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## Introduction

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FRINGE ECONOMY LENDING AND  
OTHER ABERRANT CONTRACTS

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## FRINGE ECONOMY LENDING AND OTHER ABERRANT CONTRACTS: INTRODUCTION

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Aberrant Contracts, rent to own agreements, third party legal lending contracts, payday loans, and title loan—often referred to as “fringe banking” in the fringe economy, are contractual relationships that lack the characteristics of arms length, bargained for exchanges that dominate the focus of general contract law as taught in most U.S. law schools. These atypical agreements are, more often than not, used by individuals who lack the financial ability to otherwise acquire the goods or services obtained. The loans themselves are generally “involves small dollar amount loans made for short periods of time.”<sup>1</sup> Because these loans involve exorbitant fees and interest rates, some view the businesses that provide these loans or services as loan sharks, preying on the working poor by offering modern household necessities—refrigerators, washers and dryers, services, or cash flow that consumers need but are unable to acquire with credit cards, bank overdraft protection, or traditional loans. On the other hand, advocates for these businesses assert that the consumer adds value to their lives with the goods or services provided that cannot be otherwise afforded;<sup>2</sup> the rates charged reflect the risks undertaken in servicing this particular market.

This symposium begins with Professor Terrence Cain’s article entitled: *Third Party Funding of Personal Injury Tort Claims: Keep the Baby and Change the Bathwater*.<sup>3</sup> Here, Professor Cain describes the specific context of litigation loans acquired by tort plaintiffs from third parties in anticipation of a recovery in a pending lawsuit. The dynamics of this setting are typical of most fringe economy agreements: a necessitous or financially constrained borrower, a ready and willing lender, and interest rates that would astound a knowledgeable borrower, here a mere 280%, and that entangle the borrower with debt that is difficult to eliminate. Professor Cain

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1. Michael H. Anderson, *An Economic Perspective on Subprime Lending*, 89 CHI.-KENT L. REV. 53, 57 (2013).

2. Michael H. Anderson, *An Economic Investigation of Rent-to-Own Agreements*, 89 CHI.-KENT L. REV. 141, 146-47 (2013).

3. Terrence Cain, *Third Party Funding of Personal Injury Tort Claims: Keep the Baby and Change the Bathwater*, 89 CHI.-KENT L. REV. 11 (2013).

advocates maintaining the service provided by the industry but insists that the service must be subject to federal regulation. He concludes by proposing a model act for Congress as well as states to consider.

Professor Michael H. Anderson, an economist, weighs in suggesting an historical symmetry between the ten-year period of the 1970's and 80's, with its three recessions between 1973 and 1981, and our current economic crisis in his essay on the subprime lending industry entitled: *An Economic Perspective on Subprime Lending*.<sup>4</sup> He evaluates the common subprime mechanisms—rent-to-own, pay day lending, pawn shops, and title pawn lending. He concludes that rates between 200% and 1000% APR are a reality for borrowers who contract in these markets despite the original short-term goal and low principal amount of the loan. His analysis suggests that payday and pawn loans are the most egregious and calls for regulation of the subprime lending industry.

Professor Amy Schmitz, in *Females on the Fringe: Considering Gender in Payday Lending Policy*,<sup>5</sup> assesses the prevailing data on payday loans and concludes, as does Professor Anderson in his assessment of the rent-to-own industry,<sup>6</sup> that the ills of payday lending disproportionately impact women and their families. Professor Schmitz joins other symposium authors in calling for regulation but goes beyond that call by suggesting creative, realistic options, both community based and Federal, to address the adverse impact of payday lending and to fill the void likely to be created by effective regulation of the payday lending industry.<sup>7</sup> Two thoughtful essays follow Professor Schmitz' offering potential solutions to the debt crisis of fringe economy lending.

Timothy E. Goldsmith and Nathalie Martin share the results of their empirical research on the public perception of and the need for interest rate caps in their essay: *Interest Rate Caps, State Legislation, and Public Opinion: Does the Law Reflect the Public's Desires?*<sup>8</sup> Goldsmith and Martin add the results of their study of New Mexico consumers that 86% of participants thought that the rate caps should be imposed on short-term loans with over 72% selecting 25% or less as the cap to the staggering statistics from several states suggesting that the general public prefers reasonable

4. Anderson, *supra* note 1.

5. Amy Schmitz, *Females on the Fringe: Considering Gender in Payday Lending Policy*, 89 CHI.-KENT L. REV. 65 (2013).

6. Anderson, *supra* note 2.

7. *See generally*, Anderson, *supra* note 1; Cain, *supra* note 3; Schmitz, *supra* note 5.

8. Timothy Goldsmith & Nathalie Martin, *Interest Rate Caps, State Legislation, and Public Opinion: Does the Law Reflect the Public's Desires?*, 89 CHI.-KENT L. REV. 115 (2013).

caps on short-term loans like payday loans.<sup>9</sup> This accumulated data suggests that an accurate understanding of public perception should motivate the various legislative bodies across the nation in states that do not currently cap store-front or short-term loans to change existing law.

Professor Anderson's second essay, *An Economic Investigation of Rent-to-Own Agreements*,<sup>10</sup> offers the rent-to-own paradigm and its demographics as a better approach to short term lending. The symposium concludes the assessment of fringe economy lending as aberrant contracting with a lender perspective article that addresses the wisdom of securitizing the receivables from fringe lending. Professor Thomas E. Plank in his article, *Securitization of Aberrant Contract Receivables*,<sup>11</sup> identifies the goals and requirements for securitizing receivables and the issues that must be addressed when considering the securitization of fringe banking receivables. Professor Plank concludes by discussing the risks inherent in fringe banking receivables and the concerns that must be weighed to determine if the benefits of securitization can be realized.

The next set of articles by Professors Woodward and Bowers address other concerns with aberrant agreements, whether the term "aberrant" refers to fringe economy lending or mass marketed adhesion contracts: choice of law and payment application. Professor Emeritus William Woodward addresses the legal uncertainty inherent in the union of choice of law provisions and arbitration of consumer claims in his essay, *Legal Uncertainty and Aberrant Contracts: The Choice of Law Clause*.<sup>12</sup> He offers legislation—non-waivable consumer protection statutes—as the sole remedy "to resolve the extraordinarily complex legal problem that confronts a consumer when the vendor replaces local consumer protection with that of another place through a contractual choice of law provision."<sup>13</sup> Professor Woodward uses California's non-waivable two-way fee-shifting statute as an example to illustrate his position.

Professor Bowers in his article, *Some Economic Insights Into Application of Payments Doctrine: Walker-Thomas Revisited*,<sup>14</sup> posits that the striking of the cross-collateral provision in the infamous *Walker-Thomas*

9. *Id.* at 120-29.

10. Anderson, *supra* note 2.

11. Thomas E. Plank, *Securitization of Aberrant Contract Receivables*, 89 CHI.-KENT L. REV. 171 (2013).

12. William Woodward, *Legal Uncertainty and Aberrant Contracts: The Choice of Law Clause*, 89 CHI.-KENT L. REV. 197 (2013).

13. *Id.* at 200-01.

14. James Bowers, *Some Economic Insights Into Application of Payments Doctrine: Walker-Thomas Revisited*, 89 CHI.-KENT L. REV. 229 (2013).

contract because it was unconscionable “relegates the plaintiff to the default provisions of the common law, which may be even more unfavorable to the consumer than the stricken clause.”<sup>15</sup> Revised UCC Article 9 creates an opportunity to address anew default application rules. Professor Bowers argues persuasively that consumers have several reasons for preferring, in a series of transactions with a given creditor—a fact pattern that often occurs in the rent-to-own context, to have their property interests protected in the last-purchased-collateral rather than the first.

Finally, the symposium concludes with other examples of contracts deemed by leading contract and commercial law scholars as “aberrant.” Professor Nancy Kim convincingly demonstrates that electronic contracts and electronic modifications of contracts are inherently aberrant in her article *Situational Duress and the Aberrance of Electronic Contracts*<sup>16</sup> and proposes an extension of the doctrine of duress as a defense in the electronic contracting context. Professor J. Lyn Entrikin tackles the monumental task of advocating for change in the multifarious world of property taxes in her extensive study entitled: *Tax Ferrets, Tax Consultants, Bounty Hunters, and Hired Guns: The Property Tax Netherworld Fueled by Contingency Fees and Champertous Agreements*.<sup>17</sup> Professor James J. White defines an aberrant contract as an asymmetric one that begins with terms proposed to consumers by powerful corporation on a “take it or leave it” basis. He considers an aberration of this model, the tenure contract, “executed between a strong employer and a weak employee. But here the rule is reversed; the employee, presumptively the weaker party, gets his terms.”<sup>18</sup> In his essay, *Tenure, The Aberrant Consumer Contract*, Professor White considers three issues: the origin of tenure, the terms of tenure, and its continued viability. He concludes by advocating abolition of tenure because tenure “injures our students, blocks the way to eager and highly competent professors, and generally degrades the efficiency of our schools.”<sup>19</sup> The final submission in this symposium is Professor Scott Burnham’s assessment of exculpatory contracts as aberrant contracts. In his essay, *Are You Free To Contract*

15. *Id.* at 231.

16. Nancy Kim, *Situational Duress and the Aberrance of Electronic Contracts*, 89 CHI.-KENT L. REV. 265 (2013).

17. J. Lyn Entrikin, *Tax Ferrets, Tax Consultants, Bounty Hunters, and Hired Guns: The Property Tax Netherworld Fueled by Contingency Fees and Champertous Agreements*, 89 CHI.-KENT L. REV. 289 (2013).

18. James J. White, *Tenure, The Aberrant Consumer Contract*, 89 CHI.-KENT L. REV. 353, 353 (2013).

19. *Id.* at 378.

*Away Your Right To Bring A Negligence Claim?*,<sup>20</sup> he evaluates the three prevailing approaches to the enforceability of exculpatory clauses and proposes an analytical framework for courts to use when evaluating the enforceability of these clauses.

These thoughtful articles and essays are only part of the conversation in identifying solutions to the aberrancy of fringe economy lending and other agreements that deviate substantially from the arm's length, bargained-for exchange paradigm that is taught and upon which prevailing doctrines used to police contracts are based. As the dialogue continues either in response to the ideas and theories presented herein or as additions to them, the engagement should serve as an impetus for change.

20. Scott Burnham, *Are You Free To Contract Away Your Right To Bring A Negligence Claim?*, 89 CHL.-KENT L. REV. 379 (2013).



