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Dude, Where's My Car Title?: The Law, Behavior, and Economics of Title Lending Markets

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DUDE, WHERE'S MY CAR TITLE?: THE LAW, BEHAVIOR, AND ECONOMICS OF TITLE LENDING MARKETS

*Kathryn Fritzdixon**
*Jim Hawkins***
*Paige Marta Skiba****

Millions of credit-constrained borrowers turn to title loans every year to meet their liquidity needs. Legislatures and regulators have debated how to best regulate these transactions, but surprisingly, we still know very little about the customers who use title loans. This Article reports findings from the first large-scale academic study of title lending customers. We surveyed over 450 title lending customers across three states and obtained information about customers' demographic and behavioral characteristics.

Based on the results of our survey, and guided by insights from behavioral economics, this Article seeks to reframe the title lending debate. Instead of focusing on the risks and consequences of borrowers' cars being repossessed, as the vast bulk of the literature does, we argue that the primary problem that most borrowers face is underestimating the true cost of taking out a title loan. Borrowers' survey responses demonstrate that many borrowers are overly optimistic and experience self-control problems that affect their ability to make timely loan payments. We argue that these deviations from the assumptions of classical economics do not warrant an outright ban of title lending, but they do provide room for policy interventions. Policymakers can improve efficiency in title lending markets by requiring

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lenders to disclose to consumers the likely experiences they will have with their title loans rather than merely requiring lenders to communicate pricing information.

TABLE OF CONTENTS

I.	INTRODUCTION.....	1014
II.	METHODOLOGY.....	1018
III.	TITLE LENDING LAW.....	1021
	A. <i>Idaho</i>	1022
	B. <i>Georgia</i>	1024
	C. <i>Texas</i>	1025
IV.	THE DEMOGRAPHICS OF CUSTOMERS IN TITLE LENDING MARKETS.....	1027
	A. <i>Sex</i>	1029
	B. <i>Race</i>	1030
	C. <i>Age</i>	1031
	D. <i>Occupation</i>	1032
	E. <i>Educational Attainment</i>	1034
	F. <i>Use of Other Financial Service Products</i>	1034
	G. <i>Use of the Loan Proceeds</i>	1036
	H. <i>Borrowers' Means of Getting to Work</i>	1037
V.	THE BEHAVIORAL ECONOMICS OF TITLE LENDING.....	1038
	A. <i>Optimism and Overconfidence</i>	1041
	B. <i>Choice Over Time</i>	1044
	C. <i>Limited Attention</i>	1047
VI.	CONCLUSION AND POLICY RECOMMENDATIONS.....	1050

I. INTRODUCTION

Millions of people who are outside the mainstream banking system turn to title loans each year as a means of accessing credit.¹ Every year around 7500 title lenders make more than \$1.5 billion in loans across the country.² In Texas alone in 2012, borrowers took out almost \$500 million in title loans.³ Title loans are high-cost, short-term, small-dollar loans secured by a vehicle that the borrower usually owns outright. The most

1. See generally Jim Hawkins, *Credit on Wheels: The Law and Business of Auto Title Lending*, 69 WASH. & LEE L. REV. 535 (2012) (describing title lending transactions) [hereinafter Hawkins, *Credit on Wheels*].

2. Jean Ann Fox et al., *Driven to Disaster: Car-Title Lending and Its Impact on Consumers*, CENTER FOR RESPONSIBLE LENDING (Feb. 28, 2013), <http://www.responsiblelending.org/other-consumer-loans/car-title-loans/research-analysis/CRL-Car-Title-Report-FINAL.pdf> (finding that “approximately 7,730 car-title lenders operate in at least 21 states costing borrowers \$3.6 billion each year in interest on \$1.6 billion in loans”).

3. OFFICE OF CONSUMER CREDIT COMMISSIONER, 2012 CREDIT ACCESS BUS. ANN. REP. 3 (May 6, 2013), available at http://www.occc.state.tx.us/pages/publications/consolidated_reports/CAB/050613%20CAB%20Annual%20CAB%20Report.pdf.

common term for the loan is one month, the interest rate charged is commonly around 300% (when expressed as an annual percentage rate), and the lender has the right to repossess the borrower's vehicle if the borrower defaults on the loan.⁴

The fact that these loans typically have high interest rates and threaten to deprive borrowers of their means of transportation has generated significant concern about the loans' welfare effects at both the state⁵ and federal level.⁶ Law on title lending differs greatly throughout the country, with some states banning the industry entirely and others allowing it to operate with virtually no oversight. It is also in flux. For instance, in 2008, New Hampshire effectively shut the doors of all of its title lenders by imposing a thirty-six percent interest rate cap,⁷ but then repealed the cap and welcomed lenders back only four years later.⁸ Even local governments in cities across the country, like Chicago, are currently considering regulations to restrict title lending.⁹ The Consumer Financial Protection Bureau, the federal agency in charge of consumer credit regulation, has the power to pass rules for title lenders¹⁰ and has shown interest in fringe banking companies,¹¹ but is still in the midst of considering what actions to take.

This regulatory uncertainty entreats a critical analysis of how lenders and customers act in title lending markets. A general examination of consumer credit markets is insufficient because it misses the unique concerns generated by title lending. Moreover, a theoretical analysis of how classical economic principles would operate in the title lending market is inadequate because customers frequently deviate from the assumptions made in these models.¹² As Oren Bar-Gill has noted, "Regulation should

4. See generally Hawkins, *Credit on Wheels*, *supra* note 1.

5. See, e.g., *Gov Vetoes Bill to Raise Title Loan Interest in NH*, YAHOO! NEWS (July 6, 2011, 4:28 PM), <http://news.yahoo.com/gov-vetoes-bill-raise-title-loan-interest-nh-202828930.html> (discussing the New Hampshire Governor's decision to veto a bill permitting title lending because of the risk title lending poses to borrowers' continued employment).

6. See, e.g., 146 CONG. REC. H5181-02 (daily ed. June 27, 2000) (statement of Rep. Mascara) (arguing that title lending customers "depend on their automobiles and trucks for transportation to their jobs, vital medical appointments, and school for their children" and concluding that "the loss of a vehicle through an unfair foreclosure often results in the loss of a job or other serious consequences").

7. Garry Rayno, *Lynch Vetoes Bill that Would Allow Interest Rates to Top 400% a Year*, UNION LEADER (Jan. 27, 2012, 2:48 PM), <http://www.unionleader.com/article/20120127/NEWS06/120129914&template=mobileart>.

8. Garry Rayno, *NH Joins Other States to Help Protect Consumers Against Predatory Lenders*, UNION LEADER (Oct. 6, 2012, 8:02PM), <http://www.unionleader.com/article/20120127/NEWS06/120129914&template=mobileart>.

9. See Press Release, City of Chicago, Mayor Emanuel Announces New Reforms to Protect Chicago Families from Financial Fraud (Dec. 5, 2012), available at http://www.cityofchicago.org/city/en/depts/mayor/press_room/press_releases/2012/december_2012/mayor_emanuel_announcesnewreformstoprotectchicagofamiliesfromfin.html [hereinafter Press Release, City of Chicago].

10. See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (giving the Bureau authority to "regulate the offering and provision of consumer financial products or services under the Federal consumer financial laws").

11. See Press Release, City of Chicago, *supra* note 9 (describing a partnership between the Bureau and the city of Chicago aimed at stopping title lending abuses).

12. See *infra* text accompanying notes 138-90 (outlining several ways people behave in opposition to the predictions of classical economics).

only be considered where such specific evidence proves the existence, in the specific market, of a behavioral market failure that generates significant welfare costs [A]ny legal intervention must be based on a detailed, market-specific inquiry.”¹³

Although other fringe banking issues have received significant critical attention in the legal literature,¹⁴ most of the important empirical questions about title lending remain unanswered, especially questions surrounding the characteristics and behavior of people who use title loans.¹⁵ To craft optimal title lending regulation, however, policymakers need to understand who uses title loans and why, what risks people face in using them, and whether people using title loan products conform to the assumptions of the rational actor model used in traditional economics (and by many policymakers). In other alternative financial services markets, significant information about these issues already exists. The Federal Reserve’s Survey of Consumer Finances asks subjects about payday loan use,¹⁶ and the Federal Deposit Insurance Corporation (“FDIC”) National Survey of Unbanked and Underbanked Households asks about alternative financial services other than title loans.¹⁷ Similarly, Michael Barr gathered detailed information about the demographic characteristics of consumers using a wide variety of short-term credit other than title loans.¹⁸ But, none of the existing scholarship answers these critical questions for title lending markets.

This Article is the first large-scale empirical investigation of the customers who use title loans. Based on a survey of over 450 customers, in three states, we find that the typical title lending customer has a moderate level of education, is middle-aged, is white, and is a woman. Using survey evidence, we make the case that in general, customers suffer from behavioral biases that impede perfectly rational use of the title loan product. Namely, they are overly optimistic, have limited self-control, and display limited attention. Yet, the results are not overwhelming, and the responses in our surveys discredit the idea in some prior work that title lending customers are a vulnerable, irrational population.

13. Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749, 801–02 (2008).

14. For some recent examples in the legal literature, see Mechele Dickerson, *Vanishing Financial Freedom*, 61 ALA. L. REV. 1079 (2010); Richard Hynes, *Payday Lending, Bankruptcy, and Insolvency*, 69 WASH. & LEE L. REV. 607 (2012); Angela Littwin, *Beyond Usury: A Study of Credit-Card Use and Preference Among Low-Income Consumers*, 86 TEX. L. REV. 451 (2008); Ronald J. Mann & Jim Hawkins, *Just Until Payday*, 54 UCLA L. REV. 855 (2007); Christopher L. Peterson, *Usury Law, Payday Loans, and Statutory Sleight of Hand: Salience Distortion in American Credit Pricing Limits*, 92 MINN. L. REV. 1110 (2008).

15. See *infra* text accompanying notes 91–100 summarizing the existing literature.

16. Brian K. Bucks et al., *Changes in U.S. Family Finances, From 2004 to 2007: Evidence From the Survey of Consumer Finances*, FED. RESERVE BULLETIN A47, (Feb. 2009), available at http://www.federalreserve.gov/econresdata/scf/scf_2007.htm.

17. 2011 FEDERAL DEPOSIT INSURANCE CORPORATION NATIONAL SURVEY OF UNBANKED AND UNDERBANKED HOUSEHOLDS 1, 6 (SEPT. 2012), available at http://www.fdic.gov/householdsurvey/2012_unbankedreport_app_g.pdf [hereinafter FDIC SURVEY].

18. Michael S. Barr et al., *Borrowing to Make Ends Meet*, in NO SLACK: THE FINANCIAL LIVES OF LOW-INCOME AMERICANS 133, 146–51 (Michael S. Barr ed., 2012) (reporting demographic information about short-term loan borrowers in a study of households in Detroit).

This Article aims to reframe the debate over title lending. Instead of merely focusing on the risk and consequences of repossession, we argue that the primary risk the vast majority of consumers face using title loans is that they will underestimate the true cost of the loan. Consumers, we contend, make systematic mistakes as they consider the loan and weigh its perceived costs and benefits. Repossession affects few borrowers, and our evidence indicates that most borrowers will not lose their only way to work because of repossession. Thus, prohibitions on title loans based on the premise that borrowers are frequently losing their vehicles are misguided. The optimal regulatory response, we argue, is requiring disclosures that inform customers of the true cost of title lending, including the likely ways in which the borrower will use the loan and not merely the pricing of the loan.

We begin in Part II by explaining the methodology of our survey and describing the regulatory reports that we obtained for this paper. We partnered with a large title lending company to administer surveys, informed by previous behavioral economics literature, to all customers, who came into ten different stores in three different states (Idaho, Georgia, and Texas), to take out a title loan or make a payment on an existing title loan. The survey asked about the borrowers' demographics, loan usage patterns, and time and risk preferences. We also obtained reports from the Idaho and Texas state regulatory agencies to determine the proportion of cars being used as collateral that are repossessed.

Part III describes the law that currently governs title lending at the federal level and locally in the three jurisdictions in which we surveyed customers. This Part explains the legal backdrop against which title loan companies operate. It serves as a general introduction to title lending law and offers a starting point as we discuss our policy recommendations.

Part IV discusses the demographics of the customers in our survey. We find that the typical title lending customer is an older, white woman who is moderately well educated. It also considers the demographic makeup of customers surveyed in previous studies of fringe banking customers for comparison, and we also compare title lending customers to the general populations in Georgia, Idaho, and Texas.

In Part V, we review the behavioral economics literature relevant to credit markets serving low-income households. We discuss the theoretical underpinnings and review the empirical and experimental support for a number of behavioral anomalies. We find that title customers are moderately overly optimistic about the time it will take them to pay off their loans and mispredict their ability to save to pay off the loan in the near future.

Finally, we conclude in Part VI by discussing our study's implications for title lending policy. We suggest that policymakers should use behaviorally informed disclosures to maximize efficient use of title loans. By disclosing pattern-of-use information along with pricing early enough in the transaction to affect consumer decision making, the law can aid in

combating the biases customers experience when considering title loans. Finally, we argue that states that have prohibited title lending have done so without sufficient empirical warrant; the risk of customers losing their jobs due to repossession has been vastly overstated and title lending customers are not the irrational, vulnerable population that previous scholarship has envisioned.

II. METHODOLOGY

To learn more about title lending customers, we surveyed over 450 borrowers across ten locations (title lending firm storefronts). To administer the survey, we partnered with a large title lending firm that operates in numerous states. By doing so, we were able to reach a much larger sample of customers than other research has been capable of reaching. For example, one of us (Jim Hawkins) previously attempted to survey title lending customers by positioning research assistants outside title lending locations and asking people to participate as they left the store.¹⁹ Using this method, he was only able to survey thirty-five customers after 100 person-hours of work. By partnering with the lender we were able to survey a much larger sample, 453 customers.²⁰ Our approach follows previous studies in other consumer credit markets that have successfully partnered with firms to reach a larger sample.²¹

We created the survey instrument using standard demographic and behavioral economic questions, as well as questions about the borrowers' expectations for the loans and their usage patterns. The behavioral questions are used to determine how much risk borrowers are willing to accept and how much they care about the future. We developed the questions for our survey by reviewing the literature on title lending specifically and behavioral economics more generally, by using the prior experience Hawkins had surveying title lending customers with a similar instrument, and by the company pre-testing an earlier draft of the survey instrument with a small group of customers.²² We included four questions on the survey that the company specifically wanted answered. The

19. See generally Hawkins, *Credit on Wheels*, *supra* note 1.

20. Other empirical research on consumer credit use has similar numbers of survey subjects. See, e.g., Emma Davies & Stephen E. G. Lea, *Student Attitudes to Student Debt*, 16 J. ECON. PSYCHOL. 663, 667 (1995) (140 subjects); Jeff Joireman et al., *Concern with Immediate Consequences Magnifies the Impact of Compulsive Buying Tendencies on College Students' Credit Card Debt*, 44 J. CONSUMER AFF. 155, 162 (2010) (249 subjects); Phylis M. Mansfield et al., *Self-Control and Credit-Card Use Among College Students*, 92 PSYCHOL. REP. 1067, 1072 (2003) (165 subjects); Nathalie Martin, *1,000% Interest - Good While Supplies Last: A Study of Payday Loan Practices and Solutions*, 52 ARIZ. L. REV. 563, 597 (2010) (109 subjects).

21. See, e.g., Marianne Bertrand & Adair Morse, *Information Disclosure, Cognitive Biases, and Payday Borrowing*, 66 J. FIN. 1856 (2011) (partnering with a payday loan firm to test the effects of different disclosure regimes).

22. The only important change made after the pretesting was to eliminate a question about annual income because it did not appear that customers were answering the question we intended to ask, such as stating weekly or monthly income amounts instead of annual income amounts. Because other research discusses title lending customers' incomes, we did not pursue this issue. See Nathalie Martin & Ernesto Longa, *High-Interest Loans and Class: Do Payday and Title Loans Really Serve the Middle Class?*, 24 LOY. CONSUMER L. REV. 524, 547 (2012).

questions the company wanted included were #11, 12, 13, and 19. Other than reviewing our research to ensure the company remained anonymous, the company did not have any say in our results. The survey is presented in *Appendix A*.

The surveys were completed in November and December 2012. The company chose ten representative stores in three different states: Idaho, Georgia, and Texas. The states have three distinct approaches to regulating title loans, although there are similarities that allow us to meaningfully compare consumers across all states. All three states allow very high interest rates on title loans and have some form of disclosure requirement.²³

We mailed fifty surveys to each title lending location (three in Texas and Georgia and four in Idaho), along with directions on how to administer the survey and forms for record keeping. Each title lender employee was instructed to offer the survey to all customers who took out or made a payment on a loan as long as they had not already completed a survey. The borrowers put their surveys in envelopes and sealed them so that they could be sure that their answers were confidential. All customers who completed the survey were given an informed consent form, and the University of Houston Committee for the Protection of Human Subjects approved the study.²⁴ In return for completing the survey, each borrower received a \$10 Target or Wal-Mart gift card. To ensure that no one completed more than one survey, the borrower's name was checked against the list of individuals who had already received a gift card. The employee recorded daily the number of completed surveys and the number of individuals who turned down the survey. The response rate was high at 78.8%.²⁵ Broken down by state, surveys were completed by 200 borrowers at four stores in Idaho, 149 borrowers at three stores in Texas, and 104 borrowers at three stores in Georgia.

By partnering with the title lending company, we were also able to offer the survey to all customers, making selection errors less likely at the customer level, though they may still be present at the store level. Thus while the stores were not randomly selected, the survey was offered to the entire population of borrowers at those stores during the study period.

Although we have a larger sample size than many other studies, there are still some limitations to our research design. First, the survey data is all self-reported, and we do not attempt to verify the answers.

23. See *infra* Part III. The different regulatory approaches are specifically discussed, along with the implications of these differences.

24. The protocol number is 13070-EX.

25. From our completion reports from eight of the ten stores, 396 customers completed the survey, and 104 declined to take the survey. The two stores that did not provide completion reports also had fewer completed surveys, so it is likely the response rate would be lower if data from those stores were available. Since together they represent only twenty percent of the planned surveys, this effect would not be too severe.

This approach, however, is frequently used in the literature on consumer credit products.²⁶

Second, we only surveyed borrowers at ten locations of one company so our sample is not nationally representative. In one sense, this is beneficial; because the relevant laws in our states are similar enough that we can aggregate the borrowers across stores. On the other hand, this means that we cannot directly generalize our results to the national level. Most other studies of title lending have the same limitation, and we do not have reason to believe that our ten stores are significantly different from other stores operated by this lender.

What may be a larger limitation is the fact that we have only partnered with one company. If borrowers who choose our title lending company are significantly different from those that choose other title lenders, this will create selection bias in our results.²⁷ Most other studies in this area are also conducted with just one partner company, however, so this limitation is not unique to our paper.²⁸

In addition to the survey data, we also gathered data on the title lending industry from the state regulatory agencies in Texas and Idaho.²⁹ Importantly, this data includes the repossession rates in these two states. The data provides additional insight into the consequences of title lending. Georgia does not regulate title loans at the state level through a statewide licensing requirement,³⁰ so data about repossession rates in Georgia does not currently exist. We present this data with the caveat that it is originally self-reported by the lenders and not subject to review by the state agencies.

The reports from state regulators show that less than 10% of cars are repossessed in the two states at hand. In Idaho in 2011,³¹ customers took out 27,510 new title loans.³² Of these loans, 2694 resulted in a vehicle being repossessed (with the other borrowers retaining their vehicles);³³ thus, 9.79% of title loans in 2011 in Idaho resulted in repossessions. In Texas in 2012, 7.83% of customers using single payment title

26. See Jim Hawkins, *The CARD Act on Campus*, 69 WASH. & LEE L. REV. 1471, 1484 (2012) (collecting studies using this approach for credit card research).

27. For example, the company with which we partnered does not require a pay stub in Georgia, but at least one local competitor does require a pay stub to make a loan—meaning that customers who cannot provide a pay stub may be disproportionately represented in our company's customer base.

28. See, e.g., Sumit Agarwal, et al., *Payday Loans and Credit Cards: New Liquidity and Credit Scoring Puzzles?*, 99 AER PAPERS AND PROCEEDINGS 412 (2009); Bertrand & Morse, *supra* note 21 (partnering with a single payday lender).

29. The data from New Mexico has been extensively discussed in Martin and Adams' work. See generally Nathalie Martin & Ozymandias Adams, *Grand Theft Auto Loans: Repossession and Demographic Realities in Title Lending*, 77 MO. L. REV. 41, 45 (2012). Similarly, Hawkins' article *Credit on Wheels* presents the regulatory data from Virginia, Oregon, Illinois, and Montana. See generally Hawkins, *Credit on Wheels*, *supra* note 1.

30. See *infra* text accompanying note 72.

31. The 2011 data is the most current data available from Idaho regulators at the time of writing.

32. E-mail from Anthony Polidori, Idaho Dep't of Fin. (Jan. 8, 2013, 11:09 CST) (on file with author) [hereinafter E-mail from Anthony Polidori].

33. *Id.* 2,261 vehicles were actually sold by the lender.

loans had experienced repossessions.³⁴ Texas' report does not discuss how many vehicles were redeemed by borrowers, so the figures overstate the number of vehicles borrowers actually lost.³⁵

III. TITLE LENDING LAW

This Part offers details about the title lending laws in the three states we studied. This description provides the legal context for how states have approached title lending and affords us the opportunity to offer new regulatory directions in light of the existing laws.

States have adopted a variety of approaches to regulating title lending.³⁶ Some states effectively ban title loans by setting an interest rate cap at such a low rate that no lenders will operate there,³⁷ while others authorize title lending with few laws even tailored to title loans³⁸ or allow lenders to circumvent usury caps.³⁹ Other states permit and regulate title loans through existing laws designed to address other types of credit, such as pawnshop lending.⁴⁰ Finally, some states have laws that were created specifically to address title loan transactions.⁴¹

Title loans in all of the states we studied are governed by the federal Truth in Lending Act ("TILA"). Among other requirements, TILA obligates lenders to disclose the total finance charges for title loans and to present the cost of loans as an annual percentage rate ("APR").⁴² In addition to TILA, the Talent-Nelson Amendment prevents lenders in any state from charging more than thirty-six percent APR to members of the military.⁴³ This statute has effectively ended traditional title lending to military personnel and their family/dependents.⁴⁴ Finally, the Consumer Financial Protection Bureau has authority to regulate title lending,⁴⁵ although it has not yet enacted any title lending regulations.

34. *Financial Services Activity Reports*, OFF. CONSUMER CREDIT COMM'R, <http://www.occc.state.tx.us/pages/publications/FinSvcsActivityRpts.html#CABRpts> (last visited Mar. 29, 2014). There were 27,219 repossessions for the 347,459 customers with whom companies worked in 2012. *Id.*

35. For instance, the New Mexico state report separates out vehicles repossessed and vehicles redeemed. See Martin & Adams, *supra* note 29. Idaho indicates both the number of vehicles repossessed and the number sold. E-mail from Anthony Polidori, *supra* note 32.

36. See Hawkins, *Credit on Wheels*, *supra* note 1, at 572–88 (surveying state title lending laws).

37. See, e.g., 9 VT. STAT. ANN. tit. 9, § 41a(b)(4) (West 2014) (capping loans secured by vehicles older than the previous model year at 20% APR).

38. See, e.g., ARIZ. REV. STAT. ANN. § 44-291(G) (2014) (setting a generous interest rate cap on title loans without other laws regulating the industry).

39. See *infra* text accompanying notes 80–90 (discussing how title lending companies operate in Texas).

40. See *Floyd v. Title Exch. & Pawn of Anniston, Inc.*, 620 So. 2d 576, 579 (Ala. 1993) (holding that Alabama's pawn laws apply to title loans).

41. E.g., TENN. CODE ANN. § 45-15-105 (West 2014).

42. 15 U.S.C. §1632(a) (2012).

43. 10 U.S.C. § 987(b), (d)(2)(A) (2012).

44. See generally Patrick M. Aul, *Federal Usury Law for Service Members: The Talent-Nelson Amendment*, 12 N.C. BANKING INST. 163 (2008).

45. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010); see generally Jim Hawkins, *The Federal Government in the Fringe Economy*, 15 CHAP. L. REV. 23 (2011) (describing the scope of the Bureau's power over title lenders).

In some places, title lending companies must comply with city ordinances, as well as state and federal law.⁴⁶ In Texas, for instance, Austin, Dallas, Houston, and San Antonio have passed ordinances that regulate how title lending companies offer loans, and other Texas cities are considering similar measures.⁴⁷ Yet, none of the cities in which our survey was administered had ordinances that substantially affect the title loan transaction itself.⁴⁸

The three jurisdictions involved in our survey represent three distinct approaches to title lending regulation. Idaho has a statute specifically designed for title loans; Georgia uses its pawnbroker law to regulate title lending; and Texas, while it has historically allowed lenders to operate under its Credit Service Organization law with minimal oversight, recently enacted some provisions aimed directly at title loan companies. Despite some similarities between specific laws in these different frameworks, such as the requirement that title loan companies obtain licenses with the state or municipal governments,⁴⁹ these states have adopted somewhat different approaches to regulating title lending transactions.

A. Idaho

In Idaho, the general provisions in Article 9 of the Uniform Commercial Code (“U.C.C.”) that deals with secured loans apply to title loans,⁵⁰ except to the extent that an Idaho statute specifically aimed at title loans displaces those general provisions.⁵¹ Thus, like all secured creditors, title lenders in Idaho must meet three specific formalities in order for their security interest to attach to the vehicle.⁵² First, there must be value given by both parties.⁵³ Second, the debtor must have rights in the collateral.⁵⁴ And finally, there needs to be an authenticated security agreement.⁵⁵ In addition to the Article 9 provisions, Idaho’s statute

46. Christopher L. Peterson, “Warning: Predatory Lender”—A Proposal for Candid Predatory Small Loan Ordinances, 69 WASH. & LEE L. REV. 893, 898 (2012).

47. Cindy Ramirez, *El Paso City Council to Vote on Title-loan Regulation This Week*, EL PASO TIMES, Jan. 1, 2013, http://www.elpasotimes.com/ci_22291120/city-votes-title-loan-regulation-this-week.

48. Most of the cities involved in our study have no specific ordinances, and the city ordinances that do apply to our subject stores primarily involve permits and record keeping. See, e.g., MARIETTA, GA. CODE ORDINANCES, 8, ch. 12 art.12 § 050 (2014).

49. The Idaho and Texas state codes both require licensing. IDAHO CODE ANN. § 28-46-503(1) (West 2014); TEX. FIN. CODE ANN. § 393.603 (West 2014). Georgia’s state law authorizes municipalities to license lenders. GA. CODE ANN. § 44-12-136 (West 2014). (“Municipal authorities may license pawnbrokers, define their powers and privileges by ordinance, impose taxes upon them, revoke their licenses, and exercise such general supervision as will ensure fair dealing between the pawnbroker and his customers.”). Some cities have exercised this authority. See, e.g., MARIETTA, GA., CODE ORDINANCES pt 8, ch. 12, art. 12, § 050 (2014) (“It is unlawful for any person to engage in, conduct or carry on within the City of Marietta any pawnshop, as defined herein, without a permit or a currently valid occupation tax certificate to do so.”).

50. U.C.C. § 9-101 (2007).

51. IDAHO CODE ANN. § 28-46-502(3) (West 2014).

52. U.C.C. § 9-201 (2007).

53. *Id.* § 9-203(b)(1).

54. *Id.* § 9-203(b)(2).

55. *Id.* § 9-203(b)(3).

mandates that title lenders include the following information in their title loan agreement: make, model, and year of the titled personal property; VIN and license plate number; name, address and date of birth of the debtor; date the agreement is executed; and the maturity date of the title loan agreement.⁵⁶ Under Article 9, the secured creditor must perfect that interest to obtain priority over other creditors and purchasers,⁵⁷ and maintain perfection throughout various potential changes in the collateral, the jurisdiction in which the collateral is held, and the name of the debtor.⁵⁸

Article 9 leaves the definition of a “default” on the loan for the parties to stipulate in their individual security agreements.⁵⁹ Once a default has occurred, the secured party has a number of rights concerning the collateral. Most importantly, the secured party has the right to take possession after default, so long as there is no “breach of the peace.”⁶⁰ The secured party may also initiate a so-called “Article 9 sale” so long as the sale is conducted in a commercially reasonable manner.⁶¹ The debtor must receive notice from the secured party of such disposition of collateral.⁶² The secured party may also accept and keep the collateral in full or partial satisfaction of the outstanding debt.⁶³ Finally, the debtor may redeem his interest and receive his property back from the secured party if he pays off all of the debt owing.⁶⁴ If the secured party does not comply with the U.C.C. in dealings with the debtor, the debtor may be entitled to certain damages.⁶⁵

In addition to the Article 9 provisions, Idaho’s statute mandates that title lenders include the following disclosure in each loan agreement:

- (1) This loan is not intended to meet long-term financial needs.
- (2) You should use this loan only to meet short-term cash needs.
- (3) You will be required to pay additional interest and fees if you renew this loan rather than pay the debt in full when due.
- (4) This loan may be a higher interest loan. You should consider what other lower cost loans may be available to you.
- (5) You are placing at risk your continued ownership of the titled personal property you are using as security for this loan.
- (6) If you default under this loan the title lender may take possession of the titled personal property used as security for this loan and sell the property in the manner provided by law.
- (7) If you enter into a title loan agreement, you have a legal right of rescission. This means you may cancel your contract at no cost to

56. IDAHO CODE ANN. § 28-46-504(1) (West 2014).

57. U.C.C. § 9-308 (2007).

58. *Id.* § 9-316, 507.

59. *Id.* § 9-601 cmt. 3.

60. *Id.* § 9-609.

61. *Id.* § 9-610.

62. *Id.* § 9-611.

63. *Id.* § 9-620.

64. *Id.* § 9-623.

65. *Id.* § 9-625.

you by returning the money you borrowed by the next business day after the date of your loan.

(8) If you believe that the title lender has violated the provisions of the Idaho Title Loan Act, you have the right to file a written complaint with the Idaho Department of Finance and the Department will investigate your complaint.⁶⁶

Along with these disclosure rules, the state requires that title loans be thirty days in length, but it allows them to be renewed automatically.⁶⁷ It does not impose a limit on the amount of interest the title lender charges for the loan, but it does limit the amount of the loan relative to the value of the vehicle.⁶⁸ There are no limits on the number of times a loan can be rolled over (renewed), but the statute requires that on the third renewal of a loan, the debtor must make an additional principal payment and pay the interest due on the loan. The statute states: “the debtor shall be required to make a payment of at least ten percent (10%) of the principal amount of the original title loan in addition to any finance charges that are due.”⁶⁹

If the debtor defaults on the loan, there are two important rules governing the situation, beyond the general rules in Article 9. First, the lender is required to mail a letter to the debtor informing the debtor that “the debtor has ten (10) days from the date of the notice in which to cure the default.”⁷⁰ Second, the statute specifically prohibits lenders from collecting any deficiency from the debtor personally unless the debtor prevents repossession, damages the vehicle, or commits fraud; the lender’s only recourse is to repossess the vehicle.⁷¹

B. Georgia

Georgia regulates title loans as pawn loans, specifically including title lending in its definition of “pledged goods,” which the statute defines as “tangible personal property, including, without limitation, all types of motor vehicles or any motor vehicle certificate of title, which property is purchased by, deposited with, or otherwise actually delivered into the possession of a pawnbroker in connection with a pawn transaction.”⁷² In addition to the general rules governing pawnbrokers, Georgia’s statute has several rules that apply specifically to title lending.

Georgia has a disclosure requirement with simpler language than the Idaho statute (in addition to other disclosure rules similar to those

66. IDAHO CODE ANN. § 28-46-504(2)(c) (West 2014).

67. *Id.* § 28-46-506(1).

68. *Id.* § 28-46-508(3) (prohibiting loans “in which the amount of money loaned, when combined with the outstanding balance of other outstanding title loan agreements the debtor has with the same lender secured by any single titled personal property, exceeds the retail value of the titled personal property as determined by common motor vehicle appraisal guides”).

69. *Id.* § 28-46-506(3).

70. *Id.* § 28-46-507(1).

71. *Id.* § 28-46-508(2) (West 2014).

72. GA. CODE ANN. § 44-12-130(5) (West 2014).

required by federal law).⁷³ Lenders must include the statement: "Failure to make your payment as described in this document can result in the loss of your motor vehicle. The pawnbroker can also charge you certain fees if he or she actually repossesses the motor vehicle."⁷⁴ Like Idaho, Georgia mandates that title loans be for thirty days,⁷⁵ but unlike Idaho, Georgia's law does not govern rollovers in any way, and it puts caps on the fees that lenders may charge, although the caps are high.⁷⁶

If the borrower defaults, the statute empowers the lender to repossess the vehicle,⁷⁷ but it sets limits on the fees lenders can charge in connection with the repossession.⁷⁸ Like Idaho, Georgia prohibits agreements that make the borrower personally liable for the debt.⁷⁹

C. Texas

Title loan companies in Texas operate under a unique arrangement in which the title loan company does not generally directly lend the customers any money. Instead, they act as Credit Service Organizations ("CSOs"), which are organizations that, under the Texas Finance Code, either improve consumers' credit histories or obtain extensions of consumer credit on behalf of consumers.⁸⁰ As a CSO, the title loan company brokers a loan between the consumer and a third-party lender. The title loan company guarantees the loan for the lender and charges a fee to the customer.⁸¹ The United States Court of Appeals for the Fifth Circuit has affirmed that this statute permits payday lenders to operate in this manner,⁸² and until recently, title loan companies operating as CSOs were

73. *Id.* §§ 44-12-138(b)(5)-(6).

74. *Id.* § 44-12-138(b)(3).

75. *Id.* § 44-12-131(a)(1).

76. *Id.* § 44-12-131(a)(4)(A) ("During the first 90 days of any pawn transaction or extension or continuation of the pawn transaction, a pawnbroker may charge for each 30 day period interest and pawnshop charges which together equal no more than 25 percent of the principal amount advanced, with a minimum charge of up to \$10.00 per 30 day period.")

77. *Id.* § 44-12-131(a)(3).

78. *Id.* § 44-12-131(a)(4)(C) ("In addition to the charges provided for in subparagraphs (A) and (B) of this paragraph, in a pawn transaction or in any extension or continuation of a pawn transaction involving a motor vehicle or a motor vehicle certificate of title, a pawnbroker may charge the following . . . (ii) No more than \$5.00 per day in storage fees, but only if an actual repossession pursuant to a default takes place on a vehicle which was not already in the pawnbroker's possession and only for each day the pawnbroker must actually retain possession of the motor vehicle; and (iii) A repossession fee of \$50.00 within 50 miles of the office where the pawn originated, \$100.00 within 51 to 100 miles, \$150.00 within 101 to 300 miles and a fee of \$250.00 beyond 300 miles, but only if an actual repossession pursuant to a default takes place on a vehicle which was not already in the pawnbroker's possession.")

79. *Id.* § 44-12-137(a)(7).

80. TEX. FIN. CODE ANN. § 393.001(3)(A)-(B) (West 2014).

81. *EZCORP Inc. Reports Operating Results (10-K)*, GURUFOCUS (Dec. 14, 2009), <http://www.gurufocus.com/news/78990/ezcorp-inc-reports-operating-results-10k> ("Our services include arranging loans with independent third-party lenders, assisting in the preparation of loan applications and loan documents, and accepting loan payments for the lenders. We do not make, fund or participate in the loans made by the lenders, but we assist customers in obtaining credit and enhance their creditworthiness by issuing a letter of credit to guarantee the customer's payment obligations to the independent third-party lender.")

82. *Lovick v. Ritemoney, Ltd.*, 378 F.3d 433 (5th Cir. 2004).

under little direct regulation. As in Idaho, title loan companies in Texas had to comply with Article 9's provisions and TILA, but otherwise they had substantial leeway in conducting their business.

In 2011, the Texas legislature passed a law that required CSOs acting as "credit access businesses" to follow certain guidelines starting in January 2012.⁸³ The most significant provisions relate to disclosures title lending companies must make. First, in a conspicuous place at each lending location, title lending companies must post a notice that says:

An advance of money obtained through a payday loan or auto title loan is not intended to meet long-term financial needs. A payday loan or auto title loan should only be used to meet immediate short-term cash needs. Refinancing the loan rather than paying the debt in full when due will require the payment of additional charges.⁸⁴

In addition to this posted disclosure, the statute lays out several other remarkable disclosures that lenders must make,⁸⁵ including the following information:

- (1) the interest, fees, and annual percentage rates, as applicable, to be charged on a deferred presentment transaction or on a motor vehicle title loan, as applicable, *in comparison to interest, fees, and annual percentage rates to be charged on other alternative forms of consumer debt*;
- (2) the amount of accumulated fees a consumer would incur by renewing or refinancing a deferred presentment transaction or motor vehicle title loan that remains outstanding for a period of two weeks, one month, two months, and three months; and
- (3) information regarding the typical pattern of repayment of deferred presentment transactions and motor vehicle title loans.⁸⁶

With regard to title lending in particular, the company must warn customers that "the consumer may be required to surrender possession of the motor vehicle to the lender or other person to satisfy the consumer's outstanding obligations under the loan."⁸⁷ Finally, the new Texas law also imposes reporting requirements on title loan companies.⁸⁸

Beyond these disclosure laws, Texas continues to have little direct title lending regulation. It imposes no limit on the charges companies can assess,⁸⁹ no requirements for how long loans must last, no limits on the number of times a borrower rolls over a loan, and no limit on the loan amount. The rules in Article 9 concerning when a borrower defaults on a loan apply to title loans in Texas. Unlike the laws in Idaho and Georgia which alter the U.C.C.'s rule, Article 9 allows title loan companies to sue

83. TEX. FIN. CODE ANN. § 393.221–393.224 (West 2014).

84. *Id.* § 393.222(a)(3).

85. These pattern of use disclosures are unique because most consumer credit disclosures focus merely on conveying static price information. *See infra* text accompanying notes 177–85.

86. TEX. FIN. CODE ANN. § 393.223(a) (West 2014) (emphasis added).

87. *Id.* § 393.223(b).

88. *Id.* § 393.627.

89. The CSO statute does not limit the amount CSOs can charge for their loan brokering services. *See id.* § 393.001.

borrowers for any amount remaining due on the loan after the collateral is sold.⁹⁰

All of these laws, at both the state and federal level, have been passed without any information about the demographics of title lending customers or their behavioral tendencies. Parts IV and V take up these questions in hope of better informing these legislative decisions.

IV. THE DEMOGRAPHICS OF CUSTOMERS IN TITLE LENDING MARKETS

Understanding who uses title loans is important in assessing whether regulation of title lending is advisable and what types of regulation would be optimal. In other fringe credit markets, we have extensive data on the demographics of customers. The Federal Reserve's Survey of Consumer Finances, for instance, asked households about payday loan use for the first time in 2007, generating a nationally representative sample of borrower information.⁹¹ Similarly, the FDIC National Survey of Unbanked and Underbanked Households asks whether households have used many other alternative financial services, but does not address title loans in their questions.⁹² Thus, in the title lending context, no similar resources for demographic data exist.

Prior work focusing on the demographics of title lending customers has been limited both in its approach to the issue and the factors it considered. Nathalie Martin and Ernesto Longa summarize prior work on the demographics of title lending customers in a recent article.⁹³ The two main studies they discuss are one by Nathalie Martin and Ozymandias Adams from 2012 that found, using data from regulators in New Mexico, that "the average title loan borrower in New Mexico makes between \$ 20,116 and \$ 27,719,"⁹⁴ and one by the state of Illinois which concluded that in 1999–2000, "title loan customers in Illinois earn an average of \$ 19,808."⁹⁵ But, beyond information about customers' income in two states, these studies do not offer a rich picture of who title lending customers are.

Martin and Longa also discuss geographical studies that find that title lenders are more likely to open stores in "low-income neighborhoods with moderate poverty, where a large percentage of the residents are members of racial/ethnic minority groups, young or elderly, or recent immigrants . . . [and where m]any residents . . . also lack a high school di-

90. U.C.C. § 9-609 (2001).

91. Bucks et al., *supra* note 16, at A47.

92. FDIC SURVEY, *supra* note 17, at 29. The other alternative financial services are non-bank money orders, check cashing, or remittances, payday loans, pawnshops, rent-to-own stores, and refund anticipation loans.

93. Martin & Longa, *supra* note 22, at 550.

94. *Id.* (citing Martin & Adams, *supra* note 29, at 76, 77, Tables 12-12.1).

95. *Id.* (citing ILLINOIS DEP'T OF FINANCIAL INSTITUTIONS, CONSUMER CREDIT DIVISION, SHORT TERM LENDING: FINAL REPORT 26, available at <http://www.idfpr.com/dfi/ccd/pdfs/Shorterm.pdf> (last visited Mar. 29, 2014)).

ploma.”⁹⁶ The data from these studies, however, are not about title lending exclusively but include payday lenders, check cashing stores, and other lenders, making it difficult to know which findings are relevant to title lending stores in particular.⁹⁷

In addition, Todd Zywicki has published a series of articles based primarily on interviews with title lenders.⁹⁸ Zywicki argues that title lending customers fall into three groups: moderate income customers with impaired credit histories, lower income customers, and small business owners.⁹⁹ Our work differs fundamentally from Zywicki’s because our empirical strategy involves gaining information directly from customers and not from lenders’ perceptions of customers. We also obtain a wider variety of information about customers than Zywicki.

Our survey offers the first detailed look at the demographics of title lending customers, supplementing the information reported in prior work and, for the first time, addressing more directly some of the key demographic categories, such as education level, gender, and race. Summary statistics for several of the measures are presented in Table 1. We also provide data on the population of the states in which we surveyed customers, where applicable, so that we can compare the proportion of each subpopulation of title lending customers to the same subpopulation in the general population in the state.¹⁰⁰

96. See *id.* at 552 (citing Robin A. Prager, *Determinants of the Locations of Payday Lenders, Pawnshops and Check-Cashing Outlets*, FED. RES. BD., 3, 21 (2009), available at <http://www.federalreserve.gov/pubs/feds/2009/200933/200933pap.pdf>).

97. See, e.g., WILLIAM C. APGAR JR. & CHRISTOPHER E. HERBERT, U.S. DEP’T HOUSING & URBAN DEV., *SUBPRIME LENDING AND ALTERNATIVE FINANCIAL SERVICE PROVIDERS: A LITERATURE REVIEW AND EMPIRICAL ANALYSIS*, U.S. DEP’T HOUSING & URBAN DEV. xi, available at <http://www.huduser.org/Publications/pdf/sublending.pdf> (describing the alternative financial service providers the authors studied as including “check cashing outlets, payday lenders, pawnshops, title lenders, tax refund anticipation lenders, small loan firms, and rent-to-own stores”).

98. See e.g., Todd Zywicki, *Consumer Use and Government Regulation of Title Pledge Lending*, 22 LOY. CONS. L. REV. 425 (2010) [hereinafter Zywicki, *Consumer Use*]; Todd J. Zywicki, *Money to Go*, 33 REG. 32 (2010) [hereinafter Zywicki, *Money to Go*]; Todd Zywicki & Gabriel Okolski, *Potential Restrictions on Title Lending*, 62 MERCATUS ON POL’Y 1 (2009).

99. Zywicki, *Consumer Use*, *supra* note 98, at 426.

100. We obtained data about the population of each state from the U.S. Census Bureau. *American Fact Finder, Georgia* UNITED STATES CENSUS BUREAU, <http://factfinder2.census.gov/faces/nav/jsf/pages/index.xhtml> (insert “Georgia” into the “Community Facts” search box, and select “Go”) (last visited Mar. 25, 2013); *American Fact Finder, Idaho*, UNITED STATES CENSUS BUREAU, <http://factfinder2.census.gov/faces/nav/jsf/pages/index.xhtml> (insert “Idaho” into the “Community Facts” search box, and select “Go”) (last visited Mar. 25, 2014); *American Fact Finder, Texas*, UNITED STATES CENSUS BUREAU, <http://factfinder2.census.gov/faces/nav/jsf/pages/index.xhtml> (insert “Texas” into the “Community Facts” search box, and select “Go”) (last visited Mar. 25, 2014).

TABLE 1: AGE, GENDER, AND RACE OF TITLE LENDING BORROWERS

	Full Sample	Texas		Idaho		Georgia	
		Borrowers	State-wide	Borrowers	State-wide	Borrowers	State-wide
Median Age	40	42.6	33.6	38.6	34.6	43	35.3
Male	41.56%	47.30%	49.60%	39.70%	50.10%	36.89%	48.90%
White	57.78%	42.68%	80.90%	74.87%	93.90%	46.15%	63.20%
Black	17.78%	28.57%	12.20%	0.50%	0.80%	35.58%	31.00%
Hispanic	15.56%	20.41%	38.10%	14.07%	11.50%	11.54%	9.10%
Asian	0.67%	1.36%	4.00%	0.50%	1.30%	0.00%	3.40%
Other	7.56%	6.12%	-	9.55%	-	5.77%	-
Two + races	0.67%	0.68%	1.70%	0.50%	2.10%	0.96%	1.80%

A. Sex

As Table 1 indicates, we find that 41.56% of borrowers surveyed are male, meaning that women are slightly more likely than men to use auto title loans. This finding is similar to the demographics for other alternative financial services. Women are also more likely to use payday loans,¹⁰¹ pawnshops,¹⁰² and rent-to-own services.¹⁰³

A variety of explanations have been offered for why women are more likely than men to use alternative financial service providers. First, men may be less likely to admit that they are experiencing financial need, leaving their wife or partner to seek financing.¹⁰⁴ Second, women may seek loans from title lenders because they bear more financial responsibility for children, and they are more likely to declare bankruptcy than men.¹⁰⁵ But, because our survey captured responses from people both originating loans and making payments on loans, it could be simply that more women were making the payments on loans that were cosigned with a man.

101. Paige Marta Skiba & Jeremy Tobacman, *Do Payday Loans Cause Bankruptcy?* 5, 7 (Vanderbilt Univ. Law Sch. Law & Econ. Working Paper No. 11-13, 2011), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=%201266215.

102. Marieke Bos et al., *The Pawn Industry and Its Customers: The United States and Europe* 5 n.3 (Vanderbilt Univ. Law Sch. Law & Econ. Working Paper No. 12-26, 2012) (finding “women make up 55 percent of pawnshop borrowers”).

103. JAMES M. LACKO ET AL., FED. TRADE COMM’N BUREAU OF ECON., SURVEY OF RENT-TO-OWN CUSTOMERS 38 Table 3.2 (2000) [*hereinafter* FTC SURVEY] (reporting 5.2% of women in the researchers’ sample group had used rent-to-own services in the last five years whereas only 4.5% of men had).

104. Robert W. Johnson & Dixie P. Johnson, *Pawnbroking in the U.S.: A Profile of Customers*, CREDIT RESEARCH CENTER SCHOOL OF BUSINESS GEORGETOWN UNIVERSITY WASHINGTON D.C. 37, 41 (1998).

105. ELIZABETH WARREN & AMELIA WARREN TYAGI, THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE 160–62 (2003).

B. Race

Rows 3 through 7 in Table 1 present our racial statistics. The majority of borrowers are white, at 57.78%. The next most highly represented group is African-Americans at 17.78%, followed by Hispanics at 15.56%. 7.56% of borrowers identified as “Other,” while less than one percent of borrowers were Asian (.67%) or two or more races (.67%). There are also large differences between states. Columns 3–8 of Table 1 break down the survey results by state. For example, Idaho has a significantly higher proportion of white borrowers than either Texas or Georgia. Some commentary criticizes title loans by arguing that title lending companies target minorities.¹⁰⁶ Others, however, claim that minorities do not use fringe credit products at a rate higher than whites after controlling for income.¹⁰⁷

Comparing our survey results to the overall state populations shows that some minority groups are overrepresented among title lending customers as compared to the general population. In Georgia, only 31% of the state population is black, while nearly 36% of the borrowers in our survey classified themselves as black. In Texas, almost 30% of our borrowers are black, while only 12% of the state population is black. On the other hand, only 20% of borrowers in Texas are Hispanic, compared with 38% of the population. And in each survey state, Asians are underrepresented in our borrowers. We did not ask any questions about income, so we cannot control for any income effects. It is possible that if we controlled for the borrowers’ income, the rate of use would not be different in a statistically significant way.

We can also compare the number of minorities using title loans to numbers of the same subpopulation using other alternative financial service (AFS) providers. Table 2 compares our full sample to the people who use two other alternative financial services, payday loans and rent-

106. For only a few of many examples, see URIAH KING ET AL., CTR. FOR RESPONSIBLE LENDING, RACE MATTERS: THE CONCENTRATION OF PAYDAY LENDERS IN AFRICAN-AMERICAN NEIGHBORHOODS IN NORTH CAROLINA 2 (Mar. 22, 2005), available at http://www.responsiblelending.org/north-carolina/nc-payday/research-analysis/racematters/tr006-Race_Matters_Payday_in_NC-0305.pdf (finding “that North Carolina payday lending storefronts are disproportionately located in African-American neighborhoods”); Regina Austin, *Of Predatory Lending and the Democratization of Credit: Preserving the Social Safety Net of Informality in Small-Loan Transactions*, 53 AM. U. L. REV. 1217, 1218–19 (2004) (“Black Americans experience a number of problems in their efforts to obtain and use credit. Of particular concern is their vulnerability to so-called ‘predatory lenders.’ . . . Examples of targeted consumers include women, minorities, low-income wage earners, and senior citizens. The chief objects of criticism are financial firms that conduct business in what is variously known as the subprime, secondary, fringe, or alternative market, including payday lenders, car title pawn operators, small loan and mortgage companies, rent-to-own stores, check cashing outlets, and rapid refund tax services.”) (footnotes omitted).

107. Donald P. Morgan & Kevin J. Pan, *Do Payday Lenders Target Minorities?*, FED. RES. BANK N.Y. (Feb. 8, 2012), <http://libertystreeteconomics.newyorkfed.org/2012/02/do-payday-lenders-target-minorities.html> (finding that blacks and Hispanics do use payday loans more often than whites but concluding that “once we control for financial characteristics—such as past delinquency, debt-to-income ratios, and credit availability, blacks and Hispanics are not significantly more likely than whites to use payday credit”).

to-own stores, as well as people who have used any alternative financial services in the past month (not including title loans).

TABLE 2: RACE OF USERS OF ALTERNATIVE FINANCIAL SERVICES¹⁰⁸

	Title loans	Payday loans	Rent-to-own	All AFS (used in past month)
White	57.78%	57%	57.30%	43.10%
Black	17.78%	30%	31.40%	29.10%
Hispanic	15.56%	8%	8.40%	23.50%
Asian	0.67%	3%	2.00%	2.00%
Other	7.56%	-	2.70%	2.20%
Two+ races	0.67%	-	-	-

As Table 2 indicates, we found there were fewer black and Hispanic individuals among title loan customers compared to users of other fringe credit products. Given the large Caucasian population in Idaho, however, these results might not be generalizable. In addition, black and Hispanic individuals own cars at lower rates than white individuals,¹⁰⁹ which may explain the difference as compared to other fringe credit products.

C. Age

The median age of the title lending borrowers in our survey was 40 years old. In other fringe lending contexts, borrowers are much more likely to be younger. For instance, the FTC found that 51% of rent-to-own customers were between 18 and 34 years old.¹¹⁰ Similarly, 52.49% of pawnshop customers in Florida and 38.15% of those in Texas were between 18 and 34, with 82.81% in Florida and 71.32% in Texas being younger than 45.¹¹¹ Younger people may be more likely to seek credit from alternative financial service providers because they do not have the established credit and income histories to qualify for mainstream credit, so it is remarkable that title lending customers are older.¹¹² The most

108. Rent-to-own data from FTC SURVEY, *supra* note 103, at 41 Table 3.3; Payday loan data from Martin & Longa, *supra* note 22, at 534 (citing *Payday Loan Demographic Study—December 2010*, ONLINE PAYDAY LOANS (Dec. 4, 2010), <http://www.online-payday-loans.org/articles/demographics-december-2010/>); all other data from FDIC SURVEY, *supra* note 17, at Box 6.

109. Robert D. Bullard, *Addressing Urban Transportation Equity in the United States*, 31 *FORDHAM URB. L.J.* 1183, 1191 (2004) (“Nationally, only 7% of white households do not own a car, compared with 24% of African American households, 17% of Latino households, and 13% of Asian-American households.”).

110. FTC SURVEY, *supra* note 103, at 32.

111. See Bos et al., *supra* note 102, at 21 Table 5.

112. AARP PUB. POL’Y INST., A PORTRAIT OF OLDER UNDERBANKED AND UNBANKED CONSUMERS: FINDINGS FROM A NATIONAL SURVEY 57 (2010), available at <http://assets.aarp.org/rg-center/ppi/econ-sec/underbank-economic-full-092110.pdf>; see also Kelly J. Noyes, *Get Cash Until Payday! The Payday-Loan Problem in Wisconsin*, 2006 *WIS. L. REV.* 1627, 1633 (“Payday-loan consumers

likely explanation for this observation is that, unlike in other fringe credit transactions, title lending customers must typically own a vehicle outright to take out a title loan.

D. Occupation

We also asked about the borrowers' occupations. The results of this question are presented in Tables 3 and 4. The first table summarizes the answers we received based on the options we presented, whereas the second classifies the occupations according to the Bureau of Labor Statistics (BLS) Major Occupation Group classification system.¹¹³ We present the second table because almost 30% of borrowers chose "Other" as their occupation. Of those borrowers, however, 84.5% wrote in their occupation.

TABLE 3: OCCUPATION OF BORROWERS

	Full sample	Texas	Idaho	Georgia
Self-employed	17.01%	19.86%	11.34%	23.76%
Construction	6.58%	6.16%	8.76%	2.97%
Sales	7.94%	9.59%	7.22%	0%
Education	3.17%	3.42%	4.64%	6.93%
Healthcare	12.02%	12.33%	14.95%	5.94%
Hotel/Food Services	11.11%	6.85%	11.34%	16.83%
Other	29.25%	30.82%	27.32%	30.69%

Once we classify our borrowers according to the BLS Major Occupation Groups, we are able to describe the employment of 86% of our borrowers.¹¹⁴

also tend to be young adults: 62% of payday-loan customers in Colorado were between the ages of twenty and twenty-nine.”).

113. This is the highest level of the classification systems used by BLS to study compensation and by the Census to identify the occupations of Americans in the American Community Survey. BUREAU OF LABOR STATISTICS, NATIONAL COMPENSATION SURVEY—WAGES, U.S. DEPT OF LAB., <http://www.bls.gov/ocsm/commain.htm> (last visited Mar. 29, 2014).

114. Note that the percentage of self-employed individuals decreased because some people who chose self-employed wrote in what field they work in, effectively putting them into another job category.

TABLE 4: JOBS CLASSIFIED ACCORDING TO THE BLS MAJOR OCCUPATION GROUPS

	Percentage
Professional, technical, and related	5.96%
Executive, administrative, and managerial	2.65%
Sales	9.93%
Administrative support	1.77%
Precision production	1.10%
Machine operators	3.75%
Transportation and materials moving	4.19%
Handlers, equipment cleaners, helpers, and laborers	6.40%
Service occupations	21.63%
Self-employed	15.89%
No job	13.02%
Not classified	13.69%

Our results in Table 3 based on the category chosen by the borrowers shows that 15.89% of our sample was self-employed, compared with 6.2% of the general population in the 2011 Census that identified as “self-employed in own not incorporated business.”¹¹⁵ This finding is significant because past commentary on the industry has argued that title loans could serve as an important (and perhaps the only) source of credit for some self-employed people.¹¹⁶ Any regulatory intervention into title lending markets should weigh the costs of denying access to credit to these individuals. One cost of prohibiting title loans, for instance, is that these small businesses may be unable to obtain credit elsewhere.

Interestingly, we find that 13.02% of our borrowers did not have a job at the time they took the survey. This includes people who identified as housewives or stay-at-home mothers (16 borrowers), as retired or on disability (33), as students (4), and as unemployed (3). For the portion of the jobless borrowers with no income stream, i.e., without family members or entitlement programs supporting them, this finding appears to confirm industry critics’ fears that title lending companies do not evaluate the borrower’s ability to repay the debt before making loans.¹¹⁷ One caveat of the finding, however, is that only 24 of the unemployed borrowers were originating a loan the day they were surveyed; the other 35 customers could have been visiting the store to make a payment on a loan for another employed customer.

115. China Layne, *Changes in Self-Employment: 2010–2011 American Community Survey Briefs*, U.S. CENSUS BUREAU (Jan. 30, 2013), <http://www.census.gov/prod/2013pubs/acsbr11-21.pdf>.

116. Hawkins, *Credit on Wheels*, *supra* note 1, at 544–45; Zywicki, *Consumer Use*, *supra* note 98, at 449.

117. See Hawkins, *Credit on Wheels*, *supra* note 1, at 553–54 (collecting arguments).

E. Educational Attainment

Table 5 presents the educational attainment results from the survey. 52.59% of our customers have at least some college education.

TABLE 5: EDUCATIONAL ATTAINMENT (PERCENTAGE)

	Full sample	Texas	Idaho	Georgia
Less than high school diploma	8.80%	7.43%	7.22%	13.86%
High school diploma	38.60%	28.38%	40.72%	49.5%
Some college	37.92%	43.92%	38.14%	28.71%
College degree	8.58%	13.51%	5.15%	7.92%
Postgraduate	6.09%	6.76%	8.76%	0%

While this may seem low since it implies that almost half of our sample has at most a high school diploma, it is actually very close to the national average for educational attainment.¹¹⁸ Thus, our findings are contrary to the suggestion of Martin and Longa that title lending targets people with low education.¹¹⁹

Also, in comparison to users of other fringe banking products, title lending customers are relatively well educated. 73% of rent-to-own customers had no more than a high school diploma in the FTC's survey,¹²⁰ and over 15% of customers who used any alternative financial service had less than a high school diploma in the FDIC Survey.¹²¹

F. Use of Other Financial Service Products

We asked customers to identify other financial products they use. The answers to this question can inform several significant policy debates. First, one concern that commentators favoring regulatory intervention express about users of fringe credit is whether they have access to mainstream financial products and services.¹²² Our survey can help us understand the extent to which title lending customers are outside of the mainstream banking system. Second, commentary that is critical of prohibiting fringe credit products argues that borrowers who cannot use one type of alternative financial service will simply substitute another prod-

118. Data from the U.S. Census Bureau in 2011. Population 18 and older—56.24%, population 25 and older—56.86%. *Educational Attainment in the United States: 2011 - Detailed Tables*, UNITED STATES CENSUS BUREAU Table X, <http://www.census.gov/hhes/socdemo/education/data/cps/2011/tables.html> (last visited Mar. 25, 2014).

119. Martin & Longa, *supra* note 22, at 552.

120. FTC SURVEY, *supra* note 103, at 32.

121. FDIC SURVEY, *supra* note 17, at 75.

122. See generally Michael S. Barr, *Banking the Poor*, 21 YALE J. REG. 121 (2004) (describing the difficulties people without bank accounts face and suggesting policies to increase bank utilization rates).

uct that is less efficient.¹²³ Our study can shed light on the extent to which title lending borrowers already actively participate in other credit transactions.

We asked borrowers what other financial services they used at least once in the past year. The results are summarized in Table 6.¹²⁴

TABLE 6: OTHER FINANCIAL SERVICES USED

	Percentage
Checking account	56.67%
Payday loan	16.44%
Check cashing	10.44%
Credit card	18.89%
Prepaid credit card	8.67%
Pawnshop	11.33%
Rent-to-own	4.00%
Borrow from friends or family	13.11%
Personal loan from bank	3.11%
None	10.44%
N	450

Over 40% of our borrowers have not used a checking account in the past year, suggesting that they are unbanked.¹²⁵ Less than 20% have used a credit card in the past year. The title loan customers we surveyed were more likely to be unbanked than other fringe credit users. Rent-to-own customers reported having credit cards (48.4%) and checking accounts (67.5%) at higher rates than the title loan customers.¹²⁶ Similarly, payday loan customers must write a postdated check in order to obtain a loan, so they need to have a checking account.¹²⁷ Given the general belief that people outside of the mainstream banking system are more vulnerable,¹²⁸ this finding raises concerns about title lending customers.

123. Mann & Hawkins, *supra* note 14, at 886–95; Todd J. Zywicki, *The Economics of Credit Cards*, 3 CHAP. L. REV. 79, 98–99 (2002). *But see* Angela Littwin, *Testing the Substitution Hypothesis: Would Credit Card Regulations Force Low-Income Borrowers into Less Desirable Lending Alternatives?*, 2009 U. ILL. L. REV. 403, 403 (arguing that insufficient data support the substitution hypothesis).

124. Because borrowers were asked to choose all they have used, the percentages sum to more than 100%.

125. Because a checking account is the most basic account a person can open at a bank, it is likely that people who do not have a checking account also do not have other bank accounts.

126. FTC SURVEY, *supra* note 103, at 45 Table 3.5.

127. *See* Mann & Hawkins, *supra* note 14, at 857. The website Payday Loan Ranger advertises payday loans for borrowers without a checking account, but this is highly unusual in the industry. *Getting A Payday Loan Without Bank Account*, PAYDAY LOAN RANGER, https://www.paydayloanranger.com/Payday_Loan_Without_Bank_Account.php (last visited).

128. *See generally* Barr, *supra* note 122 (analyzing how low-income communities are affected by market imperfections including having less access to alternative forms of credit).

G. Use of the Loan Proceeds

In our survey, we also asked customers “Why did you take out this title loan?” This allows us to determine whether consumers are using title loans to meet unexpected financial or consumption shocks or are using them for normal, expected expenses. If consumers use the loans for unexpected shocks, then title loans perform the important function of smoothing consumption for people who may not have access to traditional consumer lending institutions.¹²⁹ If, on the other hand, consumers are using the loans to cover normal, anticipated expenses, this may show either a lack of self-control or uncontrolled financial distress.¹³⁰

We also explicitly asked whether the loan is for business expenses. Since automobiles are often one of a person’s largest assets, title loans may provide important financing for self-employed borrowers, as we point out above.¹³¹ Prohibiting title loans would shut down what may be one of the only sources of business credit available for individuals without established borrowing histories with banks. We present the survey results on this question in Table 7.

TABLE 7: REASON FOR TAKING OUT THE LOAN

	Percentage
Business expense	6.00%
Rent/mortgage	20.00%
Medical	7.78%
Gift	13.33%
Utilities	18.67%
Car Repair	17.11%
Education	3.33%
Other	37.78%
N	450

Our results show that only a small proportion of borrowers were using the loan for business expenses. Only 6% of the borrowers listed “business expenses” as a reason for taking out the loan. Our survey cannot address the question of whether this is the only source of business credit available for these borrowers, but it seems like business credit is not a significant portion of the loans.

129. In economic terms, consumption smoothing means spreading the effects of any negative shocks over a long period of time rather than over a short period of time. The desire to smooth consumption is an important assumption of all standard economic models of consumer behavior. It is also supported by empirical evidence. See, e.g., Martin Browning & Thomas F. Crossley, *The Life-Cycle Model of Consumption and Saving*, 15 J. ECON. PERSP. 3 (2001) (discussing the life cycle model framework in economics).

130. See *infra* Part V.B. on self-control issues in behavioral economics.

131. See Zywicki, *Consumer Use*, *supra* note 98, at 426.

Just under a quarter of borrowers used the loan for medical expenses or car repairs, which we believe are most likely to be “emergency” expenses.¹³² In these cases, title loans can serve an important economic purpose of allowing people to spread out the effects of unexpected expenses over a longer period of time. Other reasons, like rent or mortgage payments and education expenses, are more likely to be normal rather than emergency expenses. Twenty-three percent of borrowers selected these reasons. For these borrowers, it is harder to argue that the loans serve this consumption smoothing purpose. “Gifts” was quite large, at almost 14%, but we believe this result is because of the timing of our survey. The surveys were administered in late November and December, so we believe that this number would be lower at another time of the year.

Unfortunately, a significant number of borrowers selected “Other” and did not write down the reason why they took out the loan. For these borrowers, we cannot evaluate their reasons for taking out the loan.

H. Borrowers' Means of Getting to Work

Many opponents of title lending argue that borrowers who are unable to repay the loan will lose their vehicles, and, because of that loss, are at a higher risk of losing their jobs.¹³³ For borrowers to lose their jobs as a result of taking out a title loan, two things must occur. First, customers must lose their vehicles through repossession. Our results show that this does not occur frequently. The regulatory data for Idaho and Texas place the repossession rates per new loan (not per rollover) in both states under ten percent.¹³⁴ Second, after losing the vehicle, borrowers must have no other way to get to work. To address this second condition, question 3 of our survey asks, “If you lost the vehicle that you used to get your loan, how would you get to work?” If most consumers would not have another way to get to work, this would confirm fears that the loss of the vehicle has dire consequences for borrowers’ employment. On the other hand, if most borrowers do have another way of getting to work, it may not cause any disruption in employment.

132. Other expenses, like utilities, could also be emergency expenses, if, for example, the utility bill was unexpectedly high one month, but we cannot distinguish between unexpectedly large bills and normal, expected bills with our question.

133. This argument is ubiquitous in the literature discussing title lending and in policy statements about title lending. For a few examples, see 146 CONG. REC. H5181 (daily ed. June 27, 2000) (statement of Rep. Mascara); Jean Braucher, *Theories of Overindebtedness: Interaction of Structure and Culture*, 7 THEORETICAL INQ. L. 323, 332 (2006); Jeff Peterson, *Predatory Lending: Profile & Analysis*, ARIZ. RURAL POLICY INST., N. ARIZ. UNIV. 5 (Aug., 8, 2007), http://franke.nau.edu/images/uploads/rpi/predatory_lending_080807.pdf.

134. See *supra* Parts II.A and II.C (discussing Idaho’s and Texas’ regulatory reports).

TABLE 8: OTHER TRANSPORTATION TO WORK

	Percentage (n=451)
Do not work outside the home	11.97%
Use public transportation	12.86%
Use another vehicle I own	41.24%
Walk to work	10.42%
Get rides from friends/family	15.96%
Buy a new car	4.88%
No other way to work	14.86%

Our results show that, in fact, most workers would have another way to get to work. Table 8 presents these results.¹³⁵ Over 40% of borrowers reported that they would use another car that they or their family owns. Interestingly, 4.88% stated that they would buy another car if they lost the one used to collateralize the loan.¹³⁶ Less than 15% of borrowers stated that they would have no other way to get to work. While not insignificant, this small percentage suggests that the dire consequences that critics predict are unlikely to occur for the vast majority of title borrowers. Rough calculations would place the percentage of title borrowers who lose their jobs as a result of title lending at 1.5%.¹³⁷

With this demographic information, we have a fuller understanding of who title lending customers are. But, merely knowing their characteristics is insufficient as we consider how to best regulate the industry. We next turn to what our survey tells us about how these customers behave.

V. THE BEHAVIORAL ECONOMICS OF TITLE LENDING

“Behavioral economics increases the explanatory power of economics by providing it with more realistic psychological foundation Often these departures are not radical at all because they relax simplifying assumptions that are not central to the economic approach.”¹³⁸ As Camerer and Loewenstein succinctly note, the field of behavioral economics consists, for the most part, of relatively minor deviations from a very

135. Because customers were instructed to select all that apply, the percentages sum to more than 100%.

136. We did not ask any questions about income or wealth, so these customers may not actually be capable of purchasing another vehicle.

137. This would assume that having one’s car repossessed and losing one’s job if one’s car is repossessed are independent. In that case, if 10% of customers have their cars repossessed, and 15% of those customers have no other way to work, then only 1.5% of customers would lose their jobs because of title lending. This is likely not the case, since a borrower whose car is repossessed probably has lower wealth and income than a borrower whose car is not repossessed, and is therefore probably more likely to lack another way of getting to work. The percentage is therefore probably somewhere between our 1.5% figure and the repossession rate in the state.

138. Colin F. Camerer & George Loewenstein, *Behavioral Economics: Past, Present, Future, in* ADVANCES IN BEHAVIORAL ECONOMICS 3,3 (Colin F. Camerer et al. eds., 2004).

strict traditional notion of decision making. Though these changes are often small, such relaxations of the assumption constraining traditional economic thought can vastly improve upon economists' understanding of decision making in a number of contexts. As we argue below, behavioral economics helps us better understand consumers in the title lending market, and more importantly, can help frame policy solutions to what is a new, rapidly changing market.

Microeconomics has a workhorse model (which Camerer and Loewenstein allude to) that economists use to understand and predict behavior of consumers and other decision makers. This assumes people act rationally and do not make mistakes when it is at all costly to do so.¹³⁹ Like any theoretical model of human behavior, this rational-actor model is a caricature of real decision making and often grossly simplifies actual behavior.¹⁴⁰ That being said, this and other models provide useful insights into decision making in a number of contexts, and the rational actor model has come to define modern microeconomics.¹⁴¹

In this model's basic form, people maximize a "utility function" at every point in time.¹⁴² A utility function is a way to quantify happiness or well-being, which is called "utility" in economics. The basic idea is that people (e.g., consumers making financial decisions) pick the option that will make them the best off from the available options. Of course these decisions are often made in the face of uncertainty: I will take the surface roads because I expect there to be heavy traffic. This maximizes one's utility *ex ante*. It may have been the case that taking the highway would have been better, but given the information on hand at that time (Google Maps said there was a red line on the highway), the driver made the rational choice.

Decision makers in this rational decision-making framework can be characterized as possessing the following qualities:¹⁴³ (1) they have access to all of the existing, relevant information to inform their choices, (2) they use that information appropriately and in accordance to the laws of probability, (3) they respond to prices, and (4) they have "fixed, well-defined preferences."¹⁴⁴ These "preferences" are what make up a utility function and are assumed to be purely selfish and self-serving (no caring

139. GARY S. BECKER, *THE ECONOMIC APPROACH TO HUMAN BEHAVIOR* 153 (1976).

140. For more on how "all models are wrong" and general tips on modeling in economics and behavioral economics, see generally, Matthew Rabin, Professor of Economics, Univ. of Cal. Berkeley, Lecture at American Economics Association Meeting (Jan. 5, 2010) [hereinafter Rabin Lecture].

141. See ANDREU MAS-COLELL ET AL., *MICROECONOMIC THEORY* 17–39 (1995) (discussing consumer choice).

142. See Paul A. Samuelson, *A Note on Measurement of Utility*, 4 *REV. OF ECON. STUDIES* 155, 156 (1937) ("During any specified period of time, the individual behaves so as to maximise the sum of all future utilities, they being reduced to comparable magnitudes by suitable time discounting.").

143. This is only a bare bones delineation of the model's assumptions. For more on what the traditional microeconomic model assumes, see ANDREAU MAS-COLELL ET AL., *supra* note 141, at 40–91.

144. See Dan Ariely et al., "*Coherent Arbitrariness*": *Stable Demand Curves without Stable Preferences*, 118 *Q. J. ECON.* 73, 103 (2003) (discussing coherent preferences in depth). Preferences would not be well-defined if, for example, arbitrary information affected people's willingness to pay for a good, or irrelevant choices affected people's decision processes. *Id.* at 102.

for other people, altruism, reciprocity, etc.).¹⁴⁵ This model has come to proliferate in law and economics and in legal analysis as well.¹⁴⁶

In the context of title lending, a rational borrower considering using a title loan would (1) gather a sufficient amount of information about the loan and its prices, (2) accurately understand the terms of the loan (APR, fees, repossession policies, etc.), (3) gather information about alternative sources of credit, and (4) use the laws of probability to calculate the chances by which he would be able and unable to repay his loan. These probabilities would be based on a number of uncertain factors: income, regular expenses (rent for example), and unexpected expenses (doctor visits, etc.). The rational model even predicts that consumers would have *rational expectations* about these uncertain expenses; borrowers do not need to predict the future perfectly, but they need to (under the rational model) have an accurate understanding of the underlying distribution of changes to spending they could face. That is, they know the likelihood of experiencing a good or bad “shock,” and they plan their behavior, saving and spending according to those likelihoods. Further, under the rational model, consumers would have rational expectations about the probability of having their car repossessed. With that probability in mind, they would weigh the options of taking the loan or not taking the loan.

Despite its prominence, there is overwhelming evidence from both psychology and economics against many of the assumptions that go into the rational actor model.¹⁴⁷ Enter behavioral economics. This field maintains most of the primary elements of the rational actor model of decision making, but alters it to incorporate psychological evidence concerning how humans actually behave in real life. For example, we know that the way decisions are presented or “framed” to consumers can dramatically affect choices.¹⁴⁸ Furthermore, people seem to evaluate potential losses in utility in a way that is inconsistent with the traditional rational model.¹⁴⁹ People are, of course, not purely self-interested,¹⁵⁰ people procrastinate,¹⁵¹ people’s preferences are often unstable and incoherent,¹⁵²

145. Colin Camerer & Richard H. Thaler, *Anomalies: Ultimatums, Dictators and Manners*, 9 J. OF ECON. PERSP. 209, 218 (1995).

146. Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1471–79 (1998).

147. On deviations from time consistency, see George Loewenstein & Drazen Prelec, *Anomalies in Intertemporal Choice: Evidence and an Interpretation*, 107 Q.J. ECON. 573, 574–78 (1992). On non-selfish behavior, see Gary Charness & Matthew Rabin, *Understanding Social Preferences with Simple Tests*, 117 Q. J. ECON. 817 (2002). On framing effects, see examples in Camerer & Loewenstein, *supra* note 138, at 3, 3–51. On misprediction of preferences, see Norbert Schwartz & Fritz Strack, *Reports of Subjective Well-Being: Judgmental Processes and Their Methodological Implications*, in WELL-BEING: THE FOUNDATIONS OF HEDONIC PSYCHOLOGY 62, 63 (Daniel Kahneman et al. eds., 1999).

148. Mark Kelman et al., *Context-Dependence in Legal Decision Making*, 25 J. LEGAL STUD. 287, 305 n.25 (1996).

149. Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263, 263 (1979).

150. Matthew Rabin, *Incorporating Fairness into Game Theory and Economics*, 83 AM. ECON. REV. 1281, 1281 (1993).

151. Ted O’Donoghue & Matthew Rabin, *Choice and Procrastination*, 116 Q.J. ECON. 121, 121 (2001).

152. Ariely et al., *supra* note 144, at 74.

and people misunderstand and miscalculate when thinking about probabilities and other complicated math problems required by utility maximization.¹⁵³

Given the mountain of evidence that people are not purely rational, especially when it comes to borrowing and saving behavior, we argue that borrowers in the title lending market are unlikely to follow the rational model of behavior. Below we summarize the relevant literature and then explain which anomalies are most relevant in this market and how they play out. We argue that borrowers are, for the most part, weighing perceived costs and benefits rationally. They may be, however, mispredicting their ability to repay the loan. People seem to think they will be able to repay (i.e., save in between when loan payments are do) more aggressively than they do. This misprediction may be due to misperceiving costs incurred in the intervening periods between loan payments, or it may be due to overoptimism about one's own future behavior.

Sections A, B, and C outline these psychological factors as they relate to title lending. In each case, we demonstrate how title lending customers likely underestimate the true cost of title loans.

A. *Optimism and Overconfidence*

Overoptimism¹⁵⁴ and the closely-related overconfidence¹⁵⁵ are well-documented behavioral anomalies.¹⁵⁶ Nobel prize-winning psychologist Daniel Kahneman notes, "people tend to be overly optimistic about their relative standing on any activity in which they do moderately well."¹⁵⁷ A classic example of this is that the vast majority of drivers (ninety-three percent) think they are better at driving than the median driver.¹⁵⁸ Of course, since "median" means the point at which half of people are above and half are below, it is not mathematically possible that ninety-

153. Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCIENCE 1124, 1124 (1974).

154. See Ulrike Malmendier & Geoffrey Tate, *Who Makes Acquisitions? CEO Overconfidence and the Market's Reaction*, 89 J. FIN. ECON. 20, 21–22 (2008) (discussing the impact of overoptimism on mergers and acquisitions); Neil D. Weinstein, *Unrealistic Optimism About Future Life Events*, 39 J. PERSONALITY & SOC. PSYCHOL. 806, 806 (1980) (discussing people's unrealistic optimism about future events).

155. Don A. Moore & Samuel A. Swift, *The Three Faces of Overconfidence in Organizations*, in SOCIAL PSYCHOLOGY AND ORGANIZATIONS 147, 147–49 (David De Cremer et al. eds., 2011).

156. It may even be "rational" in that depressed people are the most precise about their abilities and people may be overoptimistic for evolutionary reasons. See Lauren B. Alloy & Lyn. Y. Abramson, *Judgment of Contingency in Depressed and Nondepressed Students: Sadder but Wiser?*, 108 J. EXPERIMENTAL PSYCHOL. 441, 461, 468 (1979) ("Depressed people accurately detect noncontingency between their responses and outcomes whereas non-depressed people . . . showed more pronounced illusions of control in situations in which they were attempting to obtain desired outcomes . . ."). People may also be overoptimistic for evolutionary reasons. See TALÍ SHAROT, *THE OPTIMISM BIAS: A TOUR OF THE IRRATIONALLY POSITIVE BRAIN* 14 (2012) ("[O]ur brains can often provide us with a distorted sense of reality.").

157. DANIEL KAHNEMAN, *THINKING, FAST AND SLOW* 260 (2011).

158. Ola Svenson, *Are We All Less Risky and More Skillful Than Our Fellow Drivers?*, 47 ACTA PSYCHOLOGICA 143, 146 (1981).

three percent of people are better drivers than the median driver. Even accounting for differences in the varying definitions of a “good driving,” most respondents are overconfident. Overconfidence takes many forms and people do not seem to easily learn about or adjust their overconfidence.¹⁵⁹

In the context of title lending, we might guess that borrowers are overly optimistic that they will pay their loan on time. Anecdotal evidence suggests that consumers similar to those in this market are often late paying off the loan and take longer to repay than they think they will.¹⁶⁰

Our results show that customers taking out a loan on the day of the survey do in fact show signs of overoptimism, however it is not severe. Table 9 shows the answers to the question “How many months total do you think it will take to *completely* pay off this loan (after all renewals/rollovers?)” for customers who were taking out a loan on the day of the survey. The table also includes the information from a required Texas disclosure that shows how long borrowers usually take to pay off their title loan.¹⁶¹ The percentage of people in our sample who thought they would pay the loan off in two to three months is higher than the general usage data would imply, and the percentage of people in our sample who thought it would take six or more months to pay off the loan is too low compared to the general usage data. This leads us to believe that people may be overly optimistic about their ability to repay. This could be because of so-called “consumption shocks” that occur over the borrowing period: a child gets sick, the utility bill is larger than expected, etc., or it could be because people have less money in their bank account at the end of the 30 days than they thought they would—not because of unexpected bills but because of unpredicted impatience with savings and spending, a possibility we discuss next. But overall, the results are not severe. People are relatively good at predicting their ability to repay, although there is room for improvement.

159. Matthew Rabin, *Psychology and Economics*, 36 J. ECON. LITERATURE 11, 31 (1998).

160. Lynn Drysdale & Kathleen E. Keest, *The Two-Tiered Consumer Financial Services Marketplace: The Fringe Banking System and Its Challenge to Current Thinking About the Role of Usury Laws in Today's Society*, 51 S.C. L. REV. 589, 599 (2000).

161. OFFICE OF THE CONSUMER CREDIT COMM’R, FILLABLE AUTO TITLE MULTIPLE PAYMENT DISCLOSURE (2012), available at <http://www.occc.state.tx.us/pages/industry/CAB/Fillable%20Auto%20Title%20Multiple%20Pay%20Disclosure%20%28Dec%2012%29.pdf>. The disclosure form requires a company to provide information on the cost of the loan. It also includes information on how long borrowers typically take to pay off a title loan. The data for the disclosure are taken from a 2010 Tennessee report on title pledge lending. We refer to the information on months it actually takes people to pay off the loan as general usage data.

TABLE 9: PREDICTION OF MONTHS TO COMPLETELY PAY OFF THE LOAN

	Borrowers' Predictions in Our Sample	Texas Disclosure of Actual Usage
	Percentage	Percentage
1 month	20.13%	27.00%
2-3 months	37.58%	24.00%
4-5 months	14.09%	13.00%
6+ months	28.19%	36.00%
Total	100%	100%

We would also expect that customers familiar with the title loan product and their own behavior might learn about themselves and become less overoptimistic over time. The rational model predicts that title loan customers will learn from their own use of a product with a latent risk.¹⁶² A latent risk is one that is unknown before using the product, but becomes known through the use of the product or service.¹⁶³ The more frequently a title lending customer uses title loans and experiences the unforeseen risk of multiple rollovers, the more likely the customer is to begin to foresee that risk and correct overoptimism about repayment.¹⁶⁴

Our results show that this type of learning may occur in the title loan market. Using the same question, “How many months total do you think it will take to *completely* pay off this loan (after all renewals/rollovers?),” we compare in Table 10 the answers for people taking out a loan for the first time with the answers for people who had used a title loan before.¹⁶⁵ Fewer people who have used a title loan before think that they will pay off the loan in one month than people taking out a loan for the first time do. Similarly, more people who have used title loans in the past think it will take them six or more months to pay off the loan than those who have never used one before. Thus, it appears that customers do learn about the latent risk of the product or their own behavioral tendencies through using the service.

162. See Bar-Gill, *supra* note 13, at 755.

163. See *id.* at 755–56.

164. *Id.* (“Starting with intrapersonal learning, the speed with which a consumer will learn about a latent risk associated with a product will depend on how frequently she uses the product and how frequently the risk materializes.”). See also Sumit Agarwal et al., *The Age of Reason: Financial Decisions Over the Life Cycle with Implications for Regulation 7* (Brookings Papers on Econ. Activity, Working Paper 2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=973790.

165. This table still only includes customers who were taking out the loan on the day of the survey.

TABLE 10: OPTIMISM AND LEARNING

	First loan	Not first loan
	Percentage	Percentage
1 month	27.78%	15.79%
2-3 months	38.89%	36.84%
4-5 months	14.81%	13.68%
6+ months	18.52%	33.68%
n	54	95

Even if people learn about their own behavior and how loans work through repeated interactions with a title lender, their behavior may not change over time. People may be persistently “naïve” about their future behavior. We turn to this possibility next.

B. Choice Over Time

First, we must describe the canonical model that economists use to study tradeoffs over time. Note that nearly every choice has an “inter-temporal element,” that is some costs and benefits that come at different points in time. For example, choosing to update your iPad software gives you future benefits of more user-friendly environment, but at the cost of spending some time to learn those updates before the benefits are reaped.

Recall that we consider consumers to have a utility function that represents happiness or well-being. People make choices so as to maximize that happiness, working with the set of available choices.¹⁶⁶ People pick and choose, or “trade off,” goods subject to having to stay within their “budget constraint” (loosely, their income and savings). For example, I can afford 1 banana and 2 apples or 0 bananas and 3 apples. I quite like apples, so I will go with the latter.

Just like that simple tradeoff, people trade off “utilities” and “disutilities” (which can be roughly described as bursts or doses of happiness or unhappiness) over time. People might take a hit to utility (increasing disutility) today for a future benefit: completing a homework assignment today creates disutility now but enables the future utility of being able to attend the Barristers’ Ball on Friday night. The costs and benefits involved in a tradeoff can also be reversed. Staying out late with friends on a Wednesday night could come with the extra disutility of having to cram all of one’s studying into an all-nighter before an exam rather than studying for shorter periods of time spread over the week. These same tradeoffs affect choices in lending markets: Borrowing \$500 today means big benefits today (increased cash flow) but costs in the future (monthly interest payments).

166. See *supra* note 142.

The rational actor model has precise predictions about how these tradeoffs over time are weighed. The model says that people weigh how much (or little) they care about the future, and predict their future choices in accordance with those weights. If one is a very “patient” person, she might plan to do all her homework on Monday, well before it is due. If someone was relatively “impatient,” she might choose to delay a costly task like homework for some future date. Important to this rational actor model is that people (whether they be patient or impatient) accurately predict their future behavior (outside of some major changes like a blizzard occurring and plans were changed).

Many parts of this model are intuitive: people do seem to tradeoff costs and benefits over time, and people are more patient when considering the distant future. The model even allows for there to be differences across people in their level of patience. This model, however, called “exponential discounting” is very rigid and can be unrealistic.

Beyond the rigidity of assuming people have precisely the same level of patience all the time (note this rules out behavior such as “most of the time I do my homework but once in a while I throw caution to the wind and stay out all night”), it is unrealistic in that people often mispredict their level of patience “I might be impatient today but tomorrow I will go on a diet.” Note that mispredictions about levels of patience are considered to be self-control problems by behavioral economists, and the mispredictions almost universally go in one way: people think they will have more self-control than they actually do: “I want to start saving for retirement, but I will work that out next week.” “This is my last cigarette.” “I want to lose weight, so I really really will start exercising hard, tomorrow.” And so on.

Essentially, all of us procrastinate and have self-control problems from time to time. But this common sense, all-too-common behavior is completely at odds with the rational actor model. In fact, the weight of experimental evidence, and evidence from the real world, and mere common sense suggest people are “present-biased.” They are impatient in the short-run, patient when making choices over the longer run, and further, they mispredict these preferences. Behavioral economists recognize this reality and have begun to document the importance of such behavior in consumer markets.

Models of “present-biasedness” have been used to understand behavior in many areas, including credit markets. Evidence of present-biasedness has been shown in the context of smoking,¹⁶⁷ weight loss, saving,¹⁶⁸ credit cards, payday loans, and pawnshops. Consequently, thinking about present-biasedness in the world of title lending is obvious.

167. Jonathan Gruber & Botond Koszegi, *Is Addiction “Rational”? Theory and Evidence*, 116 Q.J. ECON. 1261, 1293–94 (2001).

168. James J. Choi et al., *Plan Design and 401(k) Savings Outcomes* (Nat'l Bureau of Econ. Research Working Paper No. 10486, 2004), available at <http://www.nber.org/papers/w10486.pdf>.

Borrowing today means receiving benefits (getting the principal amount of the loan) now, with costs (having to pay back principal plus interest payments—potentially very large interest payments) to be incurred in the future.¹⁶⁹ We note that borrowing at high interest need not necessarily be “irrational.” People could be reasonably calculating the tradeoffs and making choices accordingly. Those tradeoffs would almost surely be considered “impatient” if we were to calibrate the tradeoffs empirically. But again, impatience is not irrational. The misprediction of one’s level of patience is. If I need emergency medical treatment now, the utility I get from obtaining money now by borrowing could be so large that it is rational for me to borrow at 300% APR to cover the medical expenses.

We posit that just like almost any other market that has been studied involving consumer choice, borrowers in the title lending market think they will be patient, saving for the future, and that they will easily pay off the lender in a timely manner. But under a model of misprediction of future patience, a borrower, for example, will in the end fail to be as patient as he expected, and will have a harder time repaying than expected at the time he took out the loan.

To learn about the levels of patience (or impatience as it were) of our consumers, we asked them two questions related to their tradeoffs over time (also called “time preferences”).¹⁷⁰ The first question asked them to hypothetically choose between receiving \$60 today or receiving \$75 in one month as a lottery prize. The second asked them to make a similar comparison looking six months into the future: choose between receiving \$100 in six months or \$125 in seven months. By combining these two answers, we can determine the basic time preference category of the borrower. For example, a person who chose to delay payment for more money in both scenarios would be considered patient, but a person who chose less money sooner in both scenarios would be deemed impatient. A person who makes the inconsistent choice of impatience in the first scenario but patience in the second scenario is present-biased because “the implied discount rate in the near-term frame is higher than that of the distant frame.”¹⁷¹ Table 11 presents the results of the time preferences of borrowers.

169. To take a simple example, many students borrow to finance their college education in order to obtain the benefits of a degree early in life, before they have had a chance to save up enough money for tuition. They plan to deal with the costs later in life, when they are better situated to pay off the debt. Borrowing money allows them to “smooth” their consumption over their life course. See Allison Mann et al., *Debt, Bankruptcy, and the Life Course* 11–12 (Working Paper, 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1492845&download=yes (explaining but also critiquing this view).

170. These are questions 9 and 10 in our survey instrument. See Appendix A.

171. Nava Ashraf et al., *Tying Odysseus to the Mast: Evidence from a Commitment Savings Product in the Philippines*, 121 Q.J. ECON. 635, 647 (2006).

TABLE 11: TIME PREFERENCES

	Percentage	Count
Impatient	30.24%	137
Present bias	19.21%	87
Future bias	13.47%	61
Patient	37.09%	168
Total	100.00%	453

We find that 19% of our borrowers were present-biased. Recall that this means they think they will be more patient tomorrow than they are today and will mispredict their willingness to save over the course of the month to pay off the loan. 30% of borrowers were impatient, meaning that they highly discount the future but are consistent in their choices. 37% were actually patient, meaning they were not irrational in their predictions about future discounting, and they were not impatient.¹⁷²

We think there is more to the story; while a hyperbolic model is a nice way to more realistically capture certain aspects of decision making, it can also be quite rigid in itself. It assumes, for example, that people have the same level of self-control problems in every time period, ruling out the possibility that someone might be mostly patient but once in a while throw caution to the wind and, for example, stay out all night partying.¹⁷³ It also assumes that people understand the inherent risks in a product or service, but that they misunderstand their own preferences. Next, we discuss more basic mistakes in decision making, and specifically, rely on limited attention, a very basic, common sense approach to decision theory, but one that has been relatively new on the scene to empirical behavioral economists.

C. Limited Attention

Several recent papers have used the fact that people have limited attention to explain behavior.¹⁷⁴ Many types of decisions are complicated and involve processing large amounts of information.¹⁷⁵ When required to process a lot of information, people use mental shortcuts or “heuristic-

172. See *id.* at 646 (discussing survey instruments). Other authors have asked borrowers the exact same questions. For example, Ashraf et al. find that “[a]pproximately 27.5 percent of individuals were hyperbolic [present-biased], that is more patient over future tradeoffs than current trade-offs, whereas 19.8 percent were less patient over future trade-offs than current trade-offs.” *Id.* at 647. Our results are similar to theirs.

173. See generally David Huffman & Matias Barenstein, *A Monthly Struggle for Self-Control? Hyperbolic Discounting, Mental Accounting, and the Fall in Consumption Between Paydays* (IZA Discussion Paper No. 1430, 2005), available at http://ftp.iza.org/dp1430_rev.pdf.

174. See, e.g., Josef Falkinger, *Limited Attention as a Scarce Resource in Information-Rich Economies*, 118 *ECON. J.* 1596 (2008).

175. See e.g., Oren Bar-Gill, *Seduction by Plastic*, 98 *NW. U. L. REV.* 1373, 1373 (2004) (describing the complexity of credit card contracts and the ways in which these contracts confuse consumers).

tics”¹⁷⁶ to ease the decision-making process. Using heuristics in a context like subprime lending may narrow one’s attention to the attractive-seeming aspects of the loan that the lender wants to highlight, at the cost of concealing important facts that may turn out to be detrimental.

Behavioral economists have theoretical models for how people use their attention. For example, in Gabaix and Laibson’s work,¹⁷⁷ they show that many goods are marketed intentionally with “salient” and “shrouded” attributes, for example, a printer that is inexpensive but uses extremely costly ink.¹⁷⁸ Consumers do not, or do not fully, consider the cost of replacing the ink when purchasing the printer. Another nice example of work that studies limited attention in a large consumer market (note that much of the research is from lab experiments) is Lacertal, Pope, and Sydnor.¹⁷⁹ They use 22 million used car sale transactions to document the existence of a “left-digit bias”; that is, when shopping for cars, both consumers and dealers assign disproportionate weight to the left-most digits in the mileage figure (making 49,900 and 50,000 miles appear to be vastly different mileage figures, for example).¹⁸⁰ This is borne out in the patterns of used car auction purchase prices.

In the world of title lending, we think that a few aspects of the transaction are particularly salient, and some are more shrouded. For instance, title lending advertising emphasizes the speed at which the customer can obtain the cash,¹⁸¹ the maximum loan amount the lender will give,¹⁸² the ability of the customer to keep their cars,¹⁸³ and the conven-

176. Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, in *JUDGMENT UNDER UNCERTAINTY: HEURISTICS AND BIASES* 3, 3 (Daniel Kahneman et al. eds., 1982).

177. See Stefano DellaVigna, *Psychology and Economics: Evidence from the Field*, 47 J. ECON. LITERATURE 315, 348–62 (2009); Dean Karlan et al., *Getting to the Top of the Mind: How Reminders Increase Savings*, (Nat’l Bureau of Econ. Research, Working Paper No. 16205, 2010).

178. Xavier Gabaix & David Laibson, *Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets*, Q.J. ECON. 505, 506–11 (2006).

179. Nicola Lacetera et al., *Heuristic Thinking and Limited Attention in the Car Market*, 102 AM. ECON. R. 2206 (2012).

180. *Id.*

181. To obtain a rough sense of the advertising on title lending websites, we viewed the websites of four prominent title lending companies. See *Benefits of a Title Loan with LoanMax*, LOANMAX TITLE LOANS, <https://www.loanmaxtitleloans.net/BenefitsOfTitleLoan> (last visited Mar. 29, 2014) (advertising “[i]nstant, on-site approvals” and “[s]ame-day loans in 20 minutes or less”) [hereinafter LOANMAX TITLE LOANS Benefits]; *Title Loans*, ACE CASH EXPRESS, <https://www.acecashexpress.com/title-loans/> (last visited Mar. 29, 2014) (promising the ability to “[a]pply online or in-store in just minutes” and “instant approval”); *Title Loans Up to \$25,000 at the Cash Store*, CASH STORE, <http://www.cashstore.com/title-loans> (last visited Mar. 29, 2014) (“Title loans are a great lending option that allow you to get up to \$25,000 fast. Through car title loans you can quickly get the money you need”) (footnote omitted) [hereinafter CASHSTORE]; TITLEMAX, <http://www.titlemax.biz> (last visited Mar. 29, 2014) (“[I]nstant approval on car title loans, which means you get your cash fast!”).

182. CASH STORE, *supra* note 181 (allowing \$25,000); *Frequently Asked Questions – Title Loans*, ACE CASH EXPRESS, <https://www.acecashexpress.com/title-loans/faq> (last visited Mar. 29, 2014) (allowing \$2,500) [hereinafter ACE CASH EXPRESS]; LOANMAX TITLE LOANS, <https://www.loanmaxtitleloans.net> (last visited Mar. 29, 2014) (allowing \$10,000); TITLEMAX, *supra* note 181 (allowing \$10,000).

183. ACE CASH EXPRESS, *supra* note 182 (“You get the money and you get to keep driving your car.”); CASH STORE, *supra* note 181 (“Best of all, you get to keep and drive your car while you pay back the loan!”); LOANMAX TITLE LOANS, *supra* note 182 (“You keep your car!”); TITLEMAX, *supra*

ience of doing business with the company.¹⁸⁴ Title lending advertisements do not generally mention the interest rate of the loans, the likelihood a loan will result in a vehicle being repossessed, or the likely amount of time it will take for the borrower to repay the debt.¹⁸⁵

State and federal disclosure laws require that the loan contracts disclose the finance charge and interest rate, but they do not, for the most part, require that lenders disclose any pattern of usage information to inform borrowers about the likely consequences of having taken out a loan.¹⁸⁶ More importantly, laws do not generally require price disclosures be made upfront—that is before the borrower has invested substantial effort into obtaining the loan. For instance, Texas' law requires that lenders provide disclosures at the time the loan is made,¹⁸⁷ but the statute does not require the disclosures any earlier in the process than when the borrower is signing the final paperwork. Even though loan documents may have pertinent pricing information and may be short,¹⁸⁸ the disclosure of price is shrouded by the timing in which the borrower receives it.¹⁸⁹

In sum, a mountain of common sense as well as empirical work documents attention as a scarce resource. Lenders are acutely aware of this phenomenon and without regulatory prodding, will emphasize favorable transaction terms and shroud unfavorable ones.¹⁹⁰ By shrouding price terms and the likely ways the borrower will use the loan, lenders are able to encourage borrowers to underestimate the cost of the title loan.

Each of these behavioral deviations from the rational choice model suggests that borrowers in title lending markets are underestimating the true costs of the loans. Some borrowers are overly optimistic about the speed at which they will repay the debt, some experience self-control problems that cause them to mispredict their future patience, and others exhibit limited attention and focus on non-price terms of the transaction. While none of these suboptimal decisions portray title loans as scandalous, they do indicate a need for laws to correct irrational behavior in this market.

note 181 (“The best part about getting a car title loan with TitleMax is that you get to keep driving your car.”).

184. *Locations*, LOANMAX TITLE LOANS, <https://www.loanmaxtitleloans.net/Locations> (last visited Mar. 29, 2014) (“[C]onvenient locations!”); TITLEMAX, *supra* note 181 (touting “over 175 locations offering title pawns across the state of Georgia”).

185. All of the websites in note 180 fail to mention these facts.

186. *See supra* Part III.

187. TEX. FIN. CODE ANN. § 393.222 (West 2014).

188. *See Hawkins, The Federal Government in the Fringe Economy*, *supra* note 45, at 64–65 (describing Speedy Cash's title loan contract as being around five pages long).

189. *See Mann & Hawkins, supra* note 14, at 904 (making a similar observation in the context of payday lending).

190. *Id.* at 904–05.

VI. CONCLUSION AND POLICY RECOMMENDATIONS

We have presented survey evidence that reveals demographic information about title lending customers and demonstrates how title lending customers deviate from the theoretical portrait of the rational actor in systematic, predictable ways. But the question remains: what should regulators do about this lending product? Our conclusion is to suggest one type of regulation, product-use disclosures, and to discourage another, prohibition.

We argue that the primary response to the problem of underestimating the true cost of title loans is behaviorally-informed disclosures.¹⁹¹ Policymakers should require that title lending companies post information about how people actually use title loans: information about the number of times people rollover their loan, the amount of money these rollovers cost in total, the number and amount of late fees and other fees people pay, and the likelihood of defaulting on the loan. Oren Bar-Gill's recent book, *Seduction by Contract*, distinguishes between product-attribute disclosures and product-use disclosures.¹⁹² Product-attribute disclosures provide information about the product itself, such as a loan's interest rate or the fee for paying late.¹⁹³ Product-use disclosures, on the other hand, inform customers about their own probable future use patterns, such as common "[b]orrowing patterns and the incidence of late payment."¹⁹⁴ This latter type of disclosure is so important because if title lending borrowers are likely to make the types of mistakes we identify in Part V, information about the title loan product's attributes will be insufficient to ensure the market functions. For instance, if borrowers only know the loan's APR but are overly optimistic about how long it will take them to pay off the loan, they will underestimate the cost of the loan. Similarly, if they are present-biased and mispredict their abilities to be patient and save to pay off the loan, they will make mistakes about how long it will take to repay the debt (and ultimately the loan's cost). Borrowers need to know the likely way they will use the product to weight its utility.

Lenders can base product-use disclosures on either average-use patterns that focus on how a large group uses a product or individual-use patterns that focus on how a specific individual has used a product in the past.¹⁹⁵ While individual-use disclosures are more effective in communicating relevant, believable information to borrowers, they are infeasible in title lending markets because many borrowers do not have long-term

191. For the origin of this term and its application in the mortgage context, see Michael S. Barr et al., *Behaviorally Informed Home Mortgage Credit Regulation*, in *BORROWING TO LIVE: CONSUMER AND MORTGAGE CREDIT REVISITED* 170 (Nicolas P. Retsinas & Eric S. Belsky eds., 2008).

192. OREN BAR-GILL, *SEDUCTION BY CONTRACT: LAW, ECONOMICS, AND PSYCHOLOGY IN CONSUMER MARKETS* 33–34 (2012).

193. *Id.* at 33.

194. *Id.*

195. *Id.* at 35.

relationships with single title lenders.¹⁹⁶ Thus, the best option for title lending disclosures is to see how borrowers generally use the product.

Some work disputes the efficacy of disclosure-based regulations, arguing that disclosure has failed as a regulatory strategy to improve markets.¹⁹⁷ Omri Ben-Shahar and Carl Schneider, for instance, point to “empirical evidence [to] show that mandated disclosure regularly fails in practice”¹⁹⁸ While we have to leave the general concerns about disclosures to others, there is empirical evidence in fringe consumer credit markets that product-use disclosures do affect consumer decision making. Marianne Bertrand and Adair Morse offered payday lending customers four different types of information treatments as the customers took out payday loans and then measured the effect of the information on consumer behaviors, operating on the assumption that “if all or a subset of payday borrowers are cognitively impaired, one might expect borrowing behavior to respond to how the costs (and benefits) of the payday products are being disclosed.”¹⁹⁹ One information treatment presented a graphic depicting how long it takes the average person to pay off a payday loan.²⁰⁰ Bertrand and Morse explain that “this treatment gets borrowers to take a broader look at the payday borrowing decision, and may therefore also partly undo borrowers’ tendency to apply too narrow a decision frame.”²⁰¹

To assess the effect of the information treatments, they tracked the behavior of customers subjected to the different treatments and compared each group to a control group and to each other. Based on this comparison, they conclude that

information that makes people think less narrowly (over time) about finance costs results in less borrowing. In particular, reinforcing the adding-up dollar fees incurred when rolling over loans reduces the take-up of future payday loans by 11% in the subsequent 4 months.²⁰²

Following Bertrand and Morse’s graphic depiction of patterns of use, Texas now requires a disclosure statement to be given to any customer taking out a title loan that includes information on fees and actual

196. *Id.* at 35, 107.

197. Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 651 (2011) (“Although mandated disclosure addresses a real problem and rests on a plausible assumption, it chronically fails to accomplish its purpose. Even where it seems to succeed, its costs in money, effort, and time generally swamp its benefits. And mandated disclosure has unintended and undesirable consequences, like driving out better regulation and hurting the people it purports to help.”); Lauren E. Willis, *Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending*, 65 MD. L. REV. 707, 789-90 (2006) (“First, the quantity of disclosures can create an information overload. Second, they are given at a time when the borrower is no longer in a decisionmaking frame, but is already psychologically committed to the loan and likely to ignore red flags under the influence of motivated reasoning. Finally, the disclosures reinforce a false sense of security about the home borrowing process, in part through the representativeness heuristic.”).

198. Ben-Shahar & Schneider, *supra* note 197, at 651.

199. Bertrand & Morse, *supra* note 21, at 1866.

200. *Id.* at 1872-73.

201. *Id.* at 1873.

202. *Id.* at 1865.

usage patterns of the loan.²⁰³ The disclosure includes information on the proportion of people who roll over their loans for two to three months, four to five months, and six or more months, and the proportion of people who do not roll over their loans.²⁰⁴ To look at whether this disclosure is effective in changing people's beliefs about how they will use the loan, we must compare the expected number of months to repayment for Texas borrowers and for borrowers in our other states. Unfortunately, once we restrict our sample to borrowers taking out the loan on the day of the survey, we are left with only thirty borrowers from Texas. Our results, therefore, cannot provide much reliable information on the effectiveness of the disclosure, and we leave this question for further research. Nevertheless, Bertrand and Morse's work reveals the efficacy of product-use disclosures in this particular market.

While Texas' disclosure provides some of the information needed to remove bias from faulty decision-making, the disclosure would be much more effective if it were posted prominently in the store so that customers could see the information before incurring the transaction costs involved in applying for the loan.²⁰⁵ Requiring title lending companies to present pattern of use information in their advertising on the Internet and in stores would maximize the effect the information could have on borrowers and limit companies' abilities to capitalize on borrowers' limited attention.

Although we believe policymakers should intervene in the title lending market in new ways, by requiring creative and prominent product-use disclosures, the evidence we obtained through our survey does not indicate that states (or the federal government) should prohibit title lending. The primary argument advanced by policymakers for banning title lending has been that a substantial portion of customers are risking their livelihood by taking out a loan secured by their vehicle.²⁰⁶ Proponents of this view have admitted that they were uncertain of the evidence

203. The General Counsel of the Texas Office of Consumer Credit Commissioner recently explained that Texas specifically modeled its payday and title lending disclosure regulation on Bertrand and Morse's work. Sealy Hutchings & Matthew J. Nance, *Credit Access Businesses: The Regulation of Payday and Title Loans in Texas*, 66 CONSUMER FIN. L.Q. REP. 76, 89 (2012).

204. The actual disclosure mandated by the state is available on the Internet, although the form does not have the loan amounts and fees which the lender fills in. *Auto Title Loan—Single Payment*, OFFICE OF CONSUMER CREDIT COMM'R, [http://www.occc.state.tx.us/pages/industry/CAB/Fillable%20Auto%20Title%20Single%20Pay%20Disclosure%20\(Dec%202012\).pdf](http://www.occc.state.tx.us/pages/industry/CAB/Fillable%20Auto%20Title%20Single%20Pay%20Disclosure%20(Dec%202012).pdf) (last visited Mar. 29, 2014).

205. See *supra* Part III.c.

206. See Hawkins, *Credit on Wheels*, *supra* note 1, at 466 (collecting arguments from policymakers, academics, and consumer advocates). For a few examples, see H.R. CON. RES. 312, 106th Cong. (2000), available at <http://www.gpo.gov/fdsys/pkg/BILLS-106hconres312rfs/pdf/BILLS-106hconres312rfs.pdf> (“[T]itle loans and title pawns threaten the ability of consumers to hold a job since default on the loan or pawn will result in repossession and sale of their car, which is often their only means of transportation to and from work.”); DEPT OF DEFENSE, REPORT ON PREDATORY LENDING PRACTICES DIRECTED AT MEMBERS OF THE ARMED FORCES AND THEIR DEPENDENTS 16 (Aug. 9, 2006), available at http://www.defenselink.mil/pubs/pdfs/Report_to_Congress_final.pdf (suggesting title loans cause borrowers to lose an essential transportation).

for this claim,²⁰⁷ but our survey, along with state regulatory reports, strongly suggest that this concern has been vastly overstated.²⁰⁸ State regulatory reports reveal that only a small minority of borrowers lose their car to repossession, and the responses to our survey indicate that only a small minority of those customers that lose a car would be unable to get to work.

Moreover, some evidence exists that many people are using title loans in the way the rational actor model would predict, suggesting a functioning market that could result in welfare maximization.²⁰⁹ People make decent predictions about the total length of time they will pay interest on their loan, so many borrowers are not overly optimistic,²¹⁰ and our survey indicates that borrowers exhibit intrapersonal learning as they use the product over time, ameliorating some of the irrational decision making.²¹¹

Finally, the demographic information our survey uncovered does not compel radical market intervention. Title lending customers are not, when compared to the general population, disproportionately members of racial minority groups, are not exceedingly young or exceedingly old, and do not lack education. Certainly, some demographic characteristics do make title lending customers more vulnerable to unscrupulous practices, such as the fact that many are unbanked and many are self-employed, which may indicate a lack of access to other sources of credit that require income. Yet, overall, the picture of title lending customers is closer to the mainstream of society than prior research argues. Given these demographic characteristics, the evidence of rational decision making, and the vacuity of the argument that a large portion of people will lose their only way to work, the case for prohibiting title loans is unconvincing.

What is clear is that we are at an opportune moment for legal reform. In many ways, the title lending market is unlike its fellow fringe banking counterparts. Payday loans are essentially uniform across the country with a set fee for an approximately two week loan.²¹² Legislatures have taken definitive and concrete action to address the loan product.²¹³ Payday lending companies have organized into a large trade or-

207. Leah Plunkett et al., *Baby, You Can Take My Car: The Dangers of Auto Title Loans*, NAT'L CONSUMER LAW CTR. (July 15, 2010), http://www.nclc.org/images/pdf/conferences_and_webinars/auto_webinars/recordings/recording_july15.wmv.

208. See *supra* notes 133–34 and accompanying text.

209. Bar-Gill, *Seduction By Plastic*, *supra* note 175, at 1414.

210. See *supra* notes 160–61 and accompanying text. For a detailed study finding that payday lending customers are accurate in their predictions about how long they will keep out their loans, see Ronald Mann, *Assessing the Optimism of Payday Loan Borrowers* (Columbia Law Sch. Ctr. for Law and Econ. Studies, Working Paper No. 443.), 2013 available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2232954. Specifically, Mann finds that “most borrowers finally repay their loans and are free of debt within two weeks of the date they predicted on the date of the loan.” *Id.* at 5.

211. See *supra* Part V.A.

212. See generally, Mann & Hawkins, *supra* note 14, at 882 (discussing the economics of payday lending).

213. *Id.* at 874.

ganization and set out “best practices” for member stores to follow.²¹⁴ None of these things are true for title loans—the loan products vary from thirty-day loans to amortized year-long loans, many states have no title-lending specific laws, and no trade organization represents a significant portion of the market. Policymakers have a unique opportunity in title lending markets to use the behaviorally-informed economic analysis in the Article to ensure a fair, efficient market. Instead of banning title lending, policymakers should foster a market with information that will help customers understand the true cost of title loans.

214. *CFSA Member Best Practices*, CMTY. FIN. SERVS. ASSOC. OF AM., <http://cfsaa.com/cfsa-member-best-practices/liveaccid/54111.aspx> (last visited Nov. 5, 2013).

APPENDIX A

TITLE LENDING CUSTOMER SURVEY

CONTACT: JIM HAWKINS, UNIVERSITY OF HOUSTON LAW CENTER, 713-743-5018

PLEASE CIRCLE THE LETTER OF YOUR ANSWER:

1. HOW OFTEN DO YOU TAKE OUT TITLE LOANS?

- A. This is my first time
- B. Once a year
- C. 2-3 times a year
- D. 4-6 times a year
- E. More than 6 times a year

2. WHY DID YOU TAKE OUT THIS TITLE LOAN? (CIRCLE ALL THAT APPLY.)

- A. Business expenses (anything related to running a business)
- B. Rent or mortgage payment
- C. Medical Expenses
- D. Gifts
- E. Utility Bills
- F. Car repair
- G. Educational Expenses
- H. Other

3. IF YOU LOST THE VEHICLE THAT YOU USED TO GET YOUR LOAN, HOW WOULD YOU GET TO WORK? (CIRCLE ALL THAT APPLY.)

- A. I do not work outside the home.
- B. Use public transportation
- C. Use another vehicle I or my family owns to get to work
- D. Walk to work
- E. Get rides from friends or car pool
- F. Buy a new car
- G. I would not have another way to get to work

4. HOW MANY MONTHS TOTAL DO YOU THINK IT WILL TAKE TO COMPLETELY PAY OFF THIS LOAN (AFTER ALL RENEWALS/ROLLOVERS)?

- A. 7 More than 12
- B. 8
- C. 9
- D. 10
- E. 11
- F. 12

5. *HOW LONG HAVE YOU HAD THIS LOAN OUT?*

- A. I am taking out the loan today.
- B. I have had my loan out for _____ months.

6. *WHY DID YOU PICK THIS COMPANY? (CIRCLE ALL THAT APPLY.)*

- A. Price
- B. Loan amount
- C. Location
- D. Referral from someone
- E. Lender's reputation
- F. I could get the money more quickly here.
- G. Repeat Customer

7. *WHAT OTHER FINANCIAL SERVICES DID YOU USE AT LEAST ONCE IN THE PAST YEAR? (CIRCLE ALL THAT APPLY.)*

- A. Checking account
- B. Payday loan
- C. Check cashing service
- D. Credit card
- E. Prepaid credit card
- F. Pawnshop
- G. Rent-to-own company
- H. Borrow from friends or family
- I. Personal loan from bank or credit union.
- J. None.

8. *WE'D LIKE YOU TO IMAGINE THAT YOU HAD A CHOICE BETWEEN ONE OF TWO JOBS THAT ARE THE SAME, EXCEPT THAT THEY PAY DIFFERENTLY. WHICH JOB WOULD YOU CHOOSE (PLEASE CIRCLE ONE)?*

- A. JOB A has a regular paycheck of \$300 EVERY WEEK.
- B. JOB B requires the same work and hours as Job A, but has a paycheck that varies. EACH WEEK YOU WOULD HAVE A 50/50 CHANCE OF GETTING EITHER \$250 OR \$450 PAY (like a coin flip), but you would never know ahead of time whether that particular week would be high or low.

9. *IMAGINE YOU WON A LOTTERY AND HAD TO CHOOSE BETWEEN TWO PAYMENT OPTIONS, WHICH WOULD YOU CHOOSE?*

- A. OPTION A would give you \$60 PAID OUT TODAY
- B. OPTION B would give you \$75 PAID OUT ONE MONTH FROM TODAY

10. IMAGINE INSTEAD YOU WON A DIFFERENT LOTTERY (YOU NEVER WON THE LOTTERY IN THE LAST QUESTION) AND HAD TO DECIDE BETWEEN ONE OF THESE TWO PAYMENT OPTIONS, WHICH WOULD YOU CHOOSE?

A. OPTION A would give you \$100 PAID OUT 6 MONTHS FROM TODAY

B. OPTION B would give you \$125 PAID OUT 7 MONTHS FROM TODAY

11. THIS COMPANY'S CUSTOMER SERVICE REPRESENTATIVES ARE COURTEOUS AND HELPFUL.

A. Agree.

B. Disagree.

Please explain: _____

12. WOULD YOU USE THIS COMPANY'S SERVICE AGAIN IN THE FUTURE?

A. Yes.

B. No.

Please explain: _____

13. WOULD YOU RECOMMEND THIS COMPANY TO A FRIEND OF RELATIVE?

A. Yes.

B. No.

Please explain: _____

14. WHAT IS YOUR GENDER?

A. Male

B. Female

15. WHAT IS YOUR RACE?

A. Non-Hispanic White

B. Non-Hispanic Black/African American

C. Latino

D. Asian

E. Other

16. HOW OLD ARE YOU?

17. WHAT IS YOUR OCCUPATION?

- A. Self-employed
- B. Construction
- C. Sales
- D. Education
- E. Healthcare
- F. Hotel / Food Service
- G. Other: _____

18. WHAT IS THE HIGHEST LEVEL OF EDUCATION THAT YOU COMPLETED?

- A. I did not complete high school
- B. High school
- C. Some college
- D. Four year college
- E. Post-college graduate education

19. PLEASE SHARE WITH US HOW YOU LEARNED ABOUT THIS COMPANY:

- A. TV Ad
- B. Radio Ad
- C. Friend or Relative
- D. Saw the store sign