

10% IS ENOUGH

Background on a National Anti-Usury Campaign

I. Introduction

The time has come to resurrect laws against usury. The argument for limiting the practice of over-charging borrowers is fourfold:

- 1. Moral and civic prohibitions against usury** stretch back deep into our religious and national history. Our prophets and founding fathers made the clear case long before us that usury is patently wrong.
- 2. Our people are hurting** because of crushing debt loads exacerbated by exorbitant interest rates – in the form of high credit card premiums, payday loans, banking and check-cashing fees, sub-prime mortgages, rapid-refund tax return schemes, car-title scams, and other practices that reap benefits from financial misfortune.
- 3. The elimination of usury laws in America from 1978-1980 ushered in an era of deregulation that allowed financial markets to run wild**, accelerating the present economic crisis.
- 4. The elimination of usury laws helped shift the investment of American capital and talent away from manufacturing** and material innovation and into an unproductive financial sector based on trading paper rather than producing long-term wealth. That shift has damaged other sectors of the economy, decimated America's labor force and weakened America's position in the world.

For all of these reasons, Metro IAF supports a 10% cap on interest rates. This return to solid financial regulation will restore a moral order to our economy, protect people from financial exploitation, and steer our economy back on a sustainable path of growth.

II. The History Against Usury

- For most of recorded human history, usury has been prohibited by moral, religious, cultural, legal, and ethical codes.¹ The Code of Hammurabi,

one of the oldest sets of laws discovered by modern archeology, prohibits lending at excessive interest. It was written circa 1750 BC in Babylon.

- In the Hebrew Bible, exhortations against usury are found both in the Torah and in the writings of the prophets. Exodus 22:25, Leviticus 25:36-37, and Deuteronomy 23:19-20 all explicitly forbid the people of God to lend at interest to one another.
- The Prophet Ezekiel (18:19-23) includes usury in his list of “abominable things” (along with murder, rape, robbery, and idolatry).
- In Islamic scripture, the prohibition against usury is equally strong (Q2:275-281), condemning the usurer and praising the lender who forgives the debtor in difficulty.
- Both Plato and Aristotle wrote against usury, prompting temporary regulation of interest in Athens. De-regulation caused an explosion of debt that resulted in wide-scale slavery and threats of revolt (800-600 BC).
- The Roman Empire capped interest rates at 8.33% in 433 BC, experimented with a raise to 12% in 88 BC, and returned it to 8.33% in 533 AD under the Justinian Code. This cap lasted until 1453 AD.
- In his literary masterpiece “The Inferno,” Dante imagines usurers occupying the seventh circle of hell – one floor lower than murderers.
- In medieval England, those who loaned at interest faced confiscation of their land and property.
- In 1570, under Queen Mary, interest rates were capped at 10% -- a law that lasted until 1854.
- During the American colonial period, interest rates were capped at 8%. After 1776, each state adopted usury laws capping interest rates at 6%. These laws continued, with slight variations and increases, until 1978.

Until 1978, interest rate restraints were an accepted part of the American financial and political landscape. During the early part of the 20th century, some states raised the caps to 10-12%. The Uniform Loan Law allowed specially-licensed lenders to

charge rates of up to 36% for certain types of regulated loans. This was an exception. Laws against usury were the rule.

There were no payday loans, no adjustable-rate mortgages, no rapid-refund tax return schemes, and no sky-high interest rates on credit cards. This is not to say that there was no usury in America at this point. Organized crime ran loan sharks operated. They were more isolated. And they didn't have the ability to destroy millions of lives and the core of the economy.

However, in 1978, the U.S. Supreme Court ruled that national banks could apply the interest rates allowed by the states granting them charters anywhere in the nation. These national banks chose to be chartered in South Dakota and Delaware which had eliminated their interest rate caps and thus undermined the local usury caps of all the other states.

Then, in 1980, as a result of the most expensive lobbying campaign from the banking industry to date, the U.S. Congress passed the Depository Institutions Deregulation and Monetary Control Act. This law exempted all federally chartered savings banks and other financial service companies from state usury limits – effectively overriding all state usury laws.

III. The Cost of Usury on the Individual

Congregations that are part of Metro IAF organizations have conducted surveys and small group meetings assessing how much money people in our congregations are spending on high-interest debt. Before we organized this exercise, many members didn't even realize how much of their budget went towards paying down interest on usurious loans:

- **Payday loans** charging an annualized rate of over 300% (in Maryland, the Baltimore IAF affiliate successfully organized for the state-wide abolition of payday lending in 1998).
- **Adjustable-rate mortgages** with interest rates ballooning up to 15%
- **Rapid-refund tax return companies** that charge take 50% of the customer's tax return for a two-month advance – or up to a 300% annualized rate.
- **Credit card companies** that raise rates without

reason or notification, and tack on fees for both good behavior and bad. (The recent credit card reform law signed by President Obama in 2009 mandates that credit card companies notify the consumer of interest rate increases, but does not limit how much interest they can charge).

- **Banks** that charge \$50 or more for “overdraft protection” – essentially a high-rate loan for the amount of the overdrawn check.
- **Check-cashing fees** of 10% that are in effect exorbitant interest on the two-day period it takes for the check cashing agency to clear the customer's check.

These interest payments constitute money that families cannot use to save for the future or to stimulate the economy today.

In just 30 years, usurious interest rates have insinuated themselves into every corner of the American financial landscape. The consequence is that more and more Americans are caught in a spiral of debt from which they may never escape. In 1980, total consumer debt totaled \$355 billion. In 2008, consumer debt totaled \$2.6 trillion – an increase of 733%.

The average American household in 2008 held nearly \$8,700 in credit card debt.² In 2008, almost 1.2 million Americans filed for bankruptcy – a 31% increase from 2007.³

Unregulated interest rates have undermined the financial stability of individual American families. But 30 years of usury have also undermined the American economy as a whole.

IV. An Epidemic of Deregulation

To understand the role of proper regulation in protecting our economy, we must look back to the last major economic crisis: The Great Depression. It was caused in large part by the popping of a giant speculative bubble driven by investment firms that gambled extensively with depositors' money. When the bubble burst, depositors immediately went to their banks to claim their money (a “run on the bank”). But the money wasn't there, causing financial chaos, widespread bank failures, and a global economic crisis. To prevent such an economic disaster from striking again, the Franklin Delano Roosevelt administration enacted the following response⁴:

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1. **The Glass-Steagal Act of 1933**, which mandated separation between commercial and investment banks, thus preventing banks from speculating wildly with ordinary bank deposits.
 2. **The Securities Act of 1933/1934**, which created the Security and Exchange Commission to monitor and regulate the stock market, and to prohibit fraud in the sale of securities.
 3. **The Commodity Exchange Act of 1936**, which required that all commodities and futures be traded on a public, organized exchange so that everyone would know who is trading what to whom and for how much.

These laws, in combination with existing anti-usury legislation, curbed the excesses of the financial industry that caused the Great Depression. They allowed for adequate credit to flow through the markets while preventing panics and market collapse. They maintained a separation between the banking, investment, and insurance industries that minimized conflicts of interest and speculation. They promoted personalized financial institutions – like local community banks – that had a life-long relationship with their customers, understood their credit situation, and held on locally to any loans or credit they extended.

This system limited risk, but also limited potential returns. For this reason, beginning in the 1970s, banks and financial institutions began to chafe under the FDR-era restrictions. They argued that the regulatory structures of the 1930s were outdated, and prevented the banks from creating new, innovative financial products that would increase general wealth and prosperity. Since none of these institutions had an interest in another Great Depression occurring, they could and would effectively regulate themselves without government interference. The finance industry put \$300 million in lobbying money behind these arguments, thrown at both Democrats and Republicans. (Appendix 2 includes a summary list of the de-regulatory actions of the past 30 years).

This 30-year stretch of de-regulatory activity, starting with the repeal of anti-usury laws, has taken a tremendous toll on our economy. Americans have lost over \$4 trillion in value in their homes. Foreclosures continue to increase – 1.75 million in 2008 alone,

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with more coming in 2009 and 2010. Unemployment is at 10%, and government service cuts at the state and local level have been devastating.

V. Usury: The Cause of our Economic Crisis⁵

How did our economy become so dependent upon the financial sector that the popping of this bubble could cause such a dramatic depression? There have been several key developments in the 1970s and early 1980 that led to this dependence, of which the legalization of usury was most important.

The first important piece of context is the stagnation of real wages for American workers. Since 1972, the median hourly wage for Americans has stayed the same (indexed for inflation), and has in fact declined for the bottom 20% earners. At the same time, productivity has **doubled**. This means that people are working twice as effectively for the same, or less, money.

Secondly, reforms in the 1970s meant that employers could strip workers of benefits like pensions and health care by creating shell subsidiaries and transferring the liability to them. The subsidiaries would then file for chapter 11 protection, so the benefits would disappear. This change meant it was much harder for people to plan for the long term, so they stopped, and borrowed for the short-term instead.

Thirdly, the legalization of usury began in 1978 led to the removal of states' 9% caps on interest rates, as banks and credit card companies relocated to the states with no caps. Deregulation at this time also allowed the proliferation of fees. Suddenly, lending money became a hugely profitable enterprise.

Investors increasingly pulled their capital from manufacturing – the previous economic base of America – and switched it to finance. Manufacturing offered returns of in the region of 10%, whereas finance, in the form of loans and their derivatives, offered returns of 35%, and sometimes much more. With this sort of competition, profitable manufacturers could not attract the investment they needed to expand and create new jobs in their industry. Instead, they had two options: shift the jobs overseas, where lower labor costs could make them more competitive in attracting capital, or shut down entirely.

Finance won. In 1988, financial firms made only 18% of the profits that accrued to U.S. corporations. By 2002, it ballooned to 40%. Manufacturing now comprises only 12% of U.S. gross domestic product. Thus, the rise of finance at the expense of manufacturing was a significant factor in the loss of middle-class skilled manufacturing jobs, which has aggravated devastating job losses in Ohio, Michigan, and other parts of America’s industrial heartland.

At the same time, the role of the financial service industry changed. Originally, the useful social purpose of banking was to provide credit to businesses that produced goods and services that generated wealth. Interest and fees were allowed at a sufficient rate to keep the credit flowing so that the economy could function. Bankers made money for themselves by helping business make things that people needed.

However, with the repeal of usury laws, the purpose of the financial sector changed: it now existed primarily for the purpose of making more money itself, regardless of whether or not it facilitated the creation of actual tangible goods that make a society wealthy. In fact, it sought to divert capital from such endeavors and use it for making more money by trading paper back and forth. And it extorted usurious interest rates and fees from borrowers to feed its unsustainable growth.

Conclusion

There is a simple solution that will restore moral order and stability to our economy: re-instate a federal usury law capping interest at 10%.

Why 10%?

Because 10% is enough.

It is enough to allow credit to flow to all worthy borrowers. It is enough to allow bankers their fair share of profit. It is enough to protect families from permanent indebtedness. And it is enough to divert our economy away from speculative gambling and back towards productive wealth creation in the industries of the future: green manufacturing, sustainable energy, and others that the American entrepreneurial spirit has yet to imagine.

Appendix 1: Additional Resources

New York Times Business Section: http://topics.nytimes.com/top/reference/timestopics/subjects/c/credit_crisis/index.html?ref=business

“Since 1972, the median hourly wage for Americans has stayed the same...At the same time, productivity has doubled. This means that people are working twice as effectively for the same money.”

NPR’s Planet Money Series: <http://www.npr.org/templates/story/story.php?storyId=94427042>

Center for Public Integrity Investigative Series on the Top 25 Sub-Prime Lenders: http://www.publicintegrity.org/investigations/economic_meltdown/

Endnotes:

1. James M. Ackerman, Interest Rates and the Law: A History of Usury, 1981, Arizona St. L.J.61 (1981), http://www.afil.org/consumer_rsc/usury.php
2. <http://www.federalreserve.gov/econresdata/releases/statisticsdata.htm>
3. <http://www.reuters.com/article/GCA-Economy/idUSTRE5246GO20090305>
4. CQ Researcher, May 9 2008, Vol. 18, No. 18.
5. Geoghegan, Thomas. “Infinite Debt: How Unlimited Interest Rates Destroyed the Economy.” Harper’s. April 2009.

Key de-regulatory actions of the past 30 years^{1,2} Appendix 2

The Depository Institutions Deregulation and Monetary Control Act of 1980:

- Allowed banks to merge, leading to the creation, consolidation, and domination of large national banks like Bank of America, JP Morgan Chase, and Citibank over local and regional banks that had personal relationships with their customers.
- Removed all interest rate caps, allowing financial institutions to charge whatever they chose.
- Raised the bar for prosecuting lawbreaking lenders.

The Alternative Mortgage Transaction Parity Act of 1982:

- Allowed non-federally-chartered housing lenders to invent and sell sub-prime mortgages, including adjustable rate mortgages, balloon payment mortgages, and interest-only mortgages.
- Precipitated predatory lending in urban areas.

Also in 1982, “Collateralized Mortgage Obligations” are invented to package and sell shares of sub-prime mortgages without regulation.

The 1987 replacement of Paul Volcker with Alan Greenspan as Chairman of the Federal Reserve: Greenspan:

- Believed that regulation impeded markets and “innovation.”
- Flooded the markets with cash for the dot-com and housing bubbles without proper controls.
- Did nothing about the proliferation of derivatives such as Credit Default Swaps and Mortgage Backed Securities, even though they represented massive risk and were dubbed “financial weapons of mass destruction” by investor Warren Buffett.

The Interstate Banking Act of 1994 eliminates restrictions on interstate banking.

The Gramm-Leach-Bliley Act of 1999, which:

- Repealed parts of the Glass-Steagal act, allowing the merger of banking, investment, and insurance companies.

- Allowed for new financial behemoths like Citigroup, JP Morgan Chase, American Insurance Group, Goldman Sachs, and Bank of America to invest recklessly with depositor’s money.
- Changed the culture of commercial banks from agencies that manage people’s money conservatively to high-risk ventures looking for high yield returns.
- Was passed with a bi-partisan vote of congress and signed by President Bill Clinton.

The Commodity Futures Modernization Act of 2000, which:

- Prohibited the regulation of Credit Default Swaps and other banking products created to make money off of the movement of markets (rather than the price of actual goods and services).
- Precipitated the explosion of the unregulated Credit Default Swap market from zero to \$45 trillion in 2007, and then a collapse that led to the implosion of Bear Sterns, Lehman Brothers, and the near-death of AIG (saved only with a massive infusion of taxpayer money).

The Sarbanes-Oxley Act of 2002, which:

- Failed to deal with the root problems of the Enron and WorldCom accounting scandals.
- Created a culture that allowed CEOs to distort information to pump up share prices, and encouraged credit rating agencies to look the other way.

In 2004, the Securities and Exchange Commission increased the debt-to-capital ratio investment banks could hold from 12:1 to 30:1, which:

- Allowed them to buy more sub-prime mortgage backed securities with less in reserves.
- Assumed banks would regulate themselves.

Endnotes:

1. Stiglitz, Joseph. “Capitalist Fools.” Vanity Fair. January 2009. <http://www.vanityfair.com/magazine/2009/01/stiglitz200901>
2. Greider, William. “Economic Free Fall?” The Nation. August 18/25, 2008.

Myths and Realities Appendix 3

Myth:

Capping interest rates will result in drying up credit for poor people.

Reality:

- Financial institutions have always figured out how to conduct profitable business serving poor people, and they will continue to do so under reasonable limits that protect the consumer. In fact, credit unions, a multi-billion non-profit financial institution sector in the US, prosper providing consumer loans, credit cards, unsecured loans, mortgages, financial counseling, etc to all types of borrowers, including poor people—all at interest rates well below their industry's legal cap of 18%. Limited government funds should be used to expand credit unions' services to low-income borrowers not bailing out for-profit financial institutions that charge high interest rates and fees.
- We all agree that non-credit-worthy consumers should not be encouraged to take on debt, especially at high interest rates that will prevent them from ever escaping indebtedness. One of the causes of the present crisis was the aggressive marketing of credit cards to people who would never be able to repay their debt.
- If those who lend to poor people at high rates were really doing so as an altruistic service, they would be reinvesting their profits in projects that help poor people escape indebtedness. We have seen no evidence that this is their true motivation.

Myth:

Capping interest rates will result in higher costs for people with good credit.

Reality:

- Banks and credit cards companies found it possible to make money by extending credit prior to the elimination of anti-usury laws in 1978.

- Banks have been using exorbitant credit card profits to bankroll risky investments. This system must stop. There is plenty of money to be made in responsible lending to provide top service for credit-worthy consumers.

Myth:

People with bad credit should be discouraged from taking on debt. If rates are lower, poor people will borrow excessively.

Reality:

- High rates have not served as a deterrent. In fact, credit card companies have sought aggressively to recruit poor people for high-interest loans.
- Capping interest rates will require that lenders exercise conservative judgment in extending credit.

Myth:

Putting restrictions on the financial sector will stifle innovation and slow down our recovery.

Reality:

- For most of American history, financial institutions were able to thrive with reasonable interest rate caps.
- Credit flowed throughout the market, and businesses were able to obtain the financing they need to create jobs and build American wealth.
- Our economic recovery cannot be based on expansion of the financial sector. The growth of the past 30 years was a bubble. The soundest way to economic recovery is to steer our economy back towards wealth-generating production. The re-institution of usury laws will return our economy back to the right path.