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Small Loans in California

Robert E. Stone*

During the first week of March of this year the newspapers in the San Francisco Bay Area carried daily accounts of proceedings taken against the Central Industrial Loan Company of Berkeley and its Oakland branch office by the State Corporation Commissioner and of hearings before the Grand Jury in Alameda County. The proceedings, at the most recent date, indicate that the owners of the company have consented to the appointment of a receiver and the winding up of their business by the state. Just previously to that, charges had been passed around by word of mouth that the Personal Property Brokers’ Acts and California Small Loan Laws passed at the 1939 session of the legislature1 were so strict that lenders could

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1 In most states there is one class of lenders who make both secured and unsecured loans of small amounts. Hence one regulatory act is sufficient to cover the field. But the California Constitution by an amendment adopted in 1934 grants the legislature power to regulate personal property brokers, who were then defined as lenders upon security, and states that the interest charges of certain other lenders cannot be regulated by the legislature. Because there is a doubt whether the legislature has power under the constitution to change the definition of personal property brokers so as to make it include unsecured lenders, it was felt necessary to pass two acts, one known as the Personal Property Brokers’ Act, and the other known as the California Small Loan Act, the latter regulating the unsecured lender.

The two sets of acts are substantially identical in almost every respect, except for the statement of the maximum charge for interest and expense, and even here the net results are the same, the difference being solely in the form of expression. In this article, in section A, will be found a fairly detailed discussion of the personal property brokers acts. Because the California Small Loan Acts have the same regulatory features, there will be no need for any discussion of such phases of those acts. Since most lenders prefer not to take out two licenses, and since all wish to make some secured loans, all the lenders in the state except four are operating under the Personal Property Brokers’ Acts alone. Although not used to any extent, the Small Loan Act does serve a most useful purpose as a bulwark of the personal property brokers laws, preventing any evasion of them under the guise of making unsecured loans. The small loan laws are briefly discussed in section C of the text.

The Personal Property Brokers’ Act and the California Small Loan Act were introduced in the Senate by Senator John F. Shelley of San Francisco. Identical companion bills were introduced in the Assembly by Assemblyman Albert M. Wollenberg of San Francisco and James H. Phillips of Oakland. All four passed and became law.

The only difference between the two personal property brokers’ acts is that the one introduced by Assemblymen Wollenberg and Phillips [Cal. Stats. 1939, p. 2667] contains section 20.5 providing an appropriation for the use of the Corporation Commissioner in carrying out the provisions of the act, a section not found in the other [Cal.
not afford to lend small sums to needy borrowers with the consequence that they were unable to obtain money when needed. This induced the Russell Sage Foundation of New York to finance a survey of Alameda County to get at the facts, and the investigation recently made proves these charges to be false. Further, it was determined that the charges were spread by those back of the Central Industrial Loan Company, either as a smoke screen to justify their high-rating, or as a device to gain public support for the relaxing of the 1939 laws.

Despite such opposition, small loan legislation has received both judicial and popular support. Less than a year ago the California Supreme Court in a sweeping decision upheld the validity of this legislation. After devoting many pages to refuting the arguments advanced against the laws, the court said: "Other assaults upon the act are many and varied, leaving unchallenged practically nothing but the punctuation. Those which have not been discussed are either included within the points passed upon or are so inconsequential as not to merit recognition." But more remarkable was the fact that earlier the people of the state, by a referendum vote on the Personal Property Brokers' Acts—a straight-forward, uncamouflaged, two and one-half per cent per month interest measure—had overwhelmingly supported the laws. As an eastern writer said: "This was the first time that the people in any state had had an opportunity to vote directly on small loan regulation. More persons voted in this election than in any other election in California. The total vote of 2,974,406 comprised 82.4% of the state's total registered voters." These acts are revisions of the former Personal Property Brokers' Act, Cal. Stats. 1909, p. 969, as amended by Cal. Stats. 1911, p. 978, Cal. Stats. 1931, p. 558, and Cal. Stats. 1933, p. 1496.

The two California Small Loan Acts constitute new legislation. They differ only in that Cal. Stats. 1939, p. 2679, contains section 21.5 carrying an appropriation similar to that found in section 20.5 of the Personal Property Brokers' Act, a section missing from Cal. Stats. 1939, p. 2886.

The acts containing the appropriation were each signed by the Governor on July 24, 1939, while the others were approved on July 22 and 21, 1939.

2 See Note at end of article.

3 In re Fuller (1940) 15 Cal. (2d) 425, 439, 102 P. (2d) 321, 329.

4 Gisler, Organization of Public Opinion for Effective Measures Against Loan Sharks (1941) 8 Law & Contemp. Prob. 183, 196. The official explanation of the referendum given by the secretary of the California Finance Conference, an association of small loan lenders, is that the movement for a referendum was started by a single Los Angeles company whose attorney filed the petition and then called a general meeting of Los Angeles lenders who would be affected by the bills to raise funds to obtain the necessary signatures. Charges were made that the lenders were misrepresenting the referendum. Solici-
The purpose of this article is to set forth the maximum interest and charges which the state constitution and the state legislature permit the twelve different classes of legal lenders to contract for or receive. Before launching into the discussion regarding each class tors were quoted as saying that the petitions would put the loan-sharks out of business or that they would guarantee lower interest rates. It was not found possible to show that the lenders had actually authorized their solicitors to make such misrepresentations. The Los Angeles Better Business Bureau on August 24, 1939, presented to the Criminal Complaints Committee of the Los Angeles Grand Jury evidence of false representations by specific solicitors and also evidence in the form of many affidavits of outright forgery of names, but the grand jury did not have sufficient time within which to act to prevent the measures from going onto the ballot. Governor Olson in a special message to California voters asked that they be certain they understood the issues before they signed any referendum petitions on the personal property brokers' bills. On September 13 the lenders filed a petition containing 148,912 signatures asking for a referendum on the Shelley bill and a petition of 148,874 on the Wollenberg-Phillips bill. A total of 132,573 was required. The lenders in a sworn statement reported to the Secretary of State on September 27 that they had collected and spent a total of $43,795 to obtain names on these petitions. The petitions did not affect the Small Loan Law, which consequently went into effect September 19, 1939. The immediate effect was that many lenders who had theretofore operated as unsecured lenders now qualified as personal property brokers, where they would have at least a temporary and possibly a permanent respite from restrictions as to charges and interest rates.

The proponents of the referendum advanced many confusing arguments, such as that the bills would raise rates, would lower rates, would favor Wall Street, would favor the illegal lender; that the acts were unnecessary; that there was no high-rating or illegal lending in California and that the bills would favor a monopoly of lending by two big Wall Street firms and was the result of a political deal put over by certain social welfare workers. Opposed to them was a group of leading citizens working under the direction of the San Francisco Legal Aid Society who drove home the idea that a vote "YES" on propositions 3 and 4 would eliminate the loan shark. Special mention should be made of the great efforts put forth on behalf of the bills by their authors in the legislature, by the manager and staff of the Better Business Bureaus, Governor Olson, and Attorney General Earl Warren. The Shelley Act won by a vote of 1,807,847 to 724,196 while the almost identical Wollenberg-Phillips Act was approved by a vote of 1,804,597 to 709,967. The victory was all the more remarkable by reason of the fact that the San Francisco Legal Aid Society and other sponsors of the measures worked with practically no funds.

The above data is taken in part from Gisler, loc. cit. supra; Thomas, Small Loan Regulation in California (a thesis submitted in partial satisfaction for the degree of Master of Arts at the University of California, 1940) 161-167; and in part from personal knowledge of the author.

5 The extent of credit and lending business in the United States is indicated by this chart presented by Dr. M. R. Neifeld at the Consumer Credit Conference held at Seattle, Washington, PROCEEDINGS OF THE CONFERENCE ON CONSUMER CREDIT (Univ. of Wash. Nov. 1940) 39.

THE FRAMEWORK OF CONSUMER CREDIT

1937

<table>
<thead>
<tr>
<th>Outstanding Amt. (Billions)</th>
<th>Per Cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. VENDOR CREDIT</td>
<td></td>
</tr>
<tr>
<td>a. Receivables of Retail Merchants (open account and installment)</td>
<td>$3.818</td>
</tr>
<tr>
<td>b. Intermediary Finance Agencies (sales finance companies, etc.)</td>
<td>2.173</td>
</tr>
<tr>
<td>TOTAL VENDOR CREDIT</td>
<td>$5,991</td>
</tr>
</tbody>
</table>
of lender, it is necessary to present a short description of the basic laws, that is, the 1918 initiative Usury Law and the 1934 constitutional amendment, which form a framework into which all other regulatory legislation must fit.

The 1918 Usury Law provides: (1) that interest shall be at the

<table>
<thead>
<tr>
<th>II. TENDER CREDIT</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Curative Professions, Undertakers, etc.)</td>
</tr>
<tr>
<td>III. LENDER CREDIT</td>
</tr>
<tr>
<td>TOTAL CONSUMER CREDIT</td>
</tr>
</tbody>
</table>

The degree to which each group of lenders participates is illustrated by the following chart, presented by Dr. William G. Sutcliffe, Director, Graduate Division, College of Business Administration, Boston University, in the Proceedings, ibid. at 36.

### APPROXIMATE CONSUMER INSTALLMENT INDEBTEDNESS*

EXCEPT INDEBTEDNESS TO RETAILERS

<table>
<thead>
<tr>
<th>Agency or Lender</th>
<th>Number of Offices</th>
<th>Paper Purchased or Amt. Loaned During 1939</th>
<th>Amt. of Paper or Loans Outstanding at End of Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL</td>
<td>30,196</td>
<td>$5,000,983</td>
<td>$3,067,943</td>
</tr>
<tr>
<td>Sales Finance:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales Finance Companies</td>
<td>2,548</td>
<td>1,990,283</td>
<td>1,348,824</td>
</tr>
<tr>
<td>Insured Commercial Banks</td>
<td>10,381</td>
<td>750,000</td>
<td>541,243</td>
</tr>
<tr>
<td>Personal Finance:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other Industrial-banking Companies</td>
<td>231</td>
<td>432,400</td>
<td>210,176</td>
</tr>
<tr>
<td>Personal-finance Companies</td>
<td>4,035</td>
<td>727,300</td>
<td>400,700</td>
</tr>
<tr>
<td>Personal-loan Deps. of Commercial Banks</td>
<td>3,000</td>
<td>592,000</td>
<td>310,000</td>
</tr>
<tr>
<td>Cooperative Credit Unions</td>
<td>8,500</td>
<td>279,000</td>
<td>146,000</td>
</tr>
<tr>
<td>Pawnbrokers</td>
<td>1,500</td>
<td>200,000</td>
<td>93,000</td>
</tr>
</tbody>
</table>


The most recent publication on the small loan problem and its regulation is **COMBATING THE LOAN SHARK** (1941) 8 LAW & CONTEXT. PROB. 1-206. Special mention should be made of the two recently held conferences on consumer credit, one held at the University of Washington, November 13, 14, 1940, sponsored by the College of Economics and Business, The School of Law, The Graduate School of Social Work, The School of Home Economics and the Department of Political Science; the other held January 17, 18, 19, 1940, at the University of Michigan under the joint auspices of the Institute of Public and Social Administration and School of Business Administration of that University. Complete copies of all proceedings are available. See also **Frontiers of Legal Aid Work** (1939) 20S ANNALS 30-49. Leading texts on the subject are Hubachek, **ANNOTATIONS ON SMALL LOAN LAWS** (1938); Neffeld, **THE PERSONAL FINANCE BUSINESS** (1933), **COORDINATE CONSUMER CREDIT** (1936), and **PERSONAL FINANCE COMES OF AGE** (1939); Nugent, **CONSUMER CREDIT AND ECONOMIC STABILITY** (1939); Robinson and Nugent, **REGULATION OF THE SMALL LOAN BUSINESS** (1935); and other works cited in the foregoing.

6 Cal. Stats. 1919, p. lxxxvii. This article will not treat of the law of usury in general, nor what constitutes usury. Below follows a partial digest of writings on the California phases of this subject.

Stone and Thomas, **California's Legislature Faces the Small Loan Problem** (1939) 27 CALIF. L. REV. 286, presented the thesis that it would be possible to draft legislation which could pass the tests of constitutionality in California and still be effective in driving out the loan sharks. The article also summarized the facts showing the need for regulation, traced the history of usury legislation in California and digested the bills then
rate of seven pre cent per annum; (2) that it shall be competent for parties to contract at a rate not exceeding twelve per cent per annum, but any rate exceeding seven per cent "shall be clearly expressed in writing"; and (3) that "Any agreement or contract of any nature in conflict with the provisions of this section [in excess of the rates set out above] shall be null and void as to any agreement or stipulation therein contained to pay interest and . . . the debt can not be declared due until the full period of time it was contracted for, has elapsed." However, the plaintiff is entitled to recover the amount of the principal loaned to the defendant together with costs and attorney's fees provided for in the note. It is the illegal portion of the contract, that is, the portion relative to the interest charge—which is void and unenforceable. (4) The penalties are varied. One who shall have paid more interest than is allowed under the Act may recover from the person who shall have received the same treble the amount of money so paid, and the one or ones so receiving are guilty of a misdemeanor.

The portions of the Law limiting brokers' charges to five per cent on loans of $1,000 and to three per cent on loans for larger sums were declared unconstitutional because the subject of brokers' fees was not mentioned in the title of the Act. On larger loans the interest charges permitted by the valid portions of the Act were high enough to allow the lender to stay within those limits, absorb incidental costs in the item of interest, and still make a profit on the transaction. But in the smaller brackets where the costs of doing business are relatively high and the repayments are made in small installments over a period of time, it was found impossible to lend money if the lender could col- pending before the 1939 legislature. Coffin, Usury in California (1928) 16 CALIF. L. REV. 281, 387, discussing the cases decided through 1927. The effect of the cases decided during the period from 1928 to 1933 is discussed in Hugill, Protection Afforded the Borrower (1932) 20 CALIF. L. REV. 361; 21 ibid. at 72; (1933) ibid. at 287; ibid. at 526.

The future holdings of the courts were anticipated in regard to the invalidity of the rate structure of the early personal property brokers acts in Note (1930) 18 CALIF. L. REV. 542; (1931) 19 ibid. at 213. See also (1932) 21 ibid. at 72. (1930) 18 ibid. at 436, discusses the California cases indicating that usury is not a real defense as against a holder in due course of a negotiable instrument. See also (1928) 16 ibid. at 553; 17 ibid. at 73; (1930) 18 ibid. at 328. In his address before the California State Bar Association, September 4, 1925, entitled Seventy-five Years of California Jurisprudence, Dean Orrin K. McMurray gave a history of California's usury laws. (1925) 13 ibid. at 445, 454-455. Robert E. Stone, in his article on European legal aid societies also discusses usury. Certain European Legal Aid Offices (1936) 25 ibid. at 52.

McConlogue, Usury (1928) 1 So. CALIF. L. REV. 253. See also Haymond, Title Insurance Risks (1928) 1 ibid. at 422; ibid. at 304; 2 ibid. at 195; (1929) ibid. at 502; (1933) 6 ibid. at 346.

7 In re WASHER (1927) 200 Cal. 598, 254 Pac. 951.
lect only the sums allowed by the Law as interest. Hence, the broker-
age system developed as a means of evading the prohibitions of the
Usury Law. The lender would grant a loan only when the borrower
came recommended by his “broker”, and the broker would charge
the borrower a fee for obtaining the loan. These fees generally ran
from twenty-five per cent to fifty per cent to one hundred per cent
of the loan. The Usury Law having been held to limit only interest
charges, and the brokerage charges not being such, and being un-
limited by law, the perfect system for evading the Usury Law was at
hand. The brokerage system made for the wasteful duplication of
two offices, two sets of books and records and two sets of personnel,
often deceptively set up solely for the purpose of extracting the addi-
tional brokerage fee from the borrowers. “Some cases were found, in
which a wife acted as the lender and collected the interest, while the
husband acted as the broker and collected the brokerage fee. Other
cases were found where dummy companies were incorporated and
were given fictitious functions, in order that the semblance of sep-
erate entity might be preserved.”

To give the legislature plenary power to correct the evil situation
which had grown up, the people in 1934 adopted an amendment to
the state constitution. By court decision it has been held that the

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8 Report of the Interim Committee of the Assembly of the State of California for
Legis. Day, 7th Calend. Day, 41, 46. This remarkable report, filed by Assemblymen
Edward Craig, Chairman, Melvyn I. Cronin and Charles W. Lyon, members, will here-
after be referred to as Report of Interim Committee.

“From 1935 to 1939, the interest charges of personal property brokers in California
were not restricted. An analysis of all loans made by personal property brokers during
December, 1938, which is not yet complete as this is being written, suggests that roughly
three-fourths of the loans bore interest rates in excess of 50% per annum, roughly one-
half bore interest rates in excess of 100% per annum, and roughly one-fourth bore in-
terest rates in excess of 200% per annum.” Nugent, The Loan Shark Problem (1941)
8 Law & Contemp. Prob. 3, 12, n. 10. Observations of the author are that the unsecured
lender's average rates were much higher than those of the personal property broker.
See the Proceedings, op. cit. supra note 5, at 64.

9 Cal. Const. art. XX, § 22: “[I] The rate of interest upon the loan or forbear-
ance of any money, goods or things in action, or on accounts after demand or judgment
rendered in any court of the State, shall be seven per cent per annum but it shall be
competent for the parties to any loan or forbearance of any money, goods or things in
action to contract in writing for a rate of interest not exceeding ten per cent per annum.

“[II] No person, association, copartnership or corporation shall by charging any
fee, bonus, commission, discount or other compensation receive from a borrower more
than ten per cent per annum upon any loan or forbearance of any money, goods or things
in action.

“[III] However, none of the above restrictions shall apply to any building and
Usury Law remains intact as to its penal provisions and in other respects, except as modified by the amendment. The amendment consisted of four paragraphs. In the first it reduced the general maximum interest rate to ten per cent, whereas under the Usury Law it stood at twelve per cent. The second paragraph provided that the lender, by charging a bonus, fee or other commission would not be allowed to increase his compensation over the ten per cent allowed in the first paragraph. It is to be noted that neither paragraph in itself placed any limit on the brokerage charges or other expenses a lender might saddle onto the borrower, and in this respect they were no sub-

loan association as defined in and which is operated under that certain act known as the ‘Building and Loan Association Act’, approved May 5, 1931, as amended, or to any corporation incorporated in the manner prescribed in and operating under that certain act entitled ‘An act defining industrial loan companies, providing for their incorporation, powers and supervision’, approved May 18, 1917, as amended, or any corporation incorporated in and operating under that certain act entitled ‘An act defining credit unions, providing for their incorporation, powers, management and supervision’, approved March 31, 1927, as amended or any duly licensed pawnbroker or personal property broker, or any bank as defined in and operating under that certain act known as the ‘Bank Act’, approved March 1, 1909, as amended, or any bank created and operating under and pursuant to any laws of this State or of the United States of America or any nonprofit cooperative association organized under Chapter 4 of Division VI of the Agricultural Code in loaning or advancing money in connection with any activity mentioned in said title or any corporation, association, syndicate, joint stock company, or partnership engaged exclusively in the business of marketing agricultural, horticultural, viticultural, dairy, live stock, poultry and bee products on a cooperative nonprofit basis in loaning or advancing money to the members thereof or in connection with any such business or any corporation securing money or credit from any Federal intermediate credit bank, organized and existing pursuant to the provisions of an act of Congress entitled ‘Agricultural Credits Act of 1923’, as amended in loaning or advancing credit so secured, [a] nor shall any such charge of any said exempted classes of persons be considered in any action or for any purpose as increasing or affecting or as connected with the rate of interest hereinbefore fixed. [b] The Legislature may from time to time prescribe the maximum rate per annum of, or provide for the supervision, or the filing of a schedule of, or in any manner fix, regulate or limit, the fees, bonus, commissions, discounts or other compensation which all or any of the said exempted classes of persons may charge or receive from a borrower in connection with any loan or forbearance of any money, goods or things in action.

“[IV] The provisions of this section shall supersede all provisions of this Constitution and laws enacted thereunder in conflict therewith.”

10 All that the constitutional amendment does is to reduce the maximum permissible rate from 12 per cent to 10 per cent per annum; to exempt certain enumerated classes of lenders from certain of its provisions; and to place in the legislature a certain degree of control over the fixing of charges made by the exempted groups. In its own sphere of operation, and in so far as it establishes different rules from those found in the usury law, the constitutional provision is supreme—but that is the extent of its operation.” Penziner v. West American Finance Co. (1937) 10 Cal. (2d) 160, 177, 74 P. (2d) 252, 260.
stantial advances over the Usury Law. The third paragraph exempted most commercial lenders from the restrictions of the first two paragraphs. The lenders named therein are referred to by the courts and in the literature on the subject as "exempt lenders", and all other lenders, such as individuals making a casual loan, are known as "non-exempt lenders". Only the non-exempt lenders are subject to the constitutional interest limitations. However, this third paragraph did go on to say that the legislature had full power to regulate both exempt lenders' interest and other charges, a provision of the greatest importance, and a power which has been exercised by the legislature and sustained by the courts. The fourth paragraph did not repeal the Usury Law, but only provided that the amendment shall supersede all laws in conflict therewith.

11 "... as to these exempted classes the legislature is given the power to fix the maximum rate of interest they may charge, as well as to supervise said classes in other respects." Matulich v. Marlo Investment Co. (1936) 7 Cal. (2d) 374, 376, 60 P. (2d) 842, 843. Fenziner v. West American Finance Co., supra note 10; Wolf v. Pacific Southwest etc. Corp. (1937) 10 Cal. (2d) 183, 74 P. (2d) 263. "... the Constitution ... specifically exempts personal property brokers from the operation of the Usury Law and gives the legislature power to prescribe methods of regulation and rates." In re Fuller, supra note 3, at 430, 102 P. (2d) at 325. "As to the exempted groups, the legislature was reinvested with the same control over them as it had prior to the enactment of the Usury Law." Ibid. at 434, 102 P. (2d) at 327. As was said by Shaw, Acting P. J., in Crooks v. People's Finance & Thrift Co. (1930) 111 Cal. App. (Supp.) 769, 775, 292 Pac. 1065, 1067, "If there were any uncertainty as to the construction of the Usury Law on this point, which we do not concede, it would be proper to resort, in aid of its interpretation, to the arguments submitted to the voters at the time it was voted upon and adopted as an initiative measure...", so in construing the 1934 amendment it is reasonable to attempt to understand what the people thought they were voting for. And if anything is certain, it is that the people expected the legislature to put an end to loan sharkery in California. There was no printed argument against the 1934 constitutional amendment.

The argument for read in part as follows: "Fifteen years have elapsed in which the Usury Law has been well tested. Its inadequacy is blatantly apparent. Its purpose has not been fulfilled. The loan shark still prospers and collects interest grossly in excess of the specified legal rate.... The reason for the possibility of such evasion is the impracticability of the present law.... Relief may be had through the regulation contemplated by the present enactment. The supervisory control will not be absolute but subject to the vigilant review of the Legislature whose power will equalize the regulatory jurisdiction.

"California remains as the only State with a large population (a condition lucrative to the money lender) which has not provided for the sound principle of regulation .... Only merciless loan sharks ... oppose this measure. It is remedial in its nature and humanitarian in its scope. It paves the way for justice, it seeks to prevent the oppression of the masses ...." Proposed Amendments to Constitution, Propositions and Proposed Laws to be submitted to the Electors of the State of California at the General Election to be held Tuesday, November 6, 1934, together with Arguments Respecting the Same, 18, 19.
Because this amendment may be called upon to meet situations not yet in the front of men's minds, it might be well to spend the next few paragraphs determining just what it does mean. The decision in In re Fuller12 decided (1) that the Usury Law regulated only interest charges, (2) that the constitutional amendment likewise regulated only interest charges, and (3) that the second paragraph of the amendment is designed to include under the term "interest" paid to the lender "all amounts received by the lender under any other name as compensation for his own services" but is not designed to limit "legitimate items of expense". The above holding so clarified the meaning of the amendment that only now can it be analyzed with any definite feeling that one's conclusion is correct. The first portion of the third paragraph presents no great difficulty. It lists the exempt lenders. But the last clause of the first sentence, indicated in footnote nine by the bracket [a] and the last sentence of the paragraph, which immediately follows it, indicated in the footnote by the bracket [b], present many difficulties. In this discussion they are referred to as sentences (a) and (b), respectively.

In (a) we have difficulty in knowing to what the phrase "such charge" refers when nothing has been said about any charges in connection with the exempt lenders. However, the second paragraph discusses charges of a lender by way of compensation, stating that such charges must not be allowed to increase the total charges of the lender to an amount which exceeds ten per cent of the loan. This being the only reference to "charges" preceding sentence (a), it must be that to which it refers. Sentence (a) also stated that those charges, as to exempt lenders, must not "be considered in any action or for any purpose as increasing or affecting or as connected with the rate of interest heretofore fixed." In the preceding portions of the amendment, only in one instance is there a fixed rate, to-wit, in the first paragraph where the rate is fixed at seven per cent in the absence of an agreement fixing it at another figure. Hence we are driven to the conclusion that this sentence means that any charges or compensation moving to or going to the lender must not be permitted to increase or affect the seven per cent rate, or be connected to it, in the absence of an agreement otherwise. By this construction we not only find an intelligible meaning for the sentence, but further find that it is a necessary sentence. For by the first words of the third paragraph,

12 Supra note 3, at 434, 102 P. (2d) at 327.
none of the restrictions of paragraphs one or two were to apply to
the exempt lenders; and this sentence provides an exception, to-wit:
that where there has been no written agreement fixing interest at any
rate other than seven per cent, then the seven per cent rate must in-
clude all other charges going as compensation to the lender. Outside
of that one limitation, exempt lenders are free from all Usury Law
and constitutional restrictions.

Sentence (b) caused concern to some because in listing all the
items that might be regulated by the legislature, it omits the word
"interest"; therefore, it was feared that the legislature may regulate
all charges except "interest". That such a construction is not readily
to be accepted is obvious, for what would be the value of regulation
of charges which left interest uncontrolled? But such a result does not
follow from the sentence. If one will turn for a minute to the first two
paragraphs, he will find therein three definite pronouncements of law,
and by implication, a fourth. They are as follows: In the first para-
graph there is (1) a statement that on judgments, accounts, etc., the
interest is at the rate of seven per cent per annum, (2) that it is com-
petent for the parties to contract in writing for a rate of interest not
exceeding ten per cent per annum. It is to be noted that both mention
"interest", and that "interest" is not mentioned in the second para-
graph. In the second paragraph we find (3) that no person shall, by
charging any fee or other compensation, receive from a borrower
more than ten per cent. In other words the amendment recognizes
two types of charges the lender may make of sums that may go to
him, interest, and other compensation, with the limit, however, that
when added together, they must not in the aggregate exceed ten per
cent. By decision and by implication we know (4) that outlays for
expenses paid to third parties have not been regulated by the amend-
ment. Now the question is, which of the above is the legislature given
power to regulate? If by sentence (b) it had been given power to reg-
ulate only the matters set out in statement (3) above, or the expenses
implied by (4) above, then we would have a situation where it might
be argued that the legislature was without power to regulate in other
respects. The sentence does contain everything set out in statement
(3), so that we know it can regulate all types of payments going to the
lender as other compensation. But it goes beyond that and contains
language and terms not found in the first two paragraphs. It says the
legislature "may prescribe the maximum rate per annum of...com-
pensation". Now other compensation is not fixed on an annual percentage rate. That applies only to interest. That this is so is evidenced by the inclusion of "rate ... per annum" in the first paragraph dealing with interest, and its omission from the second paragraph, which deals with other compensation to the lender. Hence sentence (b) does grant the legislature power to regulate interest as well as other compensation going to the lender. Sentence (b) also says "charge or receive", "in connection with" any loan. In the first two paragraphs there is no reference to charging or receiving money "in connection with" a loan. Words are placed in a constitution to be given an effect. The only way any effect can be given to this extra phrase is to hold that the legislature is endowed with power to regulate the interest to be charged by the exempt lenders, the other compensation to be received by lenders, and the outlays and expenses lenders may be permitted to charge borrowers. Whether the legislature may change the interest rate on judgments or on accounts after demand is a matter with which we are not here concerned.

Summarizing the law as developed from the foregoing, we find that in California lenders may be divided into three major groups: (A) those lenders whose rates and methods of business can be and have been regulated by the legislature; (B) those lenders whose rates and methods of business can be, but have as yet not been regulated by the legislature; and (C) those lenders whose maximum rates of charge are fixed at ten per cent per annum by the constitution and which can be regulated by the legislature only in other respects. Hence, when one looks at a contract calling for interest and other compensation to the lender or other expenses chargeable to the borrower, there is no way of telling whether the contract is usurious without first ascertaining to which class the particular lender belongs, and then determining whether he has violated the law applicable to his type of business.

A. EXEMPT LENDERS WHOSE RATES AND METHODS OF BUSINESS HAVE BEEN REGULATED BY THE LEGISLATURE

1. Personal Property Brokers and Brokers under the 1939 Act.—Personal property brokers are lenders whose loans are secured by chattel mortgages on personal property or wage assignments. They do not take pledges as do pawnbrokers. Under the California law they are not permitted to make unsecured loans, or loans secured only by
CO-MAKERS OR TO LEND ON REAL ESTATE. A "BROKER" IS DIFFERENT FROM A "PERSONAL PROPERTY BROKER", BEING A PERSON WHO IS ENGAGED IN THE BUSINESS OF NEGOTIATING OR PERFORMING ACTS AS A BROKER IN CONNECTION WITH LOANS TO BE MADE BY A PERSONAL PROPERTY BROKER. BOTH BROKERS AND PERSONAL PROPERTY BROKERS ARE REQUIRED TO TAKE OUT LICENSES AND ARE REFERRED TO IN THE ACT AS LICENSEES.

IT IS AN INTERESTING COMMENTARY ON THE EFFECT OF THE 1939 LAW PERMITTING THE LENDER TO CHARGE AN AMOUNT SUFFICIENT TO COVER HIS COSTS OF DOING BUSINESS THAT THE "BROKER" HAS ALMOST CEASED TO EXIST IN CALIFORNIA, AND THE QUESTIONABLE PRACTICES ASSOCIATED WITH THE BROKER SET-UP HAVE GONE AS LENDERS CEASE TO NEED THE SERVICES OF THE BROKERS. THAT THE BROKERS WOULD CEASE TO BE AN IMPORTANT PART OF THE PICTURE WILL BE READILY UNDERSTOOD UPON READING THE SECTIONS GOVERning CHARGES AND RATES.

THE MAXIMUM CHARGES PERMITTED A PERSONAL PROPERTY BROKER AND BROKER, IN THE AGGREGATE, MUST NOT EXCEED TWO AND ONE-HALF PER CENT PER MONTH ON THE FIRST $100, OR MORE THAN TWO PER CENT ON THE EXCESS UP TO $300. IF THE LICENSEE HAS THE SECURITY INSURED IN HIS FAVOR, THE MAXIMUM RATE IS REDUCED TO TWO PER CENT PER MONTH. ALL CHARGES MUST BE ON THE REMAINING OR REDUCED UNPAID BALANCE AND NO INTEREST OR CHARGES CAN BE COLLECTED IN ADVANCE OR COMPOUNDED.

EXCEPTIONS ARE

They are defined in the Act as "... all who are engaged in the business of lending money and taking in the name of the lender, or in any other name, in whole or in part, as security for such loan, any contract or obligation involving the forfeiture of rights in or to personal property, the use and possession of which property is retained by other than the mortgagee or lender, or all who are engaged in the business of lending money and taking in the name of the lender, or in any other name, in whole or in part as security for such loan, any lien on, assignment of, or power of attorney relative to wages, salary, earnings, income or commission." Cal. Stats. 1939, p. 2667, § 2(2). This definition goes back substantially to 1909 when the first Personal Property Brokers' Act was enacted, although the present wording was adopted only in 1933. Cal. Stats. 1933, p. 1496, § 2(2).

Ibid. § 2(7). Practically all the discussion in the text concerning personal property brokers and brokers is applicable to small loan lenders and their brokers, by reason of the similarity of the two laws. See text section "C", and supra note 1.

"Every licensee hereunder who lends any sum of money not to exceed three hundred dollars ($300) in amount may contract for and receive thereon charges at a rate not exceeding two and one-half per centum (2½%) per month on that part of the unpaid principal balance of any loan not in excess of one hundred dollars ($100) and two per centum (2%) per month on any remainder of such unpaid principal balance. If, however, any property securing a loan made by a licensee is insured against loss in favor of the licensee the latter may only contract for and receive thereon charges at a rate not exceeding two per centum (2%) per month on the unpaid principal balance .... No charges on loans made under this act shall be paid, deducted, or received in advance, or compounded. All charges on loans made under this act (a) shall be computed
permitted only for the payment of necessary statutory filing fees, notary fees, and legitimate insurance premiums.\textsuperscript{17}

The drafters of the Act wished to leave no possibility whereby the lender or broker might add charges in addition to those permitted by the Act, so they defined charges to include every item which experience shows lenders make. "The term 'charges' includes the aggregate interest, fees, bonuses, commissions, brokerage, discounts, expenses, and other forms of costs charged, contracted for, or received by a 'personal property broker' or a 'broker' or any other person in connection with the investigating, arranging, negotiating, procuring, guaranteeing, making, servicing, collecting, and enforcing of a loan or forbearance of money, credit, goods, or things in action, or any other service or services rendered."\textsuperscript{18}

A summary of the regulatory features of the Act is here appropriate. The licensee must give the borrower, when the loan is made, a statement containing in full the rate provisions, the terms and maturity dates of the loan, and the nature of the security, if any, and complete receipts specifying how payments were applied and the amount still due; permit payments to be made in advance, and upon final payment mark all obligations "paid" or "cancelled" and release and return mortgages, pledges, and notes. He must take no confession of judgment or power of attorney. Splitting loans to obtain higher rates, wage buying and side contracts as a method of evasion are all prohibited.

\textsuperscript{17} Cal. Stats. 1939, pp. 2667, 2677, § 20, par. 5.

\textsuperscript{18} \textit{Ibid.} at p. 2668, § 2 (5).
A personal property broker and the broker must each obtain a license, the application for which must be accompanied by a $1,000 bond, to be approved by the Corporation Commissioner and running both to the state and to any persons who may have a cause of action against the obligor under the provisions of the Act. If the application and bond are approved, the Commissioner shall issue a license to make loans at the location specified in the application, provided the Commissioner shall find that the applicant is financially responsible, and has such experience, character, and general fitness as to indicate that the business will be operated honestly, fairly and efficiently.

The license must be kept conspicuously posted in the place of business. The licensee must also display a full schedule of charges. No licensee shall transact its business under any other name or at any other place of business. The Commissioner may issue branch licenses. Licenses shall not be transferable nor assignable. No other business may be carried on at the licensed places except by obtaining written permission from the Commissioner.

The licensee shall file annual reports on forms prescribed by the Commissioner, keep such records as will enable the Commissioner to enforce the Act, and preserve all books and documents for at least two years after making a final entry. In order to secure information lawfully required by him, the Commissioner may at any time order an investigation of the loans and businesses of the lender, whether operating under or without authority of the Act. The examiners shall have free access to the offices, books, vaults, etc., of the examinees, and the authority to require the attendance of witnesses and to examine them under oath. An examination is required at least once each year. The costs may be collected from the examinee. Advertising must first be filed with the Commissioner before it can be used.

The Commissioner shall, upon notice and after hearing, revoke or suspend any license, if he shall find that the licensee has failed to obey any of the provisions of the Act or the rules of the Commissioner. The Commissioner's orders are subject to judicial review.  

While the foregoing regulations are strict, it must be remembered there are in the United States unscrupulous persons who will flock to any state lacking such legislation. Experience alone provides the test as to the desirability of a law; and this law, by providing for the keeping of records, the making of annual reports, the check-up by the

10 A summary of sections 2 to 20. Ibid. at pp. 2667-2677.
Commissioner's auditor does make available to the legislature information as to the Laws' operation when it has before it for consideration amendatory or other legislation in this field.

Penalties for violation consist of forfeiture of license, but a forfeiture or surrender of a license does not affect the licensee's civil or criminal liability for acts committed prior to such surrender. As seen above, excess charges either collected or contracted for void the loan. Finally, "Any person and the several members, officers, directors, agents, and employees thereof, who shall violate or participate in the violation of any of the provisions of the rules, orders and regulations of the commissioner, or of this act, shall be guilty of a misdemeanor."\(^{20}\)

The constitutionality of the foregoing type of laws has been upheld in the United States Supreme Court and in about twenty of the states with only one exception.\(^{21}\) The California legislation was attacked as being violative of almost every clause in the state and federal constitutions and in the 1932 and earlier decisions upheld in every point except that fixing the maximum charges.\(^{22}\) The constitutionality of the rate sections is now definitely established.\(^{23}\)

In any new legislation, the question is always asked: How is it working out in practice? In the case of small loan legislation, the tests to apply would be: first, are borrowers able to get the money they need; second, are the lenders able, at the rates prescribed, to make a fair return on their investment; and, third, has bootleg lending developed to any extent? The data collected in the Note at the end of this article definitely establish the first and second of these propositions and negative the existence of any general bootlegging. The only conclusion one can draw is that the laws are successful even beyond the hopes of their sponsors. With such a record it would appear that until the state becomes more accustomed to this legislation, tinkering for the sake of minor improvements should be discouraged. It would seem to accord with sound public policy to stay off of amendments until such time as the main outlines of the law become, in a sense, a part of that great body of law which all people more or less know.

In the future, and when more data become available, it may be that changes could be made in the law along the following lines. (1) It would seem desirable to permit personal property brokers to make

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\(^{20}\) Ibid. at pp. 2671, 2678, § 21.
\(^{22}\) In re Halck (1932) 215 Cal. 500, 11 P. (2d) 389; Beneficial Loan Society, Ltd. v. Haight (1932) 215 Cal. 506, 11 P. (2d) 857.
\(^{23}\) See supra note 11 and text thereto.
unsecured loans. That the reason it was not done was due to the wording of the constitutional amendment has been stated. But it should be noted in passing, however, that although that amendment defines most of the exempt lenders by a reference to a statute which defines them, such is not the case with all of them. The amendment exempts personal property brokers, certain banks and some cooperatives without specifying that they must be such as are defined in a particular statute. From this it might be argued that the legislature has the power to redefine the terms or at least could enlarge or constrict the scope of their operations. But in the case of personal property brokers this would be more difficult, for it apparently is a term that is not used out of California, and the only definition of the term found in the books is in the California Personal Property Brokers’ Law.

The question of security raises two side problems of law. First, is a chattel mortgage on an article of personal adornment valid between the parties? If so, some lenders would like to use such in cases of apparently good moral risks in order to avoid the expense of sending someone to the borrower’s home to list and appraise the security. The other is that of wage assignments. Under the California law, wage assignments for future wages must be in writing and are valid only (a) when for necessaries, (b) when co-signed by the spouse if the assignor is married, or co-signed by the parent or guardian if the applicant is a minor, and (c) for the wages to be earned on the job the employee then has. Suppose the wage assignment so taken is invalid for failure to comply with one or more of the above requirements, or that a wage assignment, valid when taken, becomes worthless due to the employee’s changing jobs. Would this invalidate the loan? These

24 Supra note 1.
25 Supra note 9, par. [III].
26 The term “personal property broker” is not found in R. C. L.; Corpus Juris; American Law Reports; Encyclopaedia of Social Sciences; Encyclopaedia Britannica; or Webster’s New International Unabridged Dictionary, 1934 edition. It is found in 32 Words and Phrases (Perm. ed. 1940) 358, where the definition is taken from Matter of Application of Stephan (1915) 170 Cal. 48, 148 Pac. 196, Ann. Cas. 1916E 617, which in turn quotes the definition found in the California Personal Property Brokers’ Act. A search through the statutes and constitutions of the 48 states and the District of Columbia likewise failed to discover any further use of the term. In other states the equivalent terms are personal finance company, personal loan company, loan broker, money lender, chattel mortgage lender, mortgage loan company, remedial loan company, provident loan company, small loan lender, and the like.
27 There is some authority that such are valid. Note (1936) 104 A. L. R. 1219, 1220.
questions do not seem as yet to have been presented to the courts. 20

(2) Under the present law there is no express rate limit on loans above $300. But this absence of stated restriction should not be interpreted as a license to exceed the statutory limits. Even now, if a lender should make a consistent practice of making many loans in sums over $300 in order to evade the Act, the Commissioner, through his auditor’s examination, would soon discover this and under the powers given him under the Act, revoke the lender’s license. But eventually the law should be amended to provide specifically a maximum rate for loans on sums over $300. 30

(3) Under the present law, a lender, to obtain a license, need only show that he has financial responsibility, experience, character and general fitness such as to command the confidence of the community and to warrant belief that the business will be operated honestly, fairly and efficiently. Some would add other requirements. Speaking of former conditions it was said “that the majority of the violations of law and the highest rates prevailed among the operators with small capital... Protection of the borrower demands that those who engage in the business of lending money should be financially secure and able to carry on business with a sufficient reserve to meet emergency conditions and permit a normal net return without exacting excessive charges. Inadequate capital leads to abuses of the borrower, to increased rates, to oppressive collection methods and to undesirable business methods generally. Moreover the lender with a small capital is more inclined to disregard regulation and flout the law since he has no substantial investment under it. Your committee believes that any person seeking a license should be required to have no less than $25,000 capital for investment as a condition precedent to the obtaining of a license as a small loan lender.” 31

20 That wage assignments do not have the validity that some have contended for them is indicated by Local Loan Co. v. Hunt (1934) 292 U. S. 234.

30 The limit was placed at $300 because such a limit is general in most other states and decisions upholding those laws have frequently emphasized the fact that $300 was a reasonable classification of loans, separating those probably of borrowers who needed protection from those of persons who are more likely to be able to take care of themselves. On the whole it is probably true that a lender is able, in the absence of legislation, to exact more from the small borrower needing money immediately for some emergency than he would be able to exact from a man desiring a larger sum. Members of the latter class presumably have banking or other connections that give them some bargaining power. The drafters of the law placed the limit at $300 where the largest amount of judicial opinion existed to support them.

“Indiscriminate licensing of lenders leads to grave abuses. Extreme competition leads to objectionable advertising, to irritable ‘sales’ methods and to lowering of business ethics and unnecessary duplication of overhead.” Just as it is unwholesome for depositors to have a community overstaffed with banks, so it is argued that it is undesirable for the borrowing community to be oversupplied with lenders, and in one case as in the other, before a new financial institution may be opened, it should be required to obtain from the supervising authority a certificate of need and public convenience. Since, however, the present regulations seem to have eliminated the objectionable lender, it is probably unnecessary at the present time to push the above recommendations.

(4) Upon theoretical considerations it would seem that it ought to be possible to provide a flat minimum charge of, say, fifty cents per loan per month, as is the case in the pawnbrokers’ law, for very small loans. Such legislation would have to be carefully worded to prevent its becoming an inducement to split loans into small sums in order to obtain higher charges from borrowers, and it ought not to be so cumbersome as to make the law difficult to understand or to create other ambiguities. Up to the present time no state has been able to draft workable legislation permitting minimum fees for any class of lender other than the pawnbroker. As a matter of fact, it is almost impossible to find a loan which has actually carried a charge less than such a minimum, so the suggestion to amend the law in this direction appears to be much ado about nothing. For the rare instance, the answer is that all merchants expect to make a certain number of sales where the amount involved is so small that it yields no profit, but such sales are justified on the ground that they do create good-will.

(5) The present Act permits lenders to charge extra for insurance and the Commissioner by rule has had to confine this insurance as acceptable only for fire, theft, collision and comprehensive in preventing this exception from becoming a loophole for the evasion of the law. But to date no better provision on the subject seems to have been written than that provided in the Act.

(6) The last general criticism of the Act is that in the event of a violation of the law by the lender, it makes the loan void whereas the Usury Law only makes a loan void as to interest. The answer is that if the legislature had been given power to regulate interest only, then

32 Ibid. at 49.
33 Cal. Stats. 1939, pp. 2667, 2677, § 20, par. 5.
it might be that it would not have had power to provide a greater penalty than that set out in the Usury Law. But the constitutional amendment clearly permits the legislature to regulate both interest and other charges and for violation of those matters the legislature has power to provide the penalties it deems adequate. Hence, it has power to declare the principal as well as the interest uncollectible in case the lender exceeds the maximum charges permitted by law.

2. The Industrial Loan Companies.—Cooperative credit societies developed in European countries about 100 years ago. The first on this continent developed in Quebec. From these beginnings developed two different lending institutions, the credit union, to be discussed in the next section, and the industrial loan company. The industrial loan company was the product of Arthur J. Morris, a bank attorney in Norfolk, Virginia, who, from his experiences as such, knew that banking credit facilities were not available to borrowers in the lower income groups. His plan called for the creation of a corporation to operate as a bank. The institution would issue three types of paper: (1) common stock to its stockholders, (2) interest bearing notes to investors, and (3) certificates to be sold to borrowers on the installment plan at the time of borrowing. When a party wished to secure a loan, he would pay six per cent discount, produce two co-signers or endorsers, and agree to buy an investment certificate. These investment certificates were to be paid for on the installment plan, remaining with the bank as a pledge or security for the payment of the loan, would bear no interest until paid for, and when paid for, could be applied in full to the repayment of the loan. When so applied, the borrower’s note would be returned to him, marked fully paid and the investment certificate cancelled. In addition, the lender would make a charge to cover overhead and investigating fees, which was permissible under the laws of Virginia. This ingenious scheme enabled the bank to lend money without apparently violating the six per cent maximum interest usury laws. Actually, if the loan were repaid, say in twelve equal monthly installments, the six per cent discount amounted to interest at about 12.4 per cent if the borrower received $94 and paid back $100, or to about 11.2 per cent interest if he received $100 and agreed to pay back $106.

34 See text to notes 9, 10 and 11, supra.
Some states permitted these corporations to operate as banks while others did not. Even when statutes permitted them to operate, courts on occasion would hold that making a loan at six per cent discount in combination with a requirement that the borrower had to buy a certificate on an installment plan, receiving no credit in the way of interest for payments made on the certificate or in the way of reduction of principal of the loan, violated six per cent and other similar rate usury laws. But in most places the device, although a subterfuge, was held valid.

Although the rate structure of these lenders ought not to be advertised as six per cent any more than banks should advertise their discount rates as six per cent interest, nevertheless, genuinely sincerely minded people who wished to provide lending facilities for the poorer people as a method of driving out the loan shark felt compelled to follow this device where the law limited interest on loans to a six per cent rate. When the volume of business is sufficient and where the loans are larger in amount, many of the companies have voluntarily reduced their charges considerably. At present there are about 400 such institutions in the United States, doing a business of about $500,000,000 annually.

About twenty-five years ago, companies promoting Morris plan institutions organized many in California, sometimes under the name Morris Plan, at other times with the word Fidelity in the name, but most often under the name People's Finance and Thrift Company, Industrial Loan, or the like. To make it possible for them to operate in California, the Industrial Loan Company Act was passed in 1917.36 It proved attractive to prospective incorporators due to the possibilities of profit combined with an apparent low rate of charge to the borrower. After taking their fees, the promoters left the respective institutions to the management of the local owners. In a few cases they succeeded in carrying out management policies that enabled them to prosper; but in many cases the owners, being inexperienced in the small loan business, lost money, so that in the course of the last twenty years, a majority went out of business. Most all who survived do a large and desirable business, rendering a good service to that group in the community which they serve.

The California law, although amended several times, still substan-

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tially conforms to the 1917 plan. Its provisions are designed to protect the investor and look towards preserving the solvency of the institution rather than the protection of the borrower. The activities of the lenders embrace three distinct fields of financing—sales finance, cash loans, and business loans. They may make secured or unsecured loans. They advertise for business and have been held by the courts to be financial institutions which compete with banks. The California law, however, differs in a few respects from the general pattern. (1) A company may not receive deposits nor issue certificates of deposit, thus differentiating it from a bank, and (2) its certificates issued to borrowers contemporaneously with the making of the loan must be in the form prescribed by the Corporation Commissioner, and in general the business must be operated in conformity to rules and regulations prescribed by the Commissioner.

Section 4 of the Act permits an industrial loan company to deduct interest in advance at the rate of six per cent per annum and in addition to charge and deduct in advance two dollars on every fifty dollars or fraction thereof loaned. By the amendment passed in the special session of 1940, it was further provided that the total taken in advance for interest and other compensation shall not exceed one per cent of the face value of the loan for each full month for which the loan is made, and that if the loan is made for a period of less than one month, then not over one-thirtieth of one per cent for each day.


38 It is probable that the cases holding the interest rates of the Personal Property Brokers' Acts invalid had the effect of declaring invalid those of the Industrial Loan Company Act. See cases cited supra note 22. This also was the opinion of the Attorney General as evidenced by his letter of July 15, 1931, to the Commissioner of Corporations. Camalek, Digest of Personal Finance Laws, ANN. (1932) 91. In that event their charges were usurious under the Usury Law from 1918 to the time of the adoption of the constitutional amendment in 1934. Accord, Report of Interim Committee, op. cit. supra note 8, at 56; Connor v. Minier (1930) 109 Cal. App. 770, 288 Pac. 23.

39 Cal. Stats. 1st Extraordinary Sess. 1940, c. 34: "Sec. 1. Section 4 of the act cited in the title hereof is hereby amended to read as follows:

"Sec. 4. Every corporation under the provision of this act shall have power: [a] subject to the supervision and control of the Corporation Commissioner of the State of California:

"First—To loan money on personal security, or otherwise, and to deduct interest therefor in advance at the rate of six per cent per annum, or less, and, in addition, to receive and [b] shall at the discretion of the Corporation Commissioner of the State of California, issue and require uniform weekly or monthly installments on its certificates of investment, purchased by the borrower simultaneously with the said loan transaction
Most of the provisions in the Act are for the protection of the investor. There is not much to be said about the Act as a regulation of or otherwise, and pledged with the corporation as security for the said loan, with or without an allowance of interest on such installments.

"Second—To sell or negotiate choses in action [b] either in certificates, or in certificates in receipt book form, for the payment of money at any time, either fixed or uncertain, and to receive payments therefor in installments or otherwise, with or without an allowance of interest upon such installments. Nothing herein contained shall be construed to authorize corporations hereunder to receive deposits or to issue certificates of deposit. The issuance of choses in action herein authorized shall be approved as to form by the Commissioner of Corporations and shall bear the indorsement on the face of the instrument, ‘this is not a certificate of deposit’.

"Third—In addition to the interest rate charged, to charge and deduct in advance for the making of any loan pursuant to this section, the sum of [c] two dollars, or less, on every fifty dollars, or fraction thereof loaned, as [d] full and earned compensation for services of all kinds and character, [e] including brokerage, in making the loan; but the total amount taken in advance for interest and such other compensation, including brokerage, (a) shall in no event exceed one per cent of the face amount of the loan for each full month for which the loan is made, and (b) if the loan is made for a period of less than one month, shall in no event exceed one-thirtieth of one per cent of the face amount of the loan for each day for which the loan is made.

"Interest after maturity of the loan may equal but shall not exceed the rate of one percent per month on the unpaid amount of the loan.

"The total interest and other compensation of an industrial loan company and of a broker or third party negotiator charged, contracted for or received by the company and the broker or negotiator in connection with a loan made by the company shall not exceed the maximum rate of interest and other compensation herein permitted.

"No charge shall be collected unless a loan shall have been made.

"Fourth—To establish offices, or places of business within the county in which its principal place of business is located, but not elsewhere.

"[f] Fifth—To purchase, sell or discount choses in action, secured or unsecured, chattel mortgages or conditional sales contracts, which shall have a maturity within two years from the date of said purchase and such purchase, sale or discount shall not be construed to be either a loan or an investment of funds as such terms are used and defined under the provisions of this act.

"In addition to powers herein enumerated, every corporation, under the provisions of this act, shall have the general powers conferred upon corporations by Chapter III, Title I, Part IV, Division First, of the Civil Code, except as herein otherwise provided.

"Sec. 2. The title of said act is hereby amended to read as follows:

"An act defining industrial loan companies; providing for their incorporation, powers and supervision; and regulating the rates of interest and other charges of industrial loan companies and brokers or third party negotiators in connection with loans made by such companies.” (Italics added.)

Prior to each italicized section is a letter in brackets. By referring to the corresponding letter below, one may learn the date each change took effect.

[c] Cal. Stats. 1921, p. 729. This amendment also eliminated the $5.00 maximum limit on all charges other than the six per cent discount.
[d] Cal. Stats. 1935, p. 2055. Prior to this amendment lenders were not allowed to make extra charges for drawing papers, taking acknowledgments and the like, in addition to the $2.00 charges. This portion was restated differently by the 1940 amendment.
the lender. By reason of rule making power conferred, the Corpora-
tion Commissioner has devised as effective a set of rules for industrial
loan companies as could be hoped for.

That the Act permits abuses is well known. In December, 1940, a
Los Angeles company made over 8000 loans, mostly around $15 each
and none over $30, each for a two-week period. The borrowers were
largely Mexicans, Negroes and others from the lowest economic
strata. All that the lender desired was to get them once on its books,
for it knew they could never raise $15 to repay him all at once. So it
continued to exact two dollars from each every two weeks. Within a
few months it had back the entire principal of the loan, but continued
to bruise the borrowers around with its trained collectors so as to
make sure they would never miss the two dollar bi-weekly payment.40
This is one attempt to put a loophole in the California system that
should be stopped at this session of the legislature.

The Act has many weaknesses. One of the greatest is the failure
to make it mandatory to file all advertising with the Commissioner,
subject to his disapproval, prior to use, as found in the Personal Prop-
erty Brokers', California Small Loan and Corporate Securities Acts.
In fact, all of the salutary provisions for the protection of borrowers
and the regulation of lenders might well be lifted bodily from the Per-
sonal Property Brokers' Act for inclusion in the Industrial Loan Act.

In addition to the general defect, there are specific objections to
certain features. The Act permits companies to “purchase, sell or dis-
count choses in action”, including chattel mortgages and conditional
sales contracts, and it is provided that such a transaction “shall not
be construed to be a . . . loan”.41 If this is merely the power to deal in
commercial paper, subject to usury and other applicable laws, such

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40 Supra note 39.

41 Supra note 39.
as is possessed by individuals and ordinary corporations, it may not be seriously abused. On the other hand, if the effect of the quoted language is to free actual loan transactions from interest restrictions when they are cast in the form of purchases or sales or discounts of choses in action, almost unrestrained loan sharkery would be facilitated, through the resulting suspension of the operation of the customary rule permitting the introduction of evidence to establish the true character of the transaction as a loan of money. Among the numerous common types of devices that could be adapted to permit the exaction of excessive charges for what are actually loans of money are wage buying, check selling, the sale of marketable securities at high prices on credit for resale by the borrower, the purchase of securities of the borrower at a low price subject to his right to repurchase at a higher price and the sale of merchandise coupons as a condition of granting loans.\textsuperscript{42}

Pursuant to such powers as are conferred upon him, the Corporation Commissioner in the public interest has promulgated rules to govern their loan practices. He requires them to use installment investment certificates in connection with each loan transaction; to furnish to the borrower upon demand full information as to his current position; that they shall not resort directly or indirectly to any subterfuge such as “flipping” loans to defeat the rate sections of the Act, or otherwise to engage in any practice which results in circumventing the usury statutes of the state.\textsuperscript{43}

The foregoing rules leave much to be desired in three respects. First, they have to be general when they ought to be specific as are those regulating personal property brokers. Secondly, the statute only confers power on the Commissioner to issue rules, as in the case of corporations, consequently attempts to enforce a rule are likely to lead to resistance in the court to test the power of the Commissioner in such cases. The third and greatest defect is that the Act

\textsuperscript{42} That such fears are not unwarranted is evidenced by legislation in other states declaring such transactions to be loans. Modern Finance Co. v. Holz (Mass., Nov. 15, 1940) 29 N. E. (2d) 922.

\textsuperscript{43} CAL. DIV. OF CORPS., DEPT. OF INVESTMENT, SPECIAL RULES FOR INDUST. LOAN COS. (Dec. 1, 1940). “Flipping” is a term used in the trade to indicate the renewal of a loan at frequent intervals. Another practice which the Corporation Commissioner is attempting to stamp out is reached by the following rule: “An industrial loan company shall refrain from making loans in repeated and successive transactions where said loans exceed slightly $50 or multiples of $50.00, and when proof of such practice is presented to the Commissioner appropriate action shall be taken by him to halt any subterfuge to violate the usury or regulatory statutes of the State of California.” Ibid. § 7.
contains no penalties. Nowhere in it is there anything to the effect that a company guilty of overcharging or usury or false advertising or sharp practices is guilty of a misdemeanor, or that the loan or the interest provision of the loan contract is void. The most the Act expressly permits is the taking over of an office upon its violation of one of the specific provisions of the Act or proper rules of the Commissioner.

By implication and by incorporation by reference the Act does grant some valuable and important additional powers to the Commissioner. The rate section states that the lender has power to make charges to the borrower “subject to the supervision and control of the Corporation Commissioner. . . .” Another section provides that the companies shall be subject to the provisions of the Corporate Securities Act. The Commissioner’s right to issue, amend, alter or revoke permits authorizing issuance of investment certificates is reiterated in section 12. By virtue of these provisions the Commissioner must make a thorough investigation of the character and fitness of the applicant and the scheme under which he proposes to do business before granting a license. Hence the Commissioner may be able to check many loan sharks before they can get started. Under the further power of the Commissioner to examine the books of the permittees, he will discover violations of law, and may exercise his power by altering, amending or revoking the companies’ permits. But as indicated in the preceding paragraph, the absence of clear-cut pronouncements of legislative policy by specific provisions of the Act, and the failure to prescribe penalties for violations thereof, will require the courts to give the provisions referred to in this paragraph a broad and liberal interpretation in favor of the borrowing public.

It is a general principle that legislation which is general or remedial in nature is to be broadly construed in order to bring within it all transactions and persons which may be reasonably subject to it. Conversely, exemptions to such legislation, and especially exceptions which grant special privileges, are to be strictly construed so as to apply only to those cases clearly coming within the letter and the spirit of the exception. All lenders and loan transactions must, therefore, be governed by the general provisions of the Usury Law and the constitution unless they can be brought within one of the exemptions. In these laws, exceptions while numerous are narrowly defined and

44 Cal. Stats. 1st Extraordinary Sess. 1940, c. 34, § 4; Cal. Stats. 1939, pp. 1518, 1519, §§ 8, 10; Cal. Stats. 1933, pp. 584, 586, § 11a.
are conditioned upon compliance with the various acts governing the excepted classes.

The burden of showing that the lender or loan transaction comes within the exception is on the lender. This burden is not met by a mere claim to exemption or by showing colorable compliance with formal requirements upon which the exception is conditioned. In order to come within the exemption given to industrial loan companies the lender must not only be incorporated under the Industrial Loan Companies Act, but must also be "operating under that" Act. Those requirements are imposed by the constitutional amendment. The law is both general and remedial, a police regulation strictly in the public interest, and a heavy burden is imposed upon any lender claiming to be an exception to such a general constitutional provision.

Where a lender does not issue certificates, where he renews the loan every few weeks to gain increased charges of $2 per $50 or fraction loaned, where he does not see that the borrowings are reduced by periodic regular installment repayments, where in short he engages in the worst form of loan sharkery, he is not "operating under" the Industrial Loan Company Act. Rather he is operating as a loan shark in fact, but falsely claiming to be an industrial loan company. Even if he did issue certificates, nevertheless he could not claim the benefit of the exemption if in fact the borrower did not know he was buying a certificate. In other words, the certificate formula must be fully and honestly carried out to bring the operator within the protection of the exemption. If the borrower should ask what he is signing and be told "It is just a legal requirement" without explaining to him the twofold nature of the transaction, there is no compliance with the law.45

The procedure permitted industrial loan companies of charging six per cent per annum in advance, thereby permitting them to advertise loans at the rate of six per cent whereas other lenders, who may be actually charging no more, are compelled to advertise the true rate of interest, is a privilege. Although from 1918 to 1934 such lending was probably illegal,46 it has been permitted since the latter date, but

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46 Supra note 38. Cf. General Motors Corp. v. Federal Trade Comm. (C. C. A. 2d, 1940) 114 F. (2d) 33, 35, where the court upheld the F. T. C. in ordering the General Motors Acceptance Corp. to cease and desist from advertising their 6% discount rate as a "6% plan". The court held that there was evidence to support the findings of the Commission that the advertisements had "the capacity and tendency to mislead and deceive ... a substantial part of the purchasing public into the erroneous and mistaken belief
it must be assumed that the permission is conditioned upon general and fair compliance with the laws of the state governing interest rates and charges. The service fee was intended to cover the legitimate actual expense of making a loan. This expense results from looking up the borrower’s credit standing and his security. Obviously it does not occur with each bi-weekly or monthly renewal.

The conclusion is that a lender who has incorporated under the Industrial Loan Act merely for the purpose of not having to do business under the Personal Property Brokers’ Act or the Small Loan Law and without the intention of carrying on an orthodox industrial loan business, is not entitled to the protection of that Act and is therefore subject to the 1918 Usury Law and to the Personal Property Brokers’ Act and the California Small Loan Law. Courts and juries should be able to recognize fraud when it is so apparent. He has not met the burden of proving that he is “operating under” the Industrial Loan Companies Act.

If in addition to the above it can be shown that the lenders had violated the Act in other states, that they had formerly operated as loan sharks in this state, that they purposely sought a loophole by which they could under cover of law continue their practices, a criminal conspiracy is made out when such plans are followed by overt acts. If the Act were such that it could not be construed as restricting lenders along the lines herein suggested, it then discriminates unfairly in favor of certain lenders.

Inasmuch as small loan lending is competitive, there seems to be every advantage to making uniform the rules governing the lenders. It makes for fair competition and for facility in inspection, detection of violations and enforcement generally. A precedent has been set by the 1939 Personal Property Brokers’ Acts and Small Loan Acts, which are alike in rate provisions and regulatory requirements. Their constitutionality has been approved; they have been found workable in practice. It would be consistent with public policy to take those regulations and that rate structure bodily and insert them in the Industrial Loan Companies Act. It is true that those laws permit a much higher rate of charge than is now the practice amongst most industrial loan companies, but that in no way prevents them from continu-

that the said “6%”... plan ... contemplates a simple interest charge of 6% per annum upon the deferred and unpaid balance of the purchase price ... when ... in fact that total of the credit charge, computed in accordance with said “6%”... plan, amounts to approximately 11½% simple interest per annum upon the deferred and unpaid balance...”
ing to underbid their competitors, and it does make a ceiling beyond which loan sharks cannot go who might happen to get into their fold. All small loan companies are now under the supervision of the Corporation Commissioner. By making the rates and regulations of all identical, administration is facilitated.

3. Credit Unions.—In California, credit unions may be incorporated either under the federal or the California law. Those under state law may not loan money at a rate exceeding one per cent per month, inclusive of all charges. However, insurance costs are not deemed a charge incident to the making of the loan. Loans to non-members are prohibited although certain types of investments are permitted.

4. Pawnbrokers.—Pawnbrokers cannot charge more than two per cent per month on loans of $100 or less or more than one per cent per month on the excess over $100, “except that a minimum charge of fifty cents per month may be made in any case where the monthly charge permitted by this section would otherwise be less than fifty cents.” No other charges of any kind are permitted. Pledged articles must be kept for at least one year beyond the redemption date, except that clothes, furs, suitcases and the like need be kept for six months only. At the end of such periods of time, the pawnbroker may keep the pledges as his own and is under no duty to have a sale or to foreclose. Only duly licensed pawnbrokers are entitled to the privileges of this statute.

B. EXEMPT UNREGULATED LENDERS

There is no limit fixed as yet by the legislature upon the interest or other charges that may be imposed upon the borrower by the banks, building and loan organizations and certain cooperatives.

C. NON-EXEMPT LENDERS

Every individual and corporation in the state which cannot qualify as an exempt lender under the provisions of the constitution is a non-exempt lender and is subject to the limitations set out in the first

50 For full list of other exempt lenders, see text of constitutional amendment, supra note 9.
two paragraphs of the constitutional amendment and, for violations thereof, to the penalties prescribed by the Usury Law.

Unless we except the industrial loan company, nowhere amongst the list of exempt lenders is provision made for that class of lenders who lend small sums without security. The pawnbroker and the personal property broker are mentioned, but not the small loan lender as such. There is a need for such lenders. Their relative costs of doing business are high and their risks considerable. In other states one type of lender may make both kinds of loans, but because it is doubtful if the constitution would permit the legislature to re-define personal property brokers so as to include a class of lenders not so included in the definition at the time the constitutional amendment took effect, the drafters of the bills preferred not to change the definition. However, the supreme court had suggested a solution which they followed, that is, a statute which allows the legal rate fixed by the Usury Law or the constitution and yet limits the service or expense charges to the actual outlay, not to exceed a definite limit. This suggestion was incorporated in and forms the base of the rate structure set forth in the California Small Loan Acts.\footnote{Beneficial Loan Society, Ltd. v. Haight, \textit{supra} note 22. See Stone and Thomas, \textit{op. cit. supra} note 6, at 308.}

Substantially, the law is identical with the Personal Property Brokers' Acts, serving to regulate those who lend without security. The maximum charges permitted in each are the same.\footnote{Cal. Stats. 1939, pp. 2667, 2674, § 17; Cal. Stats. 1939, pp. 2679, 2686, § 16.}

The only major difference between the acts is that the agreement to repay the principal of a loan in violation of the Personal Property Brokers' Act is void whereas in the Small Loan Acts only the obligation to pay interest and charges is void.\footnote{Cal. Stats. 1939, pp. 2667, 2677, § 20; Cal. Stats. 1939, pp. 2679, 2689, § 20.}

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There is complaint that the loan laws in California are too many and too long.\footnote{There are 29 laws in the state, including the constitutional amendment. They occupy 92 pages in the statutes. To date 35 bills and constitutional amendments have been introduced at the 1941 session of the legislature on the matters directly discussed in this article.} Nevertheless it must be kept in mind that borrowers vary to an extreme degree in their needs, and in their conditions and that the kind of loan suitable for one will not be practical for another. Hence there must be a considerable variety of lending. Further, the lending business historically has attracted some of society's most un-
scrupulous individuals who are avaricious, resourceful and daring. The great variety of loan services required by borrowers makes it unusually easy for the vicious lender to find ways to avoid usury restrictions. Hence there will always be a need for comprehensive, detailed and drastic regulatory small loan laws, and for a wide awake administration to enforce them. Further, the problem of drafting statutes to accomplish these objectives has been unusually difficult in California, for the 1918 Usury Law and the 1934 constitutional amendment have compelled the legislature to enact many laws to accomplish objectives, which without those limitations could have been achieved with the use of much fewer words.\footnote{The author hopes to be able to write an article some time in the future suggesting a means whereby the laws may be simplified.}

No discussion of small loan legislation in California would be complete without saying a word about the service rendered the thousands of needy borrowers in this state by the small loan lenders. It is important that a person who needs funds be able to obtain them and there should be in society some fair way to insure this. The hundreds of lenders of whom we never hear render this service; without their civic loyalty and cooperation, without their daily practice of living up to the requirements of these laws in both letter and spirit, the laws described here could not possibly accomplish their purpose.

The reports the lenders make to the Corporation Commissioner indicate that they are making a satisfactory profit. The survey reported immediately following indicates that except for those who ought to go on relief, all residents are able when in need to obtain funds at fair prices. Outside of the loopholes found to exist in the Industrial Loan Companies Act, not much more could be asked of loan laws.

**NOTE**

**Operation of the California Laws Regulating Personal Property Brokers**

When the 1939 legislature adopted the existing Personal Property Brokers' Acts and Small Loan Acts it was recognized that the permissible charges of $2\frac{1}{2}\%$ per month on the first $100$ and $2\%$ per month on the balance between $100$ and $300$ probably represented the borderline between rates which would allow legitimate small loan operations and those which would close legal channels to a portion of the borrowing public.

The new laws have been in effect somewhat more than a year, and already marked changes can be noted. Interest rates paid by borrowers are much lower. A number of loan offices have closed, but others have opened. Few instances of violations have been reported.
Regulatory laws of this type are intended to protect certain members of society, so it is not enough to note that those persons coming under regulation have continued to do business. It is also important to take stock of what is happening to those for whose protection the laws originally were intended. In this case, that means the borrowers.

Admittedly, no public protest prompted such a study. Better Business Bureaus reported, for instance, that to their knowledge the law was working as its sponsors had hoped and no complaints were being made.

Certain lenders, however, took issue with the new rate of charges. A number of them reported that the interest rates were so low that persons seeking loans of $50 or less could not be served.

In order to investigate the situation, support was solicited from the Russell Sage Foundation and two investigators were employed to interview persons who had sought a loan from a personal property broker and been rejected. One of these investigators had worked for a time for a lending firm and was acquainted with their operations. The second man was a trained social worker.

The relations between loan applicants and finance companies are confidential in character, but through a special arrangement involving the cooperation of credit agencies it was possible to obtain the names of approximately 250 persons whose loan applications had been rejected by personal property brokers during the last quarter of 1940. In order to minimize the effect of the lending policy of any individual firm, care was taken to obtain "turn downs" from a number of lending companies.

Slightly more than 100 persons, selected at random, were interviewed individually. All of those interviewed were residents of Oakland or Berkeley, California.

Results of this survey as a commentary on operation of the existing small loan laws in California are presented in the following paragraphs, but certain qualifications must he noted. It is not contended that those persons interviewed represent a scientific sample of the entire borrowing public in California. Nor is it asserted that Berkeley and Oakland are "typical" California areas. It may be there are no truly "typical" localities. The sample taken was small, but agreement in the results attained by the two interviewers, who worked independently of each other, may offer some indication that extension of the same survey to cover a larger number of persons would offer somewhat similar results.

Data obtained from credit files showed that, of the 250 persons whose applications were rejected, 41% had sought loans of $50 or less, 30% had requested $50 to $100, and almost 10% had wanted more than $250. Among the applicants interviewed, 45% had originally applied for a loan of $50 or less, 33% had requested $51 to $100, and 6% more than $250. Statistically, the mean size of loan sought was $109.45, the median, $75, and the mode, $50.

Despite their initial rejection, more than half of the persons interviewed had been able to borrow the money from another source. Of 11 persons who had originally requested loans of $25 or less, however, only 2 had been able to obtain the money elsewhere, and one of these had borrowed from friends. The second person's application was accepted by another finance company. Sixteen of the 36 persons seeking $25 to $50 were able to obtain money elsewhere, but 8 of these ultimately borrowed more than they originally had requested. Of 4 persons who had first attempted to borrow $30 each, 2 obtained loans of $50, one of $75, and another of $225. At least 3 of these 4 obtained the money from another personal property broker. Of 4 persons who had originally applied for $50 loans, 3 obtained $100 and the fourth $200. One person who had originally asked for $35, was able to borrow $30 from a bank, and another applicant who had sought $50 originally succeeded in obtaining $10 from an industrial loan bank.

Of the 52 interviewees who had succeeded in obtaining money after first being rejected, 22 had obtained the sum originally requested, while 15 ultimately borrowed a larger sum, and 15 a smaller sum.
The tendency was for those persons who had originally sought small sums finally to borrow larger amounts, and for those who had sought larger sums to obtain smaller amounts. Of the 18 applicants for $50 or less, seven obtained the sum originally requested, 9 ultimately borrowed more, and 2 less. Of the 3 who originally had sought $300, one obtained $200 from a bank, the second $150 from a remedial loan office, and the third $100 from a personal property broker.

Of 15 cases in which the amount actually obtained was larger than that listed in the first rejected loan application, the money was provided in five instances by other personal property brokers, in three instances by banks, in one case by a remedial loan office, and in another case by an industrial loan bank. Friends provided the source in one case, and in four instances the source was not disclosed. In two of the cases in which personal property brokers made the loans, smaller loans were obtained at about the same time from industrial loan banks.

Of the 15 instances in which the amount ultimately borrowed was less than originally sought, the funds were provided by banks in three cases, by industrial loan companies in 6 cases, by personal property brokers in two cases, by a remedial loan office in one case, and by an insurance policy loan in one instance. Sources were not disclosed in two cases.

More than three-fifths of the interviewed loan applicants had had previous borrowing experience, and, significantly enough, those with such experience fared better than those who had no borrowing background when it came to obtaining money from other sources.

With respect to the purposes for which loans were sought, no significant differences existed between those who were able to get the money elsewhere and those who were not. The most popular reason for borrowing was to consolidate existing obligations. The other reasons most frequently given were the payment of current expenses, purchase of an automobile and the payment of medical or hospital bills.

Some relationship existed between the reasons given for the original rejection of the application and the ability of that applicant to obtain funds elsewhere. Approximately half of those originally rejected because of insufficient income or poor credit risk were able to obtain a loan elsewhere. On the other hand, of 25 rejected because of unsteady work or lack of tenure in their present job, only seven obtained money elsewhere. Of 11 persons refused loans because of lack of security, 8 obtained money elsewhere, and of three turned down because they were in business for themselves, 2 were able to obtain money from another source.

Without exception, those persons originally rejected because of lack of identification, of youth, of falsehood about marital status, and for similar reasons, all were able to get money elsewhere.

Among those interviewed, office workers were best able to utilize other lending sources. Of 10 office workers originally rejected, 9 obtained loans elsewhere. Somewhat more than half of the railroad workers, salesmen and independent business men, also were able to obtain loans. Less than half of the skilled craftsmen, laborers, truck drivers or persons in service occupations were so able.

More than half of those persons rejected were either single or childless. Some 43% were in their 20's and 34% in their 30's. Five of every 6 persons interviewed were males, and an equal proportion were members of the white race. More than two-thirds of the persons interviewed were renting their living quarters, and over one-fifth lived in rooming houses.

Of interest as a supplement to this statistical picture was the reaction of the investigators who conducted the interviews.

The comment of the person who had worked in the lending business was:

"All the loan applicants who were turned down would have been rejected
by any legitimate lender before the new laws became operative. I paid particular attention to cases involving requests for loans of $50 or less, but in almost every instance it was evident that the small sum requested would have been no more than a temporary stop-gap. Persons who had asked for $50 loans to consolidate bills freely admitted that it would take from $150 to even as much as $2,000 to handle their obligations."

Another significant factor is that although the investigators were attempting to locate loan applicants from as little as a week to as much as several months after they had originally applied for a loan, nearly one-third of them could not be found. Attempt was made to reach 150 persons, but of that number 35 had moved without a forwarding address, 5 had left the area entirely, and 6, investigation disclosed, had given fictitious addresses.

The social worker reported that the persons he interviewed in his portion of the survey were average, respectable, wage-earning Americans. Many of the homes were poor, but few at the abject poverty level. A considerable number of the persons lived in downtown areas or semi-industrial sections. Several divorcees were in the group.

Most encouraging sign of all was the almost unanimous report that these persons who had been rejected when they applied for loans were not aware of any illegal bootlegging of loans. Those who were able to get money from other legitimate concerns did so. Those who could not, or did not attempt to, reported that they "got along" without the money. Only one of the more than 100 persons interviewed indicated that he had heard of a bootleg loan source.

Evaluating the meaning of this survey is difficult, largely because of the small size of the sample. Several things are rather evident, however:

(1) Bootleg loans are not a serious problem, which indicates that the existing laws make it possible for lenders to meet the needs of those persons desiring small loans. Bootleggers thrive when legitimate lenders are prevented from serving ordinary borrowers.

(2) It is possible to obtain loans of $50 or less, providing the loan applicant is qualified. This is true, even though there is evidence of a tendency to encourage persons who ask for a small loan to borrow a larger sum if they have the security. This policy cannot be condemned wholesale, for it may be (as this survey indicated in part) that in a considerable number of instances the larger sum is necessary in order to meet the needs of the borrower.

(3) Borrowing is not as easy as some of the advertisements may lead prospective applicants to think, but the fact that a considerable number of persons are rejected does not mean the regulatory laws are not operating properly. There are persons to whom a loan of any size is too risky at anything less than exorbitant rates. Such persons must depend on sources other than private lending agencies, and this would be true even if the legal rate of charge were far higher than it is at present.

There may be weaknesses in the present loan structure which need to be strengthened. It appears doubtful, however, in the light of this survey, that the rate structure under which personal property brokers and small loan lenders operate is one of these.*

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*Supplementing the findings obtained by interviewing loan applicants is a file of correspondence from lenders and Better Business Bureaus. Letters from every Better Business Bureau in California but one report the small loan laws were working unusually well and that borrowers appear able to obtain such sums as were needed. With some exceptions, lenders reported an ability to serve applicants for small loans.
These comments were in response to the question: "How many applications do you have for loans under $50 and how many do you grant?"

An independent office: 250 loans of $50 or less made monthly; 65% of applications for such loans granted.

A chain organization: 935 loans of $50 or less made in 10 months. Such loans represent 21.6% of accounts.

An independent concern: Applications for loans under $50 seldom received. No record of any being granted.

A chain group: Experimenting with loans below $50. Some persons denied loans of less than $50 have taken larger loans. Others have borrowed from pocket lenders, illegal but difficult to stamp out. Others have borrowed from industrial loan companies which can obtain a higher return on $10 and $20 loans than can a personal property broker, and a number have been given charity. With another year of experience under the Act, will be able to render the proper service at the proper rates.

A chain organization: More than 10,000 loans of $50 or less made in California in first 9 months of 1940. This represents 20% of all loans. Loans of $25 or less accounted for 2.4% of all loans, those of $26 to $50, 17.9% of all loans.