed loans within the provisions of this Act, and shall be governed by and subject to the provisions of this Act.

Section 17. This section covers a number of matters in connection with the security given for any such loans. It provides that no assignment or order for the payment of salary or wages given to secure any such loan, shall be valid, unless the loan is made to the borrower at the same time that such assignment or order is executed. It provides that no assignment or order for the payment of salary or wages, nor any chattel mortgage or other lien on household furniture in possession of the borrower, shall be valid unless made in writing, signed by the borrower, and if the borrower is married, such assignment, order, mortgage or lien must be signed by both husband and wife. It

further provides that under such assignment or order for the payment of wages or salary, a sum equal to ten per cent of the borrower's salary or wages shall be collectable from the employer by the lender, at the time of each payment of salary or wages. The purpose of this provision is to avoid any undue hardship on the borrower by having a larger part of his pay check taken at any time. The last paragraph of this section does not appear in the Uniform Law. This paragraph has been added by the committee in order to avoid the possibility of an employer's making payments upon several assignments at one time. This provides that payments shall be made on only one assignment at a time, thereby limiting the amount which can be deducted from any pay check to ten per cent of the amount of that check.

Section 18. This section prohibits any person, co-partnership or corporation other than licensees from charging, directly or indirectly, more than eight per cent per annum on loans of $300.00 or less.

Secton 19. This section prescribes a criminal penalty for the violation of certain sections of this Act, and makes a violation of those sections a gross misdemeanor punishable by a fine of not more than $500.00 or by imprisonment for not more than six months, or both.

Section 20. The purpose of this section is to prevent any bank, trust company or building and loan association from engaging in business as a licensee, either directly or through its individual members, officers or directors.

Section 21. This section charges the Commissioner of Banks with the enforcement of this Act. It further authorizes him to make rules and regulations which in his judgment, are necessary for the conduct of such business and the enforcement of this Act. This section does not appear in the Uniform Law. It has been taken from the New Jersey Small Loan Law. The Commissioner of that state has found it very helpful in dealing with situations which arise and which could not be foreseen and provided for by specific provisions in the Act itself.

Section 22. This section repeals our present salary and chattel mortgage loan statute. It also provides for the repeal of all acts and parts of acts inconsistent with the provisions of this Act. This latter provision is intended to repeal our present law as to assignment of wages earned or to be earned insofar as the same may be inconsistent with the provisions of this Act regarding assignment of wages.

Respectfully submitted,

MABETH H. PAIGE, Chairman.
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