Part I
The Changing Landscape
Chapter Four
Financial Fracking in the Land of the Fee, 1980–2008

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In 1986, Tito Manor went shopping for a car. At the lot, the car salesman informed Manor that he would need someone to cosign, which his aunt, Gloria Young, ultimately agreed to do. The car salesman, who passed the completed loan application on to Fidelity Consumer Discount Company, notified both Manor and his aunt that the loan had been approved. Then, the salesman instructed them to come to the dealership and bring the aunt’s house deed, just as verification that she was indeed a homeowner. However, the dealer never informed Young that the house was being used as security for her nephew’s car loan. The lender, Fidelity, took a first mortgage on Young’s home at an interest rate of 36 percent—far in excess of the Pennsylvania state usury cap of 24 percent. Unable to keep up with the principal and interest on the car note after several months, Tito suggested that he return the car to Fidelity, to which the lender responded, according to uncontradicted deposition testimony: “We don’t want the car. We want your aunt’s house” (Mansfield 2000, 512–17). The steep loan terms made seizing the home not simply more likely, but also a more profitable alternative than seeing the loan terms satisfied.

The law making this possible was the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA). Among its other features, this law preempted state usury laws while also removing interest rate ceilings on any loan secured by residential property (Remarks of the President at the Signing Ceremony for the Depository Institutions Deregulation and Monetary Control Act of 1980). According to legal scholar Cathy Mansfield, “it didn’t take long after DIDMCA was adopted for some second mortgage lenders, and for other lenders who had been making high-cost consumer loans, to notice that DIDMCA appeared to allow them to charge an unlimited amount of interest provided they took a first lien on the borrower’s home” (Mansfield 2000, 511). Thus, a number of lenders, who would not have otherwise made first-lien home equity loans before DIDMCA, began to cast car loans, small consumer loans, and second mortgage loans as very expensive home equity first-lien loans (Mansfield 2000). High-cost lenders used the new deregulatory acts to bilk borrowers out of their cars and homes. Such loan practices were made possible because of federal preemption that allowed lenders to bypass state usury law. As the Manor Young case illustrates, beginning in the 1980s, financial deregulatory laws such as DIDMCA would erode consumer protections that had shielded
borrowers against predatory financial practices since the 1930s. This paved the way for the rise of fringe financial services and the abuses that accompanied it.

For nearly a generation, interest in asset building has been steadily spreading across the antipoverty policy landscape. Asset-building programs and policies were first tried by antipoverty advocates in the early 1990s who wished to navigate a third way between the direct income-transfer ideas of the left and the benign neglect adherents on the right (see Friedman, Vaughan, and Steinbach 1988; Haveman 1988; Sherraden 1988; Reger and Paxton 2001). Asset-building strategies would emerge as one of the four favored antipoverty, market-centered technologies of choice—along with microfinance, conditional cash transfers, or CCTs (in which money is granted to poor families on the condition those households promise to make specific investments like vaccination or high-school attendance for their children), and place-based projects such as President Clinton’s New Markets Initiative (Katz 2011, 113–50). While these interventions were gaining traction in think tank and policy circles across the political spectrum, a parallel, shadow movement was afoot, eager to make a profit from the very same low-income and working-class households that Michael Sherraden and other architects of the asset uplift school aimed to help. This extractive trend too has been abetted by government policies. Specifically, a series of deregulatory choices, mostly though not exclusively at the federal level, have turned a blind eye to equity stripping and have incentivized a sort of “financial fraking” that extracts wealth yet leaves behind a bevy of negative externalities. The result has been greater economic inequalities between upper-income and lower-income households. This chapter describes the rise and codification of consumer finance fees and its impact on four once-reliable paths to upward mobility—homeownership, higher education, employment, and transportation. Central to my study is the role played by deregulation, which has helped create an operational space for the spread of wealth-extracting consumer finance fees since the 1980s.

**Why Employment and Transportation Matter to Mobility**

The first two spheres—homeownership and higher education—focus on traditional pathways to upward mobility. Employment and transportation may also be considered pathways to upward mobility, if not in quite the same way as a home or college degree. These four domains are complementary, not mutually exclusive. While homeownership and higher education tend to encompass single financial expenditures—for example, a 30-year mortgage or 15-year student loan—the latter two spheres (employment and transportation) take into account the cumulative effect of more quotidian transactions (e.g., daily accrual of interest on a payday loan, the option of monthly or even weekly auto insurance contracts) consumers may experience. In each domain I examine how consumer financial products may exacerbate inequalities. In so doing, the chapter demystifies that upward mobility is not simply about the episodic (buying a home or borrowing a student loan) but also the everyday, that is, it reminds readers that seemingly mundane consumer financial expenses (such as auto insurance and payday loans), especially when extrapolated over time, serve to extract wealth and exacerbate socioeconomic immobility.

While employment is of course a pathway to upward mobility, the payday loan, the consumer financial product that was created expressly to address problems of work-related paycheck shortfalls, may well have the opposite unintended effect. First, as its very name intimates, a payday loan is virtually impossible to receive without a job—a fact that cannot be stated for almost any other form of short-term, consumer credit. Unemployed children, life partners, and even pets have all been known to have access to credit; not so with payday loans, where a pay stub is a must for any borrower. In this sense, a payday loan more closely correlates to employment and wages than any other consumer financial product. Second, while payday lending is certainly about access to credit, to focus exclusively on credit would be to merely focus on conditions of the supply and not the reasons for demand: mainly, the payday loan industry’s explosive growth and tremendous impact on working and middle class families, directly correlates to not only deregulation but also a declining standard of living spurred largely by wage stagnation. Third, payday lenders themselves recognize that their industry’s success is borne of wage stagnation. “There are multiple reasons fewer people are able to meet the[ir] expenses. First of all, overall wages have been stagnant for a long time,” to quote web communications of the Personal Money Store, an online marketer for the alternative short-term and mortgage consumer finance market (PayDay Loan Advocate 2010). Similarly, a report on payday lending in America, conducted by the Pew Research Center in 2012, indicated that 85 percent of borrowers assume these loans to cover ordinary living expenses (utilities, gas, groceries, and credit card) or unexpected expenses (car repair and emergency medical treatment)—the sort of expenses traditionally covered by a worker’s paycheck (PayDay Lending in America 2012). Moreover, the Pew report also suggests the negative impact payday lending may have on upward mobility as an antisavings mechanism. According to Pew, borrowers are more likely to be renters than nonborrowers in the same income brackets. For example, 8 percent of renters earning $40,000–$80,000 have used payday loans, compared with only 6 percent of homeowners earning $15,000–$40,000, according to Pew (PayDay Lending in America 2012). For renters, the high-cost transactions associated with a payday loan, relative to less expensive short-term credit options, may well strip wealth from future possible homeowners, creating another financial hurdle to increasing the personal savings that are necessary for such long-term, wealth-building investments, such as the purchase of a house.

Although traditionally not thought as such, transportation also is an area that has become critical for upward mobility, especially for a key demographic that the asset-building school looks to serve: the nation’s urban poor. Labor economists, sociologists, and urban policy historians have all documented the geography of opportunity around access to reliable transportation (Squires and Kubrin 2005, 47–68; Vale 2007; Briggs 2005; Jackson 1987; Raphael and Rice 2002, 118). Specifically, the “transportation gap” that has grown over the last five decades is not only because of deindustrialization, which has led to the oumigration of manufacturing and industrial jobs from central cities to suburbs, the US South, and abroad. It is also that declining white support for mass transportation and the principle of integrated residential housing, evinced in numerous public opinion polls since at least the 1960s, have exacerbated changes in the structural economy (Wilens 1996, 202). As the sociologist William Julius Wilson has written about the disappearance of upward mobility in the nation’s inner cities, “among two– or middle class and affluent families commuting is accepted as a fact of life…. In a multicenter job market that requires substantial resources for participation, most inner city must rely on public transportation systems that rarely provide easy and quick access to suburban locations” (Wilson 1996, 39).

Within the realm of reliable transportation, auto insurance remains an inseparable financial expenditure. “Obtaining a car creates expenses far beyond the purchase price, including insurance, which is much more costly for city dwellers than it is for suburban motorists,” Wilson writes (1996, 40–41). Driving without insurance results in imprisonment, fines, not to mention, in the event of an accident, astronomical reparations for loss of life and property. It’s not that urban motorists are, in the abstract, unable to afford insurance; rather, it is that the zip code calculus used by insurers exacts a high-cost premium for urban motorists, often pricing them out of the market altogether. Likewise, labor economists too have identified vehicle insurance as a sine qua non for upward mobility. One particular study, matching state data on auto insurance premiums to
The Nature of Consumer Finance Fees

 Fees as Hidden Charges

 Over the last 30 years, Americans have been increasingly subject to fees they may have little idea are being charged, largely because they are consumers in an increasingly underregulated financial marketplace. We pay at home, at work, at school, and in our cars. "Unexpected or hidden fees" rank as the single biggest everyday annoyance of American consumers, according to a recent survey by Consumer Reports (Consumer Reports Money Advisor 2010). Consumers regularly complain about bank teller, overdraft, and minimum balance fees, IRA or 401(k) maintenance fees, airport fees, cash advance or balance transfer fees on credit cards, activation and early termination fees doled out by cable, cell, and Internet service providers, along with mutual fund load fees, bank service fees, and college accounts fees, among other fees.

 "Hidden" does not mean that a cost, charge, or term is missing from the actual agreement or any more than a profit playing a game of hide and seek with her child is missing or disappears from the house. Hidden simply means that costs and terms are buried in fine print or impenetrable legal language that even contract attorneys often have difficulty detecting, with the onus placed on the consumer to discover it. In the case of "unexpected terms and actual costs associated with the good or service being provided by the lender or insurer. All too often the devil is in the details."

 In 1980 a typical consumer credit contract was one and a half pages, according to Wall Street Journal; by the early 2000s, it was over thirty pages (Paul 2004). These additional pages are not about protecting consumers, but are effectively the printed equivalent of the last ten or twenty unreadable terms. By inserting unexpected and unreadable terms into the fine print, lenders and other financial service companies make billions of dollars each year at the expense of families. These fees have the potential to add up over time, to levels that can significantly change the economic prospects of a household.

 I call these hidden expenses trick-and-trap (TNT) fees. By TNT fees, I mean a collection of cryptic charges on subprime mortgages, loans and grants for higher education, high-cost equity and payday loans, and zip-code-based insurance premiums. TNT fees often hide in plain sight because the true and total costs of these financial products and how these costs are determined are often buried in fine print, undisclosed and tightly guarded pricing structures, and impenetrable legal language, customers—whether by accident or design—are often "tricked" into paying exorbitant costs for consumer finance products.

 Once ensnared into paying higher costs, consumers find themselves "trapped" in an almost inescapable web of debt. Even for the so-called good debts, such as college student loans, the final amount borrowed can easily increase to three or four times more than the original loan. What makes TNT fees most dangerous is that more than three in ten are invisible, meaning that over 30% of borrowers do not even know what funding they have been provided, and what it costs them. In housing, higher education, employment, and transportation. Unlike more indulgent
a public good or service (e.g., education, housing, or legally mandated auto insurance) with one group often subsidizing another. During debates in the 1980s and 1990s, senators on both sides of the aisle openly referred to America’s financial aid system as a “tax” on students and middle-class families because students—via fees assessed to government lending programs—were being asked not simply to repay their educational loans but also to pay an additional fee to help balance the federal budget (Sanchez 1995).

Many pundits and politicians claim that this tax is paid only by the financially irresponsible, America’s urban poor, or working-class residents of the so-called secondary suburbs. However, the kudos-like spread of consumer finance fees, which have climbed over and caulked around the bank accounts of many middle-class American consumers in recent years, militates against this view. For example, although many believe that the recent mortgage crisis impacts only borrowers with poor or marginal credit, the average American subprime applicant actually possessed a prime credit score and was eligible for a conventional loan by the time the mortgage market bubble burst in 2007 (United States Financial Crisis Inquiry Commission 2011).

**Fees as Profit Stream**

Consumer finance fees have been a part of the modern consumer experience throughout much of the twentieth century. What has changed since the 1980s is the evolution of fees from a means of offsetting administrative or risk costs into a source of income itself. That is, fees are a profit stream. Fee-income started in earnest in the early 1980s with Paul Perdue, who served as the lead plaintiff in a 1978 class action suit against Crocker National Bank of California. Perdue and others sued Crocker National for charging a $6 non-sufficient funds fee when the actual cost incurred in processing the bounced check was only 30 cents; this transaction effectively netted the bank a 2000 percent profit. Plaintiffs claimed such a profit was unconscionable (SCOCAL 2009). In anticipation of the ruling in *Perdue*, a case that was ultimately settled out of court, the Office of the Comptroller of the Currency (OCC) issued an interpretive ruling in 1985, establishing that service charges were a business decision for banks and thus could preempt state law (A. S. Pratt & Sons 2010). OCC’s ruling was followed a decade later by a 1996 OCC revised provision, authorizing national banks to disregard state usury laws.

Still, fee income greatly increased until 2004, when the OCC enacted expanded preemption regulations, giving maximum latitude to banks in setting fees for both deposit products and consumer loan products. Thus, banks were given the green light to charge limitless fees for limitless amounts without being in violation of state usury laws. Another bank regulator, the Office of Thrift Supervision, made a similar ruling also in 2004 (A. S. Pratt & Sons 2010). By 2009, according to the *Financial Times* of London, US banks were collecting $35.8 billion in customer overdraft fees alone—not to mention other fees like ATM withdrawal, minimum account, and checking balance maintenance fees (Scholtes and Guerra 2009).

Even during the recession, the median overdraft fees increased, from $25 to $26, the first increase during a recession in 40 years. The larger the bank, the more likely the increase. This was understandable, according to the general counsel of the American Bankers Association, which stated that large banks do not know their customers as well as smaller community banks and thus must be compensated for their increased risk (Scholtes and Guerra 2009). Where overdraft fees really dent wallets, however, is when banks let customers take out more than they have at an ATM or through a debit-card purchase (in the past usually without an alert). In these cases, customers are not facing merchant fees, and probably the only consequence of the transaction being denied would be having to put back their groceries (Chua 2005).

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**FINANCIAL FRACKING IN THE LAND OF THE FREE**

**Fees in Modern Consumer Life**

Our current crisis in consumer finance goes back decades. During the mid-1970s, the federal government enacted a series of laws—the Equal Credit Opportunity Act of 1974, the Home Mortgage Disclosure Act of 1975, and the Community Reinvestment Act of 1977—to encourage the provision of financial services in underserved communities. Yet, almost simultaneously, a set of deregulatory policies emerged that quietly made credit, banking, mortgage, and insurance markets less accountable to governments and consumers.

The erosion of oversight escalated in the following 30 years, declining consumer protections and fostering the rise of a new fringe financial sector, one that shifted a shift away from denying credit and services to extending credit and services on high-interest terms. The net effect has been a TMT tax in disguise, a de facto levy sanctioned by the laissez-faire policies of successive governments and the private sector on citizens consumers.

Given their role in the 2008 financial crisis, abusive mortgage lenders have received relatively more scrutiny, but they are just one piece of a forgotten history about the rise of consumer finance fees in four spheres that are intertwined and inescapable in modern consumer life: homes, school, work, and transportation.

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**Depositary Institutions Deregulation and Monetary Control Act**

Modern subprime lending in housing started with three legislative acts. The first was the 1980 DIDMCA. DIDMCA was intended to boost the saving rate of Americans, which hovered near a decade low of 7.9 percent in September 1979, when the law was being debated. DIDNCA allowed for higher interest rates and thus functioned as the gateway law creating a new type of mortgage market—subprime loans. DIDMCA is critical to the subprime market for two reasons. First, it made high interest rates and fees legal. Now, effectively free to charge consumers any rates they wanted, banks had incentives to make home loans to borrowers with below prime credit scores. Second, DIDMCA also allowed the charge of unlimited interest rates for refinancing or second liens, because the law did not distinguish between purchase (mortgage origination) loans and loans made for other purposes. Thus, as we saw in the introduction of the chapter, lenders looked to charge consumers the higher interest, most profitable, first lien loans—the most common type of subprime loan—regardless of the product the consumer was purchasing (Temkin, Johnson, and Levy 2002, 4).

DIDMCA did not trigger immediate massive change in the high-risk mortgage. However, it erected the legal apparatus that was the sine qua non for making high-cost, subprime loans egal. Specifically, DIDMCA abolished the interest caps that had governed mortgage lending since the New Deal, freeing mortgage lenders to charge unprecedented rates to putatively riskier borrowers (Blier 2008, Federal Deposit Insurance Corporation 2012). How would this help the typical savings accountholder? The assumption was that once savings and loan associations (S&Ls) and other savings institutions were free to charge more on mortgage loans, the higher rates would soon trickle down as higher returns for savings accounts of bank and S&L customers. "Most significant of all," according to President Carter, "it would help improve our nation's very low savings rate" (Carter 1980). Carter, along with allies in Congress and the mortgage industry, impressed upon a skeptical public that abolishing rate caps would rebound to the benefit of the average accountholder by boosting savings. Sold on this idea, even those habitually hostile to laissez-faire economies such as the Gray Panthers, a quasi-socialist band of senior citizens in the 1970s, called for DIDMCA's passage (Rom 1996; Eisenbeis and Kaufman 2011).
While DIDMCA may not be chiefly responsible for the steady decline in the saving rate since this period, the legislation certainly failed to boost savings. In fact, in the decades following the passage of DIDMCA and other complementary financial deregulatory laws, the saving rates among American consumers actually declined, so much so that the saving rate (3.9 percent) in the years leading up to the financial collapse (ca. 2000–2008) was half the rate it had been when DIDMCA passed (Marquis 2002; Guildolín and La Jeunesse 2007; Jones 2010). DIDMCA had failed to achieve its original intent.

**Garn–St. Germain Act**

While DIDMCA phased out rate caps, the Garn–St. Germain Act of 1982 introduced to the national market some of the most exotic mortgage instruments that exist today. It did so by empowering banks to preempt state protections that had been put in place to prohibit the interstate use of creative mortgage instruments. These instruments include adjustable rate mortgages (ARMs), excessive prepayment penalties, and balloon payments, which are inflated payments due at the end of a loan agreement that lenders often refuse to refinance, thus leaving borrowers with a huge bill at the end of the loan. Among three credit ratings spawned by this 1982 law posed far greater risks at the time of the Great Recession than conventional fixed-rate mortgages, and continue to undermine homeownership stability (Nazar 2008). Specifically, an ARM was 36 percent more likely to default than a conventional fixed-rate mortgage; a mortgage containing a prepayment penalty was 52 percent more likely to default than a loan without one; and a balloon payment mortgage was 72 percent more likely to default than a conventional mortgage (Nazar 2008).

From the outset, these loan practices—blamed for greatly increasing the default and foreclosures rate in recent years—were designed to favor the lender over the borrower (Lewis 2005). That is why, when the Garn–St. Germain Act passed, the Chicago Tribune called the new law an "aid bill" for the mortgage industry (Key 1982). The abusive history of the Garn–St. Germain Act stems directly from its troubling legislative origins. Following the money of the act’s two namesakes, Bernard St. Germain (D-CT) and John Garn (R-UT), reveals the strong collusion between both political parties and the financial services industry. The congressmen profited nearly as much as the industry.

The son of a dye factory foreman, St. Germain, entered the House of Representatives in 1961 as a state legislator and was a millionaire when he left in the 1980s ("Amazing of Wealth, Ties to Bankers Questioned" 1987; United States House of Representatives, US House Committee on Ethics 1987). His personal wealth appeared to come largely from realtors, bankers, brokers, and others he was directly charged with legislating and regulating as a member and later chair of the House Banking, Finance, and Urban Affairs Committee. By the mid-1980s, the Rhode Island Democrat was one of the two biggest recipients of campaign contributions from the three financial policy action committees (PACs) lobbying for the banking reform legislation that included too many most notorious exorbitant fees like balloon payments and adjustable rate mortgages ("St. Germain Attacks Wall Street Journal" 1985; Jackson and Carrington 1985; Beinart and Slocick 1994; Sheehan 2008). In addition to taking campaign contributions from businesses he was directly charged with legislating and regulating, St. Germain also received preferential investment and real estate deals, including from one investor who, hoping to benefit from the passage of the exotic mortgage bill then being debated in Congress, put up nearly 100 percent of funding for St. Germain to purchase five restaurants (Jackson and Carrington 1985; Jackson 1987, Sheehan 2008). The bill’s GOP coauthor, Jake Garn, was equally embroiled. The Utah Republican shelled for the nation’s largest high-risk, high-yield securities company, junk bond firm Drexel Burnham Lambert. This firm, along with other financial service lobbyists, repaid the Utah senator’s promotion of DIDMCA and Garn–St. Germain by underwriting Garn’s pet project, the Garn Institute of Finance at the University of Utah (Day 1989). Funding tax-exempt foundations such as the Garn Institute constituted another way that the industry, in an effort to circumvent newly created campaign finance and related laws, kept its access to the legislative architecture writing the banking rules (Soley 1995, 94–95). Because these rules were conceived and crafted primarily by industry lobbyists, American consumers were always an afterthought.

The point here is not to impugn or impugn the motives of the law’s architects. More importantly, because Garn–St. Germain—the law that paved the way for so much creative financing of the subprime market—originates from a policy process so awash in industry money, it is impossible to know where lawmakers’ public-spirtited commitment to free-market principles ends and their loyalty to the narrow interests of the financial services begins.

**Tax Reform Act**

These two laws—DIDMCA and Garn–St. Germain—combined with a quiet revolution in fiscal engineering, the Tax Reform Act of 1986 (TRA 1986). The third step to subprime, TRA 1986 was steeped in the costly cold war mindset that private property owners were more deserving citizens than renters. Through the home mortgage interest deduction and other tax breaks created by the TRA, Congress rewarded those who purchased homes and subsidized the accumulation of home equity (Graetz 1988). Before TRA 1986, consumers could deduct the interest accumulated from a range of installment purchases (e.g., credit cards, personal loans, and even home equity loans). After the act was passed, only the interest from a primary mortgage and home equity loan (aka second mortgage) was deductible. This misguided principle ultimately created an American debt trap. In order to secure the big tax break, consumers increasingly used their homes as their primary source of investment and savings (Garon 2011). Banks quickly swooped in and began pushing the tax advantages of tapping the equity in one’s home to pay for a vacation, car, or wedding. "If you’re looking for your cheapest source of money, check your home," advised Chemical Bank in a nationally promoted advertisement (Chemical Bank 1986). As housing prices rose, homeowners took more equity out of their homes. By the late 1990s, only one-third of home equity loan proceeds financed home improvements; the balance went toward paying off school debt, medical bills, weddings, cars, vacations, and credit cards (Garon 2011, 305; Atlas 2003; Canner, Durkin, and Luckett 1998).

**The Impact of Housing-related Fees**

Without these three legislative acts—the DIDMCA, Garn–St. Germain Act, and Tax Reform Act of 1986—there would be no subprime market. Given how congenially flawed the DNA of mortgage deregulation was from the outset, readers may well ask not why subprime fails but how it managed to avoid failure for so long. Why were financial institutions and others associated with the real-estate industry so intent on pushing instruments that practically guaranteed failure? A major reason was fees—fees that were hidden in the legalese of a mortgage or a home equity contract, or, when detected, fees that trusted professionals persuaded borrowers they need not worry about (Duffy 2012; Elmer 2012).

By the 1990s, thanks to deregulatory laws like Garn–St. Germain and a tacit faith that government would bail out home lenders, fees had exponentially increased industry profits and the personal incomes of professionals at the expense of consumers. Analysis of the current financial crisis tend to focus on mortgage bundling and credit default swaps—the complex financial instruments Wall Street invented to create vast profits.
from noching (Morrissey 2008; Morgenson 2011; Gandel 2012). However, the roots of our predicament predate those exotic inventions. Initially subprime mortgages were about the money to be made from fees. Aside from paying higher mortgage rates than others, subprime borrowers who are unable to pay a balloon must refinance, thus incurring new upfront charges like origination fees. There are also prepayment penalties in which subprime borrowers are penalized for trying to repay a loan early. These penalties naturally slow down rates of repayment on balance and principal, increasing the likelihood of negative equity during a downturn in housing prices. Even before the collapse came equity stripping—the profitable practice of refinancing a home in such a way that the borrower is charged excessive fees by the lender or broker, stripping the equity out of the home and putting it in the pockets of the refinancing company. By 2005, three years before the housing bubble burst, subprime borrowers had surrendered $9.1 billion annually in high interest rates, prepayment penalties, and other related fees (Quercia, Stegman, and Davis 2005 6). That is $9.1 billion each year in equity extracted from the most vulnerable borrowers in the subprime housing market.

Schools

If a home purchase is the most expensive financial investment one can make, postsecondary education ranks second. We normally do not think of higher education as a mechanism of wealth disparity. Indeed, for much of American history, particularly the postwar era, a college degree has been regarded as society's great leveller, a pathway to upward mobility. However, this has been slowly changing in recent years, as the growing costs associated with financing a degree have increasingly made college campuses a site of indebtedness and inequality. The rich and the two out of three students who today take out a loan to attend school (Cunningham and Kienzl 2011; O'Shaughnessy 2011). In 2010, student loan debt surpassed credit card debt for the first time (Lewin 2011). The average debt for graduating college seniors with a student loan (approximately two out of every three students) in 2010 was $24,000, and the total debt was likely to top one trillion dollars in 2011 as more young people attend college and borrow money to do so (Shades 2011). Buried in the contract of government and private student loans is a trove of TTN fees that are often gone unexplained by financial aid officers and go unnoticed by borrowers. By fees for college financial aid. I mean add-on expenses such as origination charges, deferment and extension costs, early repayment penalties, and default fines in which lenders tack on collection costs as high as 20–30 percent of the loan balance before sending it to the collection agency, a process called "capitalization" (Kirkland 2011; US Department of Education and Consumer Financial Protection Bureau 2012; Wagner 2012).

Private student loans, which took off around 2001 and accounted for 14 percent of all student loans in 2008, often have even more predatory terms than public student loans. For example, some private loans go into default after just one missed payment. The terms of these private loans increase a borrower's costs and default risks—and so risk damaging her credit score and increasing the costs of future credit—without a substantial benefit (relative to a federal student loan) to the borrower. The end result of these TTN fees is exploding debt, resulting in students often owing three to four times the original loan amount. While the costs and terms may not necessarily be hidden, the loan application forms and processes are often so complicated, layered in legalese, that even the current Secretary of Education Arne Duncan admitted in his 2009 Senate confirmation hearing, "You basically have to have a Ph.D. to figure that thing out" (Confirmation of Arne Duncan 2009).

Once trapped in debt, student borrowers are offered very little in the way of consumer protections to help them escape. Unlike other forms of consumer credit, for example, the key student loan-related statutes do not have private enforcement rights or attorney's fee provisions, so it is difficult and costly to challenge them in court. Unlike conventional debts, borrowers cannot discharge student loan debt in bankruptcy court without clear proof of undue hardship. In addition to these add-on fees, which often hide in plain sight in student loan contracts, the student loan itself could be regarded as an unexpected fee, given that private and unsubsidized loans were originally designed to play only a supporting role in financing students' education.

The financial aid system was not intended to be like this. The Pell grant was originally conceived in the 1970s as the foundation of the federal student aid system, with other federal and nonfederal grant and loan programs originally intended to provide supplemental (not primary) assistance if necessary (Gladieux 1995). However, the Pell grant has long since ceased functioning as the foundation of America's financial aid system. Last year, for example, 82 percent of undergraduate aid came from non-Pell sources. Given that today's Pell covers such a small fraction of the overall cost of college, government grants function more like an introductory interest-free rate. Like most teasers, they entice customers with modest up-front benefits that are too good to last the life of the term and are offset by staggering loan totals that dwarf the initial offer or reward.

Changer in Student Aid

So what went wrong? This trend toward student indebtedness started approximately a generation ago, with its roots in deregulation, fiscal policy, and the changing view of students from future tax contributors to tax eaters. The rise of student loans is directly attributable to the decline in tax receipts once earmarked for higher education. Cuts in higher education funding since the 1980s are the number one reason for the escalation in tuition and fees. Under the guise of deregulation and deficit reduction, the Reagan Administration and their congressional allies aimed to dump students from both the Pell grant and federally subsidized student loan rolls. With this goal in mind, spending on student aid was slashed by some 25 percent between 1980 and 1983 (Rankin 1981; United Press International 1985; Broder 1987). Tax cuts necessitated government doing less with less. Specifically, Reagan's Office of Management and Budget believed that less funding would translate into less federal intrusion (OMB Director's Review 1984; see Strozier 1989). These cuts gave license to reducing the federal role in education, as Reagan rolled back regulation by reducing the enforcement budgets overseeing financial aid in higher education. An exception was the inspector general's office where the operational budget was increased and new personnel and authority were added to make a more muscular enforcement outfit that might crack down on fraud and abuse. The Administration also expanded the office by empowering it to go beyond merely collecting complaints about potential abuse or fraud, its only authorization, to initiate investigations. It added at least 130 additional audits and ten more investigations into criminal activity (OMB Director's Review 1984).

Eager to remove students from the rolls, Reagan Administration officials tightened eligibility guidelines for Pell grants and student loans, with dramatic consequences. In the years immediately following guideline changes, from 1980 to 1985, freshman participation in the Pell grant program declined by nearly half (Green 1987). Changing eligibility rules for Pell grants eliminated 267,000 freshmen from these awards between 1980 and 1986. Students who were eligible for grant assistance in their freshman year were, in year two, told that they had to take out student loans. For nearly nine years running in the 1980s, the purchasing power of Pell grants decreased as college costs grew and outpaced inflation (Boren 1989, 3). As its buying power declined what the Pell covered shrank as well—with aid shifting from grants to loans. For example, at the dawn of the 1980s, Carter submitted his budget for the fiscal year with Pell grants
family savings dried up, more students were forced to turn to loans. According to a Federal Reserve Survey of Consumer Finances, between 1983 and 2001 student loans as a share of household debt increased from 28 to 58 percent (Dykan, Johnson, and Pence 2003). Reagan Administration policies would also provide the private sector a roadmap to fees in student lending. Reagan’s policies initiated the very first set of consumer fees on student loans: origination fees. Originally created to help offset the costs of tax cuts and reduce the national debt, the origination fee was an activation charge of 5 percent to set up each guaranteed student loan (Naigele 1983, 207). Origination fees increase the final loan amount because the fee is rolled into the principal and repaid with interest. Although introduced as a temporary measure, origination fees are now a permanent fixture for all student loans. As one outlooker bristled at the time, these dollars will never be “seen or available for expenses, yet it must be repaid with interest” (Ozet 1986, 26).

By the 1990s, the federal cuts would have a cascading effect nationally, as most states began following Reagan’s budgetary template, reducing public expenditures on higher education in an effort to lower state costs (Mumper 1996; McLendon, Hearn, and Motley 2009). With government doing less, the student’s share of the cost of education spiked (Hosler, Lund, Ramin, Wesfalk, and Irish 1997). Students and universities had to pick up the tab in the form of ever-higher tuition and fees. Over the next three decades, high-cost, unsubsidized government and private student loans would increasingly fill the void left by the hemorrhaging of state and federally subsidized loan and grant programs.

Work
Like many other consumer expenses, numerous studies have shown that the cost of higher education has outpaced the average family income in recent decades (Mumper 2003; Rhodes 2006; Supino 2008). The inability of incomes to keep up with expenses is symptomatic of a larger story: household debt, which has risen twice as fast as disposable income since 1981 (Schwartz 2010). By now it is a well-worn story: household debt is nine times what it was in 1981; household debt has risen twice as fast as disposable income since 1981 (Schwartz 2010). Meanwhile, the median wage has actually fallen since 2000—even though workers are laboring harder and better than ever before (Jelke 2009, 2011). This increased worker productivity could translate into wages only if workers worked about twelve hours per week; instead, the US worker works longer hours today than at any point in the twentieth century and the United States is the most overworked developed nation in the world. However, hard work has failed to translate into success. By 2007, according to data from the Bureau of Labor Statistics, the typical American worker was 60 percent more productive than in 1950 (Rauch 2000; Miller 2010).

Equally familiar are the strategies that individuals and families have used to make up the gap between income and expenses: working more hours, creating two-earner households as well as an increase in stop-and-start wage stagnation. Perhaps the most ubiquitous response has been the proliferation of payday loan stores. Payday lending emerged to fill the unmet demands of American workers who watched their wages stagnate precisely as 2002 housing bubble burst, which once offered retail services like low-interest, short-term loans, went after bigger institutional clients (Huckstep 2007; King and Parrish 2011; Pew Charitable Trusts 2012).

So how does a payday loan work? A cash-strapped customer goes to a local payday loan store and writes a postdated check to cover expenses until his or her next payday (usually in two weeks). The borrower immediately receives the amount in cash minus the so-called transaction fee. The loan has to be repaid in full out of the borrower’s next paycheck, otherwise the borrower must assume another loan plus interest and the cost of the transaction
fee. Through the fees associated with payday loans, the free market has managed to trap the American worker further in debt (Peterson 2000; "Mayday for Payday Loans" 2007; Parrish and King 2009). It is not uncommon for a borrower to wind up paying as much as $350 for a $25 loan. Paying in cash and on time is rare. As one report notes, 90 percent of borrowers rolled their loans over—not once but at least five times (Parrish and King 2009, 5). Payday lending is, by definition, more closely tethered to income than any other form of consumer credit. Payday borrowers must provide a paycheck stub to verify employment and income, unlike charge card borrowers, for example, where a stay-at-home spouse, a child, or even family pets have been known to have lines of credit.

How Payday Lenders Game the System

Nearly every state forbids usurious rates (Francis 2010). At the federal level, it is a crime to lend money at rates more than double the state's usury rates, which vary states cap at 36 percent (Chin 2004). So how have payday lenders gotten away with charging exorbitant interest rates? Their success lies in the ability to game the system in four basic ways. First, payday lenders mask the true cost of their loans. In particular, unlike other lenders, they fail to disclose the annual percentage rate (APR). (Chin 2004). An APR is the total interest charged on principal to be paid in a year divided by the balance due. In other words, the APR is the agreed-upon yearly rate of return on the money that is borrowed. By not disclosing the APR, payday lenders appear to be in blatant violation of the Truth in Lending Act (TILA), a law passed in 1968 to make loan pricing more transparent for the consumer by requiring the cost of all loans to be calculated on the same basis, the APR. A consumer not calculating the cost of a loan based on APR might assume a payday loan is less expensive than, say, a credit card cash advance.

Payday lenders have skirted disclosing APR for good reason: doing so would expose how expensive payday loans are compared to other short-term credit transactions such as a cash advance from credit cards (Center for Responsible Lending 2001). APR matters for a two-week loan. Let us say both the credit card company and payday lender are quoting an interest rate of 18 and 15 percent, respectively. If it were based on a non-APR basis (calculated biweekly on payday), it would appear to be cheaper (15 percent) to a credit card (18 percent), which uses exclusively an APR. But when both disclose the APR, as required by TILA, the actual costs of the loans are clearer: The cost of the credit card cash advance remains 18 percent while the payday loan—after multiplying the 15 percent times twenty-six two-week terms—is skyrocketed to 390 percent (Center for Responsible Lending 2009).

Second, payday lenders successfully gained the system through the so-called strategic alliances with banks. The Gramm-Leach-Bliley deregulatory law, passed in 1999, allowed federal insured depository institutions to enter into strategic alliances by contracting out: their government-issued charters to payday lenders. Gramm-Leach-Bliley allowed retail banks to merge with other large-scale financial institutions like investment banks and insurance companies, something these institutions had been unable to do since 1933. The ability to merge also meant that government-backed banks could now enter into these alliances with high-risk financial entities such as payday lenders. Banks entered into these business relationships despite payday loans’ reputation as the most hazardous of all consumer financial products, with two out of three payday borrowers defaulting on their first loan (Skiba and Tobacman 2008). Two thirds of payday borrowers incur five or more payday loans per year (Erturk, Farrick, and King 2003). For the payday lender, these strategic alliances or the so-called rent-a-bank charter agreements freed them from tougher state usury laws. That is, payday lenders with national or state charters are empowered to preempt state usury laws and charge more than could export interest rates using the bank’s location regardless of the usury caps that may exist in the borrower’s home state (FDIC Advisory Committee on Banking Policy 2009). In exchange for their charters, banks were often promised returns on their investments in payday loan companies above 20 percent, or about double the return on traditional investments (Check-N-Go 2001).

Third, payday lenders gained the system through the additional risks associated with these strategic alliances. Strategic alliances posed a high risk for banks because it relied on borrowers who often went into default. Traditionally, banks lent money to borrowers who were expected to repay loans in full plus interest over maturity. Payday lending turned traditional banking practice on its head, however—the most profitable transactions came not from repaying the loan but, instead, rolling it over upon maturity: this triggered a whole new set of fees and expenses to be incurred by the borrower and created a highly profitable revenue stream for the creditor. While certainly profitable in the short run, these loans posed long-term problems. Finding themselves trapped in a spiral of debt, borrowers would be unable to pay their creditor (payday lender), which in turn would be unable to offer dividend payments to their investors (the bank). In part for this reason and alarmed at the spread of these strategic alliances, federal financial regulators admonished Congress and banks that the payday lenders’ debt-based business model exercised anything but traditionally sound banking judgment.

These strategic relationships not only exposed banks to "risks associated with payday lending," as regulator warned the CEOs of all national banks (Comptroller of the Currency Administrator of National Banks 2000; Hodson, Owens, and Fritts 2000). Left undisturbed, regulators concluded, payday lenders would "pose a variety of safety and soundness compliance, consumer protection, and other risks to banks" (Comptroller of the Currency Administrator of National Banks 2000). Ultimately, because these banks were federal insured institutions, they also posed a heavy risk to taxpayers. Such threats to our national economy were hiding in plain sight, especially since the debt-driven business model of payday lending had gone viral and now infected too-big-to-fail banks. Big banks would stop partnering with payday lenders on renting out their charters by the mid-2000s. Nevertheless, four of the nation’s largest banks (Wells Fargo, Citigroup, Chase, and Bank of America), with assets controlling nearly 50 percent of the US GDP, would continue exposing US taxpayers by extending billions of dollars of credit to high-risk payday lenders—an industry whose business model is predicated on their customers’ inability to make payments.

Fourth, it would have been impossible for the payday lending industry to trick the regulatory system, trap tens of millions of Americans in debt, and then have taxpayer bailed-out banks extend credit to publicly held payday lenders without the help of lawmakers. Since the problem was first introduced in the well of the House of Representatives in the late 1990s, Congress has tended to be more of a problem than the solution. For nearly a decade, a passive Congress preferred to look the other way despite repeated warnings from regulators, a growing number of consumer advocates, and even the Defense Department itself (Center for Responsible Lending 2001; US Department of Defense 2000). Clearly, money played some role. Payday lenders more than doubled their spending on lobbying and campaign contributions during mid-2002 to combat calls by the military, consumer advocates, and regulators for greater oversight. Within the financial service sector, payday lenders were second only to bankers in the amount spent on lobbying and campaign contributions (Salmon 2010; Citizens for Responsibility and Ethics in Washington 2012).

Thanks to policymakers, payday lenders were able to game the system—dodging and ignoring antitrust laws dedicated to protecting consumers while passing deregulatory
legislation, like laws allowing rent-a-banks, that ensured the buck ultimately stopped with the American taxpayer.

Payday Loans and the Middle Class

America’s middle class helps keep payday lenders in business. By 2008, there were over 24,000 payday lenders and similar high-cost check-cashing outlets, challenging the myth that these lenders cater solely to the American working poor and others living on the fringes of the nation’s financial system. In 2011, the average approved online payday borrower earned above $50,000 annually, higher than the median household income ($46,242) for the entire United States (Pew Charitable Trusts 2012). Studies of payday lending conducted by university economists since the early 2000s have routinely showed that middle-class consumers are a critical part of the customer base, with three out of four borrowers possessing a high-school diploma or some college education (Moore 2001; "Clarenort McKenna Professor Responds" 2005). A study of over 700,000 online payday loan applicants showed 45.2 percent of payday borrowers own their own homes in 2010. This common denominator is that our customers have steady sources of income and bank accounts, stated Darin Anderson, president of the industry’s largest trade association, the Community Financial Services Association (Schlens and Modiker 2008; "Community Financial Services Association" 2008). Consumer finance debt has become an inescapable part of daily life in America; nothing captures this better than the statistic that payday lending stores now outnumber Starbucks and McDonalds, establishments that our national business and political leaders once regarded as baronets of modern-day, middle-class consumption (Stegman 2007; Francis 2010; Martin and Longa 2012).

The Impact of Payday Lending

Despite the heavy demand for payday loans, this free-market cure proved at least as bad as the original cause. The average payday loan traps already financially strapped customers in a cycle of debt, largely by levying interest charges that range between 391 and 443 percent for a payday loan (King, Parrish, and Tanik 2006; Martin and Longa 2012). Such high-cost charges strip working- and middle-class households of hundreds of millions of dollars each year (Ernst, Farris, and King 2003; King, Parrish, and Tanik 2006). In the aggregate, these charges end up reducing the money retained and circulated in local economies. The above estimates of the net effects of payday lending even take into account the offsetting positive impacts the industry has on local spending, employment, and reinvestment in business. Not even the military has escaped the predatory practices of America’s most ubiquitous usurious lenders. In fact, service personnel are thrice times as likely to assume a payday loan as the average consumer; such loans account for 70 percent of losses in security clearances for service members (Stegman 2007).

Payday lending offers a window into how deregulation has contributed to exposing the nation’s entire financial system to unsafe banking practices and systemic risk. The difficulty was not simply that deregulatory laws like Gramm–Leach–Bliley opened the way for strategic alliances with banks, which exempted payday lending from state oversight. By providing the implicit federal guarantee that went with rent-a-banks deals between payday lenders and federally-insured banks, lawmakers (and D.C. regulators) also ensured that the American taxpayer would be the one held accountable for the reckless lending practices of too-big-to-fail lenders. The story of payday lending’s proliferation may be the best place to start for those wishing to understand how reckless lending and unsound financial practices spread throughout the economy, from Main Street to Wall Street.10

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Transportation

Despite the higher profile of other financial products, nowhere is a de facto, hidden consumer tax more commonly assessed but so little discussed than in the realm of auto insurance. For nearly 90 percent of American households, the vehicle linking the above together—consumer finance—housing, education, and employment—is, quietly literally, the automobile (McGuckin and Srinivasan 2003).11 The car is the most commonly held nonfinancial asset in America and, second only to a home, the most durable goods and necessity that consumers purchase. By law in almost every state, one’s car must be insured.12 Relatively speaking, then, in the world of financial services, policy makers should hardly consider lenders to be the most advanced and promoted class. That privileged perch should logically be reserved for the auto insurance industry, which occupies a unique and protected status within the US economy: it offers a service that people are required by law to purchase, yet it is provided exclusively by the private sector on a for-profit basis. This public–private collusion resulted in skyrocketing premiums for insured motorists by the mid-1980s (Cummins and Tennyson 1992).

Auto Insurance also serves as a useful reminder that when discussing the wealth gap, it may be helpful to include "accumulated effects of repeating the same pattern" (Lynch 2011, 91–95). These patterns tend to have a "dramatic impact" on a consumer’s overall financial picture” (Lynch 2011, 95), though they too often are overlooked in favor of a big-ticket, single expenditures. "People drastically underestimate how much wealth they will amass” because of small (if repeated) household decisions (Lynch 2011, 95). Patterns that exacerbate the wealth gap might be particularly instructive in the zero-sum world of auto insurance, where there is an active and on-going transfer of wealth in the form of discounted insurance rates from one pool of insured drivers to another.

Auto Insurance and Zip Codes

Because auto insurance rates are based on place of residence (zip code) rather than driving record (the so-called territorial rating system, or TRS), higher rates are often borne by those motorists least capable of paying them. For example, drivers with urban zip codes in the populous northeast and mid-Atlantic states may pay as much as $800 more each year than their fellow suburban drivers (Preston 1998; Levick 1999). Over the lifespan of a typical motorist, this can translate into a loss of more than $40,000. This estimate is relatively conservative: in California, postal code profiling is estimated to cost good drivers as much as $574 each year, the lifetime expenditure of the “deserving” motorist who has no accidents or tickets is even higher (Consumers Union 2005; Krasol 2012; Hirsch 2012). With many motorists simply priced out of the market, the result is a skyrocketing number of uninsured. The shrinking risk pool means higher premiums for the insured. This shifts a greater financial burden from the underserving motorists (e.g., one with recent accidents and tickets) to the deserving motorists—further widening the wealth gap between insured urban motorists and insured upper-middle-class drivers in suburban areas, where insurance is considerably cheaper.

Unaffordable insurance "is the most common complaint that I hear from my constituents," said a Detroit state representative who served as the ranking member of Michigan’s House Insurance Committee (Michigan Chronicle 2009). In the late 1990s, Motor City drivers paid on an average $1,200 more each year than wealthier, whiter suburban residents of the famous housing tract known as Eight Mile Road, just a few blocks north. Insurers contended that rates were legitimate because of auto thefts and risk assessments, but other studies released by the state attorney general’s office, based on the review of sixty auto insurance quotes, demonstrated average disparities of up to
financial by insurers, won election as state insurance commissioner. An underdog who pulled an upset victory largely because of heavy fire by insurers late in the campaign, as California’s chief insurance regulator, Quackenbush enacted a series of measures that appeared more responsive to his financial benefactors than voters, giving insurers greater liberties to base rates on factors besides costs, allowing safer rating methods, and promoting early settlements. Ultimately, even the laissez-faire expressed concern about such capture and urged more effective oversight: “Surely it is a little absurd to allow insurance commissioners to raise money from insurers” (The Economist 2000). The use of regulatory capture to distort price, but they have lated by 1987 have been responsible for the disparity in price, but they have been certainly helped to perpetuate it by blocking implementation and enforcement of laws designed to make insurance based more on how one drives rather than where one lives.

New Developments

Some of the developments since 1987 have been in the areas of payday lending and student financial aid. In the payday lending industry, perhaps the most significant change has been the rise of bank payday lending. Many of the largest banks have actu-
ally become directly involved in making high-interest short-term loans to their bank customers. The APR is over 300 percent (Carns 2012). Often called “direct consumer products,” banks prefer to deposit advance loans” by the bank, these loans are thought to contribute heavily to the indebtedness of the bank account holders. In part because of their charged usurious rate terms, these bank customer’s practices have become debt to their banks for 175 days per year or more. Under the maximum length of time the FDIC advises is appropriate (Center for Responsible Lending 2011). Yet, despite the growing industry practices, banks prefer to keep the practice of the public and regulators. The Wall Street Journal, Richelle Meissnick, a Wells Fargo spokes-
man said Main Street, an online personal finance publication (Skowronski 2011) woman told, “You’re never going to walk into a store and see a poster about this product in California.”

Regulatory Capture as De Facto Deregulation

While Prop 103 passed in 1988, it took a generation for its most controversial regula-
tions to take effect, establishing the territorial rating system as a primary factor in determining rates, to be implemented. Insurers blocked the full implementation of 103 for an entire gener-
ation. Their success in stymieing enforcement was due in large part because they waged a stealth campaign against regulation known as regulatory capture, which looked to restructure the rating system and much of 103 ineffective.

Regulatory capture may occur for a number of reasons, including having regulated firms influencing the appointments or elections of weak and underfunded oversight agencies. The end result is often the absence of toughness in the actual enforcement practices on the markets or industries these regulators are charged with policing (Cooper
Second, for those with federal student loans, the legislation lowers the loan repayment caps to 10 percent (down from 15 percent) of their monthly discretionary income. Third, it doubles funding for Pell grant awards by pegging it to inflation and adding $820,000 more grants by 2024. Fourth, the act provides loan debt forgiveness after 20 years for some borrowers (Baker and Herzenhorn 2010).

This act has been complemented by the work of the newly created Consumer Financial Protection Bureau. The CFPB, in cooperation with relevant federal agencies like the Department of Education, has engaged a two-pronged approach targeting consumers and lenders. For consumers, it launched a financial literacy campaign via a recently released report as means to raise greater awareness about student-borrower about the traps of private loans (United States Consumer Financial Protection Bureau and US Department of Education 2012). For lawmakers, the CFPB has issued recommendations to Congress, as charged by Dodd–Frank, about best regulatory practices to rein in private student loan abuses throughout the life of the loan, including fuller and less complicated initial contacts with prospective borrowers, improving underwriting and eligibility standards, and more flexible bankruptcy protections for private loan borrowers (Chopra 2012).

Conclusion

As Sherraden explained to a Washington Post staff writer in the spring of 1990, asset-building programs "are intended to help low-income Americans get what most Americans strive for: a college education or vocational training, a home, and a secure retirement [income]." (Spencer 1990). However, in recent decades, financial frack has become more visible and pronounced in ever more devastating connotations—homeownership, education, and employment, as well as the related expenses of transportation, health care, and other necessities of life. This is due in part to the increasing burden of student debt. While the financial crises of 2008 and 2011 have highlighted the systemic risks posed by student debt, it is clear that these risks are not confined to the financial sector. The rise in student debt has also had a significant impact on the broader economy, as rising debt levels have led to increased risk-taking by both students and lenders. This, in turn, has led to higher interest rates and reduced access to credit, particularly for those with lower incomes. As such, the debate over the role of student debt in the national economy is likely to continue to be a significant one.

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Notes

1. The rich, bipartisan recent history of asset building for the poor tends to be overlooked (Seidman 2001). For example, HUD Secretary Jack Kemp actively promoted asset building by low-income households during the George H. W. Bush Administration. The first Individual Development Account (IDA) bill was introduced in the House by Tony Hall (OH) and the Senate by Bill Bradley (NJ). As a presidential candidate, Bill Clinton endorsed IDAs in 1992 and then included them in his early welfare reform proposal in 1994. Republicans in the House (John Kasich of Ohio) and Senate (Dox Cates of Indiana) were sponsors of IDA and have been credited for the inclusion of IDAs in the Welfare Reform Act of 1996. Thereafter, J.C. Watts (R-Okl) and James Talent (R-MO) proposed family development accounts as part of the American Community Renewal Act. For more, see Laurence Seidman, "Assets and the Tax Code" in Thomas Shapiro and Edward Wolff, eds. Assets for the Poor (NY: Sage, 2010), 358.


4. This provision was confirmed by a 1996 unanimous Supreme Court decision in Smiley v. Citizenship—whereby the Rehnquist court ruled that fees were in essence interest rates and were subject to adherence to the consumer protection laws of the states where bank customers resided, effectively allowing rates to be exportable across state lines. Unfettered from the
various state usury laws, fee-based income (or simply fee income) began its rapid ascent in the consumer credit industry. Those affected first were bank credit card issuers. According to Roberts Manning, thanks largely to Smiley, "Penalty fee revenue has climbed from $1.7 billion in 1996 to $3.7 billion in 2001. The average fee has jumped from $12 in 1996 to $30 in 2002. Incredibly, combined penalty ($7.3 billion) and cash advance ($3.8 billion) fees equal the after-tax profits of the entire credit card industry ($11.13 billion) in 2001." One corner bank's total, affiliation-related revenues jumped from $28.98 million in 1994 to $51.57 million in 1996 (new fee structure imposed in second half of the year), then to $73.03 million in 1997 and then to $76.03 million in 1998 when it was acquired by FirstUSA credit card company (Bank One). During this period, for example, returned check fees for this regional bank jumped from $200,000 to $2.85 million. Statement by Robert D. Manning, "Hearing on 'Role of FCRA in the Credit Granting Process'" on Financial Institutions and Consumer Credit, House Financial Services Committee, June 12, 2003.

5. Inflation increased by 75 percent between 1978 and 1984. During the same period, total Pell dollars at traditional two- and four-year institutions increased by 52 percent and 69 percent, respectively. For more information, see Lee (1985).


7. For more information, see "An Update on Emerging Issues in Banking" from FDIC, January 2003.


9. Based on a study of 376,369 online applicants who applied between June 10 and July 11, 2010. Of those applying, the average annual salary was $41,753, and nearly 50 percent were homeowners. See "Payday Loan Industry Report 2010 Statistical Analysis of Pros and Cons." Prepared by PersonalMoneySource.com, September 2010.

10. Not that the payday lending industry was vital to the livelihood of America's financial economy. After all, borrowers receive only $38.5 billion in these short-term loans each year, an amount that barely registers a blip on the nation's financial radar. The idea that payday lenders have an impact on the larger economy and are partly responsible for the financial crisis has lived by the group's trade association as one of the fifteen great myths told about the industry. However, payday lending—which even more than the subprime mortgage market has a deleterial business model at its core—reveals a story impossible to tell elsewhere: how the reckless and unsound financial practices of shadow banks have infected mainstream banks. For additional information, see Jessica Silver-Greenberg, "Payday Lenders Go Hunting," Wall Street Journal December 24, 2010; "About the Payday Advance Industry: Mysts vs. Reality" at the trade association website.

11. This includes 87.9 percent of households that drove to work, see chapter 1. National Summary of "Journey to Work." Census Transportation Planning Products.

12. Within the United States, 47 of 50 states have compulsory vehicle insurance laws. Car finance insurance liability coverage in the form of proof of indemnification—via the uninsured pay- ing an additional amount vehicle fee (Virginia) or posting a special cash bond (Mississippi and New Hampshire)—must be demonstrated by monies in the three states where it is legally permissible to drive without buying any auto insurance.

13. Other forms of regulatory capture are identification with the industry and sympathy with the particular problems of the firms efforts to meet standards, see Toni Makkabian and John Braithwaite, "In and Out of the Revolving Door: Making Sense of Regulatory Capture." Journal of Public Policy 12(1):37-52 (2002).

14. These have certainly been major developments in rulemaking regarding auto insurance and mortgage markets. However, space and time constraints prevent a fuller discussion of the latest changes in these two critical spheres.

15. For more discussion of equity stripping of today's middle class as well as some potential pitfalls of asset building, see Robert Hillelson, "The Retirement Savings Drain: The Hidden and Excessive Costs of 401(k)s." Demos (2012). According to Hillelson, the average 401(k) account holder lost $35,000 in fees and less earnings over the life of the plan.

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