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The Beginning of the End: The Demise of Bank Partnerships with Payday Lenders

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The Beginning of the End: The Demise of Bank Partnerships with Payday Lenders

When banks eliminated profit-draining services in the 1980s, millions of low-income households were left with little access to financial services. Consumers seeking short-term loans for small amounts found that banks did not offer such loans. Because many of these consumers could not qualify for a credit card, they were forced to search elsewhere to fulfill their credit needs. Payday lenders provided access to cash to those who had minimal access to banks. Since the early 1990s, the amount of payday loans issued has risen from virtually zero to about fifteen billion dollars a year.

When one borrows money from a payday lender, the borrower typically writes a personal check payable to the lender. The amount payable represents the amount the borrower wishes to borrow, in addition to a fee. Usually, the fee equals a percentage of the value borrowed or a fee per each one hundred dollars loaned. In many states, the borrower maintains three options after writing the lender the check. At any time, the borrower may pay the lender the amount of the check's face value in order to redeem his or her check, minus the fee. The

2. Id. In the 1980s, deregulation of banking drove banks to eliminate services that lost money, such as bank accounts with small balances and free checking accounts. Lisa Blaylock Moss, Modern Day Loan Sharking: Deferred Presentment Transactions & the Need for Regulation, 51 ALA. L. REV. 1725, 1732 (2000).
3. Schaaf, supra note 1, at 340.
4. Id. at 339.
6. Schaaf, supra note 1, at 341. Thus, the borrower must have a checking account against which he writes a post-dated check. See id. The check cannot be cashed until its date, which is presumably after the borrower's next payday. See id. at 342.
7. Id. at 341.
8. Id.
9. Id. at 342.
10. Id.
borrower’s second option is to allow the lender to cash the check after the loan period. Finally, if the borrower cannot afford to pay the loan, many states allow the lender to extend the loan for another loan period, resulting in the borrower again paying the finance charge. Because most of the payday lenders charge flat fees, the loans carry exorbitant annual percentage rates, typically ranging from 250 percent to more than 1000 percent.

Many states have enacted strict usury laws prohibiting the high interest rates charged by payday lenders, while other states have enacted laws prohibiting payday lending altogether. Even with these restrictions, the practice frequently makes its way into such states through lenders partnering with a national bank located in a different state that lacks strict usury laws. Recently, federal courts have been asked to decide whether payday lenders may take advantage of what many have referred to as a “loophole” in the law.

Part I of this Note will examine state regulation of payday lending. Part II will explain the role of federal law in payday lending. Part III will discuss recent strikes against payday lending.

11. Moss, supra note 2, at 1729.
12. Schaaf, supra note 1, at 342.
19. See infra notes 23-30 and accompanying text.
20. See infra notes 31-50 and accompanying text.
lenders' partnering with national banks. Part IV will explore the future of such partnerships.

I. STATE REGULATION OF PAYDAY LOANS

In an amendment to the Truth in Lending Act's Official Staff Commentary, the Federal Reserve Board ruled that payday lenders must publish annual interest rates. Also, the Federal Trade Commission has brought charges against payday lenders for false representation to consumers. Although these federal regulations exist, payday lenders are primarily regulated by the states.

Many states have enacted usury laws that establish interest rate ceilings. States fall into three categories with regard to the regulation of payday lending. One group of states requires payday lenders to comply with usury restrictions. Another group allows payday lenders to charge any interest rate they choose. Finally, a group of states permits payday lending, but governs such lending through specific payday loan statutes.

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21. See infra notes 51-150 and accompanying text.
22. See infra notes 151-182 and accompanying text.
25. See Schaaf, supra note 1, at 356.
26. See Party Yards, Inc. v. Templeton, 751 So. 2d 121, 123 (Fla. Dist. Ct. App. 2000). The Court in Party Yards held that to establish that a transaction is usurious, the party must show: (1) an express or implied loan, (2) a requirement for repayment, (3) an agreement to pay interest in excess of the legal rate, and (4) a corrupt intent to take more than the legal rate. Id. The Court noted that corrupt intent is established if the evidence indicates that the lender knowingly charged or received interest in excess of the legal rate, considering all of the surrounding circumstances. Id.
27. Bruch, supra note 17, at 1260.
28. Id. at 1260-61. Twenty states require payday lenders to comply with usury restrictions. Id.
29. Id. at 1261. Eight states allow payday lenders to charge any interest rate they choose. Id.
30. Id. Twenty-two states and the District of Columbia have specific payday loan statutes. Id.
II. FEDERAL LAW PERMITTING BANK EXPORTATION OF INTEREST RATES

One piece of federal legislation in particular allows payday lenders to bypass the constraints of state usury laws.\textsuperscript{31} Section 85, known as the National Bank Act, has emerged as an enabling statute for payday lenders.\textsuperscript{32} The Act allows national banks to charge customers in other states interest rates limited only by the usury statutes of the state in which the national bank is physically located.\textsuperscript{33} Enacted in 1864, the Act sought to advantage weak national banks and state banks.\textsuperscript{34} The Act did not seek to provide a loophole for payday lenders, nor could those enacting the legislation even envision such a purpose.\textsuperscript{35} Payday lending is a modern problem finding a solution in long-standing legislation.\textsuperscript{36}

Under Section 85, national banks may export the usury law of their home state nationwide.\textsuperscript{37} The laws of a particular national bank’s home state then preempt any state laws restricting interest in the borrower’s state.\textsuperscript{38} The Act affects payday lending when payday lenders affiliate with federal banks located in states with no or minimal interest rate restrictions.\textsuperscript{39} Once affiliated with

\textsuperscript{31} Id.
\textsuperscript{32} Id. at 1262.
\textsuperscript{34} Bruch, \textit{supra} note 17, at 1262. In \textit{Tiffany v. Nat’l Bank of Missouri}, the Supreme Court articulated the purpose of the legislation:

\begin{quote}
It cannot be doubted, in view of the purpose of Congress in providing for the organization of National banking associations, that it was intended to give them a firm footing in the different States where they might be located. It was expected they would come into competition with State banks, and it was intended to give them at least equal advantages in such competition. In order to accomplish this they were empowered to reserve interest at the same rates, whatever those rates might be, which were allowed to similar State institutions. This was considered indispensable to protect them against possible unfriendly State legislation.
\end{quote}


\textsuperscript{36} See Bruch, \textit{supra} note 17, at 1262.
\textsuperscript{37} Drysdale & Keest, \textit{supra} note 13, at 646; see also Cades v. H & R Block, Inc., 43 F.3d 869, 873-74 (4th Cir. 1994) (holding that an out-of-state bank’s use of a local agent to make loans did not affect the preemptive force of the National Bank Act).
\textsuperscript{38} Drysdale & Keest, \textit{supra} note 13, at 646.
\textsuperscript{39} See Bruch, \textit{supra} note 17, at 1262.
these banks, payday lenders may charge their customers any interest rate allowed in the state of the bank, even if the customers reside in states having restrictive usury statutes. Thus, payday lenders circumvent state usury laws by forming partnerships with banks holding national charters.

At the end of 1999, seven national banks had partnered with payday lenders. A report issued in 2001 by the Consumer Federation of America and the U.S. Public Interest Research Group listed nine banks that worked with payday lenders. Some of these national banks contribute nothing more to the partnership than allowing the payday lender access to their state’s usury laws. Currently, approximately twelve banks partner with payday lenders. These partnerships of national banks and payday lenders account for an estimated ten percent of all payday loans issued.

In addition to Section 85, a federal statute enacted in 1980 provides the same possibility for interest rate exportation to state banks. Like Section 85, Section 1831d seeks to prevent discrimination against state banks. The legislation provides that the interest rates of a foreign bank, with a charter in a particular state, preempt the interest rates allowable by the state in which the foreign bank is chartered. Thus, the legislation provides a vehicle for payday lenders to escape state usury laws by partnering with a foreign bank.

41. Beckett, supra note 5.
44. Drysdale & Keest, supra note 13, at 604-05.
46. Id.
50. Id.
III. RECENT STRIKES AT PAYDAY LENDERS’ PARTNERING WITH NATIONAL BANKS

A. State Action

States are beginning to strike the payday lending industry’s practice of circumventing state usury laws by partnering with national banks. A new law in Maryland prohibits any company in the state from acting as a broker for payday loans from a national bank. Since 1999, officials at the New York State Banking Department have sent letters to lenders, noting that charging more than twenty-five percent interest is criminal under New York law. Although legislation regulating payday lenders’ partnerships with national banks expired in North Carolina in 2001, the North Carolina legislature is considering similar regulation.

In March 2002, Indiana enacted a law to prohibit banks from partnering with payday lenders. The chief counsel for the state’s Department of Financial Institutions, J. Phillip Goddard, accused payday lenders and banks partnering with them of “greed.” This action by Indiana forced Republic First Bancorp, Inc. of Philadelphia, a company with $680 million in assets, to exit the state. Republic First Bancorp, Inc. accounted for sixty-five percent of the short-term loan business in the state.

53. See id.
54. Schaaf, supra note 1, at 359.
56. Reosti, supra note 51, at 1.
57. Id.
58. Id.
59. Id. Republic First Bancorp, Inc. first entered the payday lending business when it partnered with Check Into Cash, Inc., a payday lender located in Cleveland, Tennessee. Id.
B. Federal Action

Recently, the United States government has taken action.\(^60\) On January 3, 2002, the Office of the Comptroller of the Currency (OCC) ordered Eagle National Bank of Upper Darby, Pennsylvania to stop providing payday loans to one of the nation’s largest payday lenders, Dollar Financial Group.\(^61\) This order provided the first concrete evidence of the OCC’s disapproval of alliances between national banks and payday lenders.\(^62\) The OCC emphasized Eagle National Bank’s lack of supervision of the loan program.\(^63\)

In the order, the Comptroller of the Currency, John D. Hawke, Jr. stated: “Eagle simply did not have the capacity to manage the relationship.”\(^64\) Hawke continued: “The bank essentially rented out its national bank charter to a payday lender to facilitate [Dollar’s] evasion of the requirements of state law that would otherwise be applicable to it.”\(^65\) Hawke emphasized that the OCC based its action against Eagle on an examination of how Eagle National Bank ran the loan program, rather than on the existence of the alliance itself.\(^66\)

Noting the shortcomings of the arrangement, Hawke pointed out that Dollar Financial Group had opened stores in some states and had begun originating payday loans without Eagle National Bank’s knowledge or approval.\(^67\) Ultimately, Hawke termed the arrangement between Eagle National Bank and Dollar Financial Group as “charter abuse.”\(^68\) Declaring the purpose of the OCC’s action, Hawke stated: “We don’t want to see the national bank charter used by nonbank entities as a way of evading

\(^{60}\) Beckett, supra note 5, at C1.
\(^{62}\) Beckett, supra note 5, at C1.
\(^{63}\) Id.
\(^{64}\) Id. at C15 (quoting Comptroller of the Currency John D. Hawke, Jr.).
\(^{65}\) Id. (quoting Comptroller of the Currency John D. Hawke, Jr.).
\(^{66}\) Id.
\(^{67}\) Id.
\(^{68}\) Id. (quoting Comptroller of the Currency John D. Hawke, Jr.).
state law." Regarding the OCC's decision, the consumer protection director at the Consumer Federation of America commented: "Eagle National Bank and Dollar Financial Group pioneered the rent-a-bank payday loan arrangement to get around state laws." The consumer protection director stated that "[t]he OCC's action is an important first step toward closing that loophole."

In October 2002, the OCC took another step in that direction. The OCC ordered Goleta National Bank to stop providing payday loans through the offices of Ace Cash Express, Inc., the nation's largest check-cashing chain. A spokesperson for the OCC said that Ace's failure to safeguard customer files on loans issued by Goleta prompted the order. The OCC also found that Ace committed "unsafe and unsound practices including a pattern of excessive exceptions to Goleta's policies and procedures." Ace agreed to pay a fine of $250,000 and Goleta agreed to a fine of $75,000. Comptroller of the Currency John D. Hawke, Jr. said: "Ace's inability to safeguard the files of customers whose loans were booked at Goleta shows just how risky those relationships can be between banks and payday lenders."

The OCC is also seeking to issue an enforcement action against People's National Bank of Paris, Texas, a company with

69. Id. (quoting Comptroller of the Currency John D. Hawke, Jr.).
70. Id. (quoting Jean Ann Fox, consumer protection director at the Consumer Federation of America).
71. Id. (quoting Jean Ann Fox, consumer protection director at the Consumer Federation of America).
74. Jackson, supra note 43, at 1. In August, more than 600 customer files were discarded in a dumpster in Portsmouth, Virginia. Id. A spokesperson for the OCC said this discarding could have compromised the customers' right to privacy. Id. Ace Cash Express was unable to account for 641 of those files. Id.
75. Id.
76. Id. The OCC also required Goleta to notify all borrowers whose loan files were lost and to advise those customers on potential identity theft. Id.
77. Id.
$103 million dollars in assets. In support of its action, the OCC claims People's National Bank is operating an illegal payday lending business. Contesting the action, People's National Bank has filed suit in federal court.

Notwithstanding the actions by the OCC, federal legislation is also pending. The Payday Borrower Protection Act of 2001, if passed, would prohibit payday loans unless authorized and regulated by state law. Moreover, the Act would disallow the exportation of interest rates for payday loans. It would achieve this by prohibiting a national bank from using a payday lender as an agent unless "such loan is in full compliance with the law of the State in which such loan is made." Therefore, the interest rate would have to comply with the usury laws of the state in which the loan is made, not the home state of the national bank.

C. The Supreme Court's Examination of a Similar Issue

Although the Supreme Court has not addressed the precise issue of payday lending, the Court has examined a similar issue. In *Marquette National Bank of Minneapolis v. First of Omaha Service Corporation*, Marquette National Bank of Minneapolis, a Minnesota-chartered national banking association, brought suit against First National Bank of Omaha, a national banking association chartered in Nebraska. Marquette brought suit to enjoin the operation of First National Bank of Omaha's credit card

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80. See id.
82. See id. at 3-4.
83. See id. at 13. The bill proposes: "To amend the Consumer Credit Protection Act and other banking laws to protect consumers who avail themselves of payday loans from usurious interest rates and other unfair practices by payday lenders, to encourage the states to license and closely regulate payday lenders, and for other purposes." Id. at 1.
84. See id. at 4-5.
85. See id. at 13.
87. Id. at 299.
program in Minnesota until the bank complied with Minnesota’s usury laws.\textsuperscript{88}

The issue before the Court was whether the National Bank Act authorized a national bank based in one state to charge its out-of-state credit-card customers an interest rate on unpaid balances allowed by its home state, when that rate was greater than that permitted by the nonresident customers’ state.\textsuperscript{89} The Court held that the National Bank Act allowed the bank to charge the higher rate.\textsuperscript{90}

Although the credit-card program at issue in \textit{Marquette} does not equate with payday lending per se, the resemblance between the two is compelling. Both programs essentially involve an extension of credit, and the Court in \textit{Marquette} noted that the credit-card program enabled cardholders to obtain cash advances from participating banks,\textsuperscript{91} just as a payday lender offers cash in advance.\textsuperscript{92} Another similarity between the credit card program and payday lenders who partner with national banks is that the credit-card program was operated by another corporation.\textsuperscript{93}

One difference between the credit card arrangement and that of a payday lender partnering with a national bank is that the credit-card program was operated by a company wholly owned by the national bank.\textsuperscript{94} \textit{Marquette} fails to shed light on the National Bank Act’s effect on payday lenders because the agent of the national bank did not claim to extend credit in \textit{Marquette}.\textsuperscript{95}

\textsuperscript{88.} \textit{Id.} at 299.
\textsuperscript{89.} \textit{Id.} at 301.
\textsuperscript{90.} \textit{Id.}
\textsuperscript{91.} \textit{See id.} at 301-02.
\textsuperscript{92.} \textit{See Schaaf, supra note 1.}
\textsuperscript{94.} \textit{See id.}
\textsuperscript{95.} \textit{See id.} at 307-08. The Court declined to rule on the issue in the case of an agent of the national bank purporting to extend credit. \textit{See id.} Accordingly, the Court’s reasoning for its holding bears no implication for payday lenders. \textit{Id.} at 308. It merely affirmed the National Bank Act’s allowance of national banks to charge interest rates permitted by their home states. \textit{See id.} The Court declared that the First National Bank of Omaha was a national bank, and thus, it was an “instrumentalit[y] of the federal government, created for a public purpose, and as such necessarily subject to the paramount authority of the United States.” \textit{Id.} After asserting that the interest rate that the First National Bank of Omaha charged is governed by federal law, the Court stated that the National Bank Act “plainly
D. Two Federal Courts Take Different Approaches

1. Ace Cash Express, Inc. v. Lingerfelt

Recently, federal courts have been asked to examine the partnership between payday lenders and national banks. The first approach comes out of *Goleta Nat'l Bank v. Lingerfelt*. Plaintiffs Goleta National Bank and Ace Cash Express, Inc. brought an action to enjoin North Carolina officials from enforcing state lending and consumer protection laws against Ace Cash Express, Inc. with regard to its practice of payday lending. The United States District Court for the Eastern District of North Carolina granted the state's motion to dismiss the suit.

Goleta National Bank and Ace Cash Express, Inc.'s action stemmed from a previous lawsuit. In January 2002, the Commissioner of Banks of North Carolina and the Attorney General of North Carolina, acting on behalf of the State, filed suit against Ace. The State alleged that Ace Cash Express was engaged in payday lending that violated North Carolina's usury statutes. Ace Cash Express removed the case to federal court, asserting that federal question jurisdiction existed because the

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96. See Jackson, *supra* note 18, at 5.
97. *See Goleta Nat'l Bank v. Lingerfelt*, 211 F. Supp. 2d 711, 711 (E.D.N.C. 2002). Hal D. Lingerfelt served as the Commissioner of Banks of North Carolina. *Id.* The Honorable Roy Cooper was also named as a defendant in his official capacity as the Attorney General of North Carolina. *Id.*
98. *Id.* at 713.
99. *Id.*
100. *Id.* The suit was filed in the Superior Court of Wake County, North Carolina. *Id.*
101. *Id.* *see* N.C. Gen. Stat. § 24-1.
State’s claims were preempted by the National Bank Act.\textsuperscript{102} The federal court ultimately granted the State’s motion to remand the case to Wake County Superior Court, concluding that the National Bank Act did not completely preempt a state action against Ace Cash Express, a non-national bank.\textsuperscript{103} The federal court reasoned that the Goleta National Bank and Ace Cash Express are separate entities, and stated: “The Complaint strictly is about a non-bank’s violation of state law. It alleges no claims against a national bank under the NBA.”\textsuperscript{104}

In Wake County Superior Court, a settlement was reached between Ace Cash Express and state officials.\textsuperscript{105} Under the agreement, the attorney general dropped the suit, and Ace Cash Express promised not to make payday loans in North Carolina for the next twelve months.\textsuperscript{106} Ace Cash Express must follow state law should it resume making payday loans once the year is over.\textsuperscript{107} To re-enter the payday lending business, Ace Cash Express additionally must obtain a state license.\textsuperscript{108}

Before the settlement in Wake County Superior Court, Goleta National Bank and Ace Cash Express requested the following relief in \textit{Goleta Nat’l Bank v. Lingerfelt}: (1) a declaration that the National Bank Act preempts the state action claim against Ace Cash Express, (2) a declaration that any North Carolina law which prohibits Ace Cash Express from engaging in payday lending violates the plaintiffs’ constitutional rights to liberty and property, and (3) an injunction preventing the State from enforcing the North Carolina laws at issue in the state action against either Ace Cash Express or Goleta National Bank.\textsuperscript{109} Plaintiffs argued that the National Bank Act asserts that the allowable interest rate on payday loans is determined by Goleta’s

\textsuperscript{102} Goleta Nat’l Bank, 211 F. Supp. 2d at 711.
\textsuperscript{103} See id. at 713.
\textsuperscript{104} See id. at 711.
\textsuperscript{105} Ben Jackson, \textit{Ace, N.C. Reach Settlement But Disagree on the Results}, \textit{AM. BANKER}, Dec. 18, 2002.
\textsuperscript{106} Id.
\textsuperscript{107} Payday Lender Agrees to Stop Making High-Fee Loans, \textit{RALEIGH NEWS & OBSERVER}, Dec. 15, 2002, at 4B. Ace Cash Express, with at least 16 branch offices in North Carolina, was charging an effective annual percentage rate of 443 percent. \textit{Id.}
\textsuperscript{108} Id.
\textsuperscript{109} See Goleta Nat’l Bank, 211 F. Supp. 2d at 713.
home state, California. Secondly, the plaintiffs claimed that because 12 U.S.C. § 24 authorized Goleta to use an agent to make loans, North Carolina laws prohibiting Ace Cash Express from making payday loans violated the plaintiffs' rights under federal law. Third, the plaintiffs asserted that, under 12 U.S.C. § 484, the United States Office of the Comptroller of the Currency has exclusive authority to regulate national banks, and therefore, the State's efforts to enforce its laws against Ace Cash Express violated the plaintiffs' rights under federal law. Finally, the plaintiffs alleged that North Carolina law, as applied against Ace Cash Express, violated the Fourteenth Amendment in that it deprived Ace Cash Express and Goleta National Bank of economic liberty and property without due process.

The State argued that Ace Cash Express (the payday lender), not Goleta National Bank (the national bank), made the loans at issue in the state action. Goleta and Ace Cash Express asserted that Ace Cash Express was merely Goleta's agent in promoting, originating, and servicing these loans. Therefore, the federal court acknowledged that the identity of the true lender was a disputed fact in both the federal and state action.

Ultimately, the court dismissed the federal suit, finding no merit in Ace Cash Express's argument that the National Bank Act's preemption rendered the state action facially conclusive. Regarding the state action, the federal court stated:

While it is true that the NBA does preempt state efforts to regulate the interest collected by national banks, the NBA patently does not apply to non-national banks. In this case, the state action claims are asserted against Ace, a non-national bank. Although Ace contends that Goleta is the real

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110. Id. at 714.
111. Id.
112. Id. at 711.
113. Id. at 714.
114. Id. at 711.
115. Id. at 711.
116. See id.
117. Id. at 718.
maker of the loans at issue, the State contends just
the opposite: that Ace is using Goleta's name as
mere subterfuge for its own unlawful lending
practices. Thus, a sharp factual issue is presented as
to whether Goleta, a national bank, is the real
lender at issue.\textsuperscript{118}

This federal court's interpretation of the National Bank
Act proves consistent with its purpose.\textsuperscript{119} At the time of its
enactment in 1864, the Act sought to provide an advantage to
weaker national banks.\textsuperscript{120} The Act did not seek to provide a
loophole for payday lenders.\textsuperscript{121} In fact, those enacting the
legislation could not even envision such a purpose as payday
lending is a modern practice.\textsuperscript{122}

2. Hudson v. Ace Cash Express, Inc.

Another federal court has taken a different stance than that
taken by the United States District Court for the Eastern District
of North Carolina.\textsuperscript{123} The second approach adopted by a federal
court comes out of \textit{Hudson v. Ace Cash Express, Inc.}\textsuperscript{124} Hudson
sued defendants Ace Cash Express, several of its officers, and
Goleta National Bank for making a payday loan in violation of
Indiana usury law and other federal laws.\textsuperscript{125} Defendants moved to
dismiss all asserted claims for failure to state a claim upon which
relief could be granted.\textsuperscript{126} The United States District Court for the

\textsuperscript{118} \textit{Id.} at 717-18.
\textsuperscript{120} \textit{Bruch, supra} note 17, at 1262.
\textsuperscript{121} See 12 U.S.C. § 85.
\textsuperscript{122} \textit{See} \textit{Bruch, supra} note 17, at 1262.
\textsuperscript{123} \textit{See} \textit{Jackson, supra note} 18, at 5.
\textsuperscript{124} \textit{Hudson v. Ace Cash Express, Inc.}, 2002 WL 1205060, at *1 (S.D. Ind. May 30,
2002).
\textsuperscript{125} \textit{Id.} The plaintiff argued that the loan violated Indiana usury law, the federal
Truth in Lending Act, and the federal Racketeer Influenced and Corrupt
Organizations Act. \textit{Id.} Because Hudson asserted two claims arising under federal
law, the United States District Court for the Southern District of Indiana exercised
supplemental jurisdiction over her state law claims. \textit{Id.}
\textsuperscript{126} \textit{Id.}
Southern District of Indiana granted defendants' motion to dismiss.127

In Hudson, the plaintiff contended that a genuine issue existed as to whether Goleta National Bank or Ace Cash Express was the actual lender.128 Asserting that Goleta National Bank was not the lender, the plaintiff argued that Goleta's role in servicing her loan was so insignificant that the court should regard Ace as the true lender, despite the fact that Goleta issued the loan.129 Also, the plaintiff suggested that the district court should regard Ace Cash Express "as the true lender because defendants' lending arrangement was designed for the sole purpose of circumventing Indiana usury law."130

The district court accepted the plaintiff's factual premises regarding Goleta National Bank's role and the defendants' purposes in making the loans.131 After recognizing its acceptance of the plaintiff's premises, the district court stated: "These arguments might appeal to those who believe substance should always trump form in the law, and they may provide a reasonable foundation for closer federal regulation of national banks that engage in such transactions. These arguments do not, however, offer a basis for giving Hudson any relief."132

The district court in Hudson cited the Supreme Court case Marquette National Bank, which held that the National Bank Act authorizes a national bank in one state to charge its out-of-state credit card customers any interest rate allowed by its home state, even when the rate charged is greater than the rate permitted by the customer's home state.133 In examining Marquette, the district court in Hudson noted that the Supreme Court recognized that the National Bank Act "will significantly impair the ability of States to enact effective usury laws."134 The Supreme Court added that "the

127. Id.
128. Id. at *4.
129. Id.
130. Id.
131. Id.
132. Id.
133. See supra notes 86-95 and accompanying text; Hudson, 2002 WL 1205060, at *4.
protection of state usury laws is an issue of legislative policy, and any plea to alter § 85 to [protect state usury laws] is better addressed to the wisdom of Congress than to the judgment of the Court.”

Likening the case to Marquette National Bank, the district court in Hudson asserted that in both cases, the plaintiff challenged a national bank’s practice of imposing finance charges allowed by its home state on its out-of-state customers whose states of residence would outlaw such charges.

Additionally, the district court analogized the case with that in an Eighth Circuit decision, Krispin v. May Dep’t Stores Co. In Krispin, the defendant, a Missouri department store, issued credit cards to the plaintiffs in Missouri. Later, the store assigned its entire interest in the credit cards to a national bank in Arizona. The store then issued a notice to the plaintiffs stating that the Arizona national bank was extending credit. The store, however, purchased the credit card receivables originated by the bank on a daily basis and collected and received cardholders’ payments. The plaintiffs sued the store, alleging that the late fees charged on their credit card violated Missouri law.

In support of the position that the National Bank Act did not apply, the plaintiffs in Krispin asserted: (1) the plaintiffs entered into their credit agreements with the Missouri store, (2) the Missouri store “remained substantially involved in the collection process,” and (3) the Missouri store retained a financial interest in the accounts even after assigning its interest to the Arizona national bank. The Eighth Circuit held that the National Bank Act applied to the credit agreements. In deciding whether the National Bank Act applied, the Eighth Circuit stated

(1979); see Hudson, 2002 WL 1205060, at *4.
137. See id.
138. See Krispin v. May Dep't Stores Co., 218 F.3d 919, 921 (8th Cir. 2000); Hudson, 2002 WL 1205060, at *4.
139. Krispin, 218 F.3d at 921-22.
140. Id.
141. Id. at 923.
142. Id. at 922.
143. See id. at 923.
144. See id. at 922-23.
that the originating entity (in that case, the bank) served as the determinative factor. Relying on Krispin, the Court in Hudson granted the defendants' motion to dismiss.

Although the district court for the Eastern District of North Carolina, in Goleta Nat'l Bank v. Lingerfelt, ruled consistently with the purpose of the National Bank Act, the federal court's reasoning in Hudson proves most consistent with that of the Supreme Court in Marquette. The federal court in Hudson refused to sacrifice form for substance in determining preemption under the National Bank Act. The court failed to inquire as to the identity of the real lender—Goleta National Bank or Ace Cash Express. In determining preemption under the Act, the identity of the true lender proves essential even when form is not compromised in interpreting the Act.

IV. PAYDAY LENDER AND NATIONAL BANK PARTNERSHIPS IN THE FUTURE

As state legislatures and courts attack partnerships between payday lenders and national banks, payday lenders are beginning to take drastic measures to keep their business alive. Check 'n Go serves as a payday lender, with 670 outlets in twenty-four states. Recently, the investors who own Check 'n Go's parent company, CNG Financial Inc., created a company to purchase a bank. That company, Cincinnati BancGroup Inc., applied to the Federal Reserve Bank of Chicago to acquire Bank of Kenney in Illinois, and thereby become a bank holding
company. This is the first time a payday lender has ever attempted to buy a bank.

Opponents argue that Cincinnati BancGroup is trying to circumvent state usury laws that ban or restrict payday lending. They assert that approving the purchase would encourage payday lenders with sufficient funds available for such a purchase to buy small banks. An attorney at the National Center on Poverty Law in Chicago said the opponents fear that the payday lender would be incorporated as part of the Bank of Kenney. Under the National Bank Act, the bank could then “export” to other states the high rates permitted by Illinois usury law. Thus, buying the Bank of Kenney would allow CNG Financial Services, Inc. to forego partnering with another bank in order to export the high rates permitted by the state of organization of that particular bank. Opponents stress that Check ‘n Go notoriously facilitates federal laws in order to avoid consumer protection laws. For instance, Check ‘n Go has been providing payday loans to consumers in North Carolina, where payday lending is illegal. Check ‘n Go accomplished this by acting as a broker of short-term loans for a national bank in Illinois.

Protesting the purchase are four members of Illinois’ congressional delegation. Questioning CNG Financial Inc.’s business plan, they urged that a public hearing be held to “discuss

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154. Id. The chairman of Bank of Kenney stated that the Bank was not looking for a buyer; Cincinnati BancGroup approached it. Id. at 1, 6.
155. Id.
156. Id.
157. See Jackson, supra note 151, at 6. The Federal Reserve Bank of Chicago has received 50 comment letters, most opposing the purchase. Id.
158. Id.
159. Id.
160. See id.
161. See id.
162. See id.
163. Jackson, supra note 151. Check ‘n Go acts as a broker for Brickyard Bank, located in Lincolnwood, Illinois. Id. Brickyard Bank has $193 million in assets. Id. But recently Brickyard Bank announced that the bank was terminating its partnerships with payday lenders. Jackson, supra note 43.
164. Jackson, supra note 151. Those four members are Representatives Danny K. Davis, Jesse L. Jackson, Jr., Bobby L. Rush, and Janice D. Schakowsky. Id. All are Democrats. Id.
the negative ramifications of a payday lender becoming a bank."\textsuperscript{165} They stated: "If the application is approved, we believe it will make a sham of the integrity of the banking regulatory framework by allowing Cincinnati BancGroup to use bank privileges to make predatory, high-cost payday loans."\textsuperscript{166}

Countering this claim, John Bruno, Cincinnati BancGroup’s President and Senior Vice President of CNG Financial, Inc., said owning a bank would facilitate access to funds from Federal Home Loan Banks and other sources.\textsuperscript{167} Furthermore, Bruno stated that the purchase would help Cincinnati BancGroup raise equity capital more successfully than it could as CNF Financial, Inc.\textsuperscript{168}

As a result of the crackdown on partnerships between payday lenders and national banks, banks are leaving the business.\textsuperscript{169} Recently, at least three banks have voluntarily left the practice of payday lending.\textsuperscript{170} Brickyard Bank of Lincolnwood, Illinois announced that the bank was terminating its partnerships with payday lenders.\textsuperscript{171} Specifically, Brickyard Bank’s Chairman, President, and Chief Executive Officer, David L. Keller, cited a September 3, 2002 order by the Federal Deposit Insurance Corp. (FDIC) and the Illinois Office of Banks and Real Estate as the reason for the bank’s decision.\textsuperscript{172}

The order required the bank, a company with $200 million in assets, to raise its capital by one dollar for every one dollar outstanding in payday loans.\textsuperscript{173} Keller said that this order made payday lending “too expensive” for Brickyard Bank.\textsuperscript{174} As reason for the order, the FDIC and the Illinois Office of Banks and Real Estate charged Brickyard Bank with “operating with an

\textsuperscript{165} Id.
\textsuperscript{166} Id.
\textsuperscript{167} See id.
\textsuperscript{168} See id.
\textsuperscript{169} See Jackson, supra note 43.
\textsuperscript{170} Id.
\textsuperscript{171} See id.
\textsuperscript{173} Jackson, supra note 43.
\textsuperscript{174} See id.
inadequate level of capital protection for the kind and quality of assets held." The order also stated that Brickyard Bank did not monitor Check 'n Go properly. Stating that the FDIC was following supervisory guidelines issued by federal banking agencies, a spokesman for the FDIC said, "This guidance indicates that we'll ask banks to hold increased reserves, including dollar-for-dollar capital for riskier lending activities on a case-by-case basis."

Other banks are not as quick to leave the business. Upon hearing that Brickyard Bank terminated its partnership with Check 'n Go, a number of other banks contacted Check 'n Go, hoping to enter the business. Although forced to stop payday lending in Indiana, Republic First Bancorp, Inc. of Philadelphia plans to continue such business. The company continues to look for payday lending opportunities, and the company's president, Harry Madonna, said short-term loans would remain one of the company's endeavors, "despite the setback in Indiana and the general controversy surrounding the relationships."

Although Brickyard Bank left the business, the bank's Chairman, President, and Chief Executive Officer, David L. Keller, stated that he believes consumer need for payday lending exists and that payday lending can be a profitable service for banks despite the risks.

VI. CONCLUSION

While the payday lending industry is being attacked by state legislation, pending federal legislation, the OCC, and in suits across the country, the industry finds a shield in the National Bank Act. By partnering with national banks, payday lenders find

175. See Jackson, supra note 43.
176. Id.
177. Id.
178. Id.
179. See id.
180. See Reosti, supra note 51.
181. See id.
182. See Jackson, supra note 43.
183. See supra notes 31-150 and accompanying text.
refuge under the National Bank Act’s allowance of interest rate exportation. These partnerships allow payday lenders to charge interest rates that otherwise would be illegal in states with restrictive usury laws.

Enacted in the nineteenth century, the National Bank Act sought to advantage weaker federal banks and state banks. The Act did not seek to provide a loophole for payday lenders, nor could those enacting the legislation even envision such a purpose. Payday lending is a modern problem finding refuge in long-standing legislation. When the national bank’s involvement is facially minimal, the National Bank Act should not provide an avenue for payday lenders to escape state laws. To allow this is to permit federal legislation to trump state legislation on an issue that the federal legislation was not meant to address.

While a significant demand for the short-term loans as provided by payday lenders is evident by the explosion of the industry in recent years, the customer’s need is exactly what gives the lender leverage. When states adopt laws to prevent lenders from charging excessive interest rates, these laws should not be circumvented by a federal act never envisioned to apply to such an issue. Until the courts look substantively to the administration of payday loans, the states’ prerogative to outlaw payday lending will continue to collapse in the face of the National Bank Act.

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185. See Drysdale & Keest, supra note 13, at 646-47.
186. See Bruch, supra note 17, at 1262.
188. See Schaaf, supra note 1, at 339.
189. See Goleta Nat’l Bank, 211 F. Supp. 2d at 718.
191. See Schaaf, supra note 1, at 345.