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The Poverty Business

Inside U.S. companies' audacious drive to extract more profits from the nation's working poor

Roxanne Tsosie decided in late 2005 to pull her life together. She was 28 years old and still lived in her mother's two-room apartment in a poor neighborhood in southeast Albuquerque known as the War Zone. She survived mostly on food stamps and welfare. The Tsosies are Navajo, and Roxanne's mother wanted to move back to a reservation in western New Mexico where the family has a dilapidated house lacking electricity and running water. Roxanne, unmarried and with four children of her own, could make out her future, and she didn't like what she saw.

With only a high school diploma, her employment options were limited. She landed a job as a home-health-care aide for the elderly and infirm. It paid $15,000 a year and required that she have a car to make her rounds of Albuquerque and its rambling desert suburbs. A friend told her about a used-car place called J.D. Byrider Systems Inc.

The bright orange car lot stands out amid a jumble of payday lenders, pawn shops, and rent-to-own electronics stores on Central Avenue in the War Zone. Signs in Spanish along the street promise "Financiamos a Todos"—Financing for All. On the same day she walked into Byrider, Tsosie drove off, jubilant, in a 1999 Saturn subcompact she bought entirely on credit. "I was starting to think I could actually get things I wanted," she says.

In recent years, a range of businesses have made financing more readily available to even the riskiest of borrowers. Greater access to credit has put cars, computers, credit cards, and even homes within reach for many more of the working poor. But this remaking of the marketplace for low-income consumers has a dark side: Innovative and zealous firms have lured unsophisticated shoppers by the hundreds of thousands into a thicket of debt from which many never emerge.

Federal Reserve data show that in relative terms, that debt is getting more expensive. In 1989 households earning $30,000 or less a year paid an average annual interest rate on auto loans that was 16.8% higher than what households earning more than $90,000 a year paid. By 2004 the discrepancy had soared to 56.1%. Roughly the same thing happened with mortgage loans: a leap from a 6.4% gap to one of 25.5%. "It's not only that the poor are paying more; the poor are paying a lot more," says Sheila C. Bair, chairman of the Federal Deposit Insurance Corp.

Once, substantial businesses had little interest in chasing customers of the sort who frequent the storefronts surrounding the Byrider dealership in Albuquerque. Why bother grabbing for the few dollars in a broke man's pocket? Now there's a reason.

Armed with the latest technology for assessing credit risks—some of it so fine-tuned it picks up spending on cigarettes—ambitious corporations like Byrider see profits in those thin wallets. The liquidity lapping over all parts of the financial world also has enabled the dramatic expansion of lending to the working poor. Byrider, with financing from Bank of America Corp. (BAC) and others, boasts 130 dealerships in 30 states. At company headquarters in Carmel, Ind., a profusion of colored pins decorates wall maps, marking the 372 additional franchises it aims to open from California to Florida. CompuCredit Corp., based in Atlanta, aggressively promotes credit cards to low-wage earners with a history of not paying their bills on time. And BlueHippo Funding, a self-described "direct response merchandise lender," has retooled the rent-to-own model to sell PCs and plasma TVs.

The recent furor over subprime mortgage loans fits into this broader story about the proliferation of subprime credit. In some instances, marketers essentially use products as the bait to hook less-well-off shoppers on expensive loans. "It's the finance business," explains Russ Darrow Jr., a Byrider franchisee in Milwaukee. "Cars happen to be the commodity that we sell." In another variation, tax-preparation services offer instant refunds, skimming off hefty fees. Attorneys general in several states say these techniques at times have violated consumer-protection laws.

Some economists applaud how the spread of credit to the tougher parts of town has raised home- and auto-ownership rates. But others warn that in the long run the development could slow upward mobility. Wages for the working poor have been stagnant for three decades. Meanwhile, their spending has consistently and significantly exceeded their income since the mid-1980s. They are making up the difference by borrowing more. From 1989 through 2004, the total amount owed by households earning $30,000 or less a year has grown 247%, to $691 billion, according to the most recent Federal Reserve data available.

"Having access to credit should be helping low-income individuals," says Nouriel Roubini, an economics professor at New York University's Stern School of Business. "But instead of becoming an opportunity for upward social and economic mobility, it becomes a debt trap for many trying to move up."

HAPPY AS SHE WAS with the Saturn (GM) she bought in December, 2005, Roxanne Tsosie soon ran into trouble paying off the loan on it. The car had 103,000 miles on the odometer. She agreed to a purchase price of $7,922, borrowing the full amount at a sky-high 24.9%. Based on her conversation with the Byrider salesman, she thought she had signed up for $150 monthly installments. The paperwork indicated she owed that amount every other week. She soon realized she couldn't manage the payments. Dejected, she agreed to give the car back, having already paid $900. "It kind of knocked me down," Tsosie says. "I felt I'd never get anywhere."

The abortive purchase meant Byrider could dust off and resell the Saturn. Nearly half of Byrider sales in Albuquerque do not result in a final payoff, and many vehicles are repossessed, says David Brotherton, managing partner of the dealership. A former factory worker, he says he sympathizes with customers who barely get by. "Many of these people are locked in a perpetual cycle" of debt, he says. "It's all motivated by self-interest, of course, but we do want to help credit-challenged people get to the finish line."

Byrider dealers say they can generally figure out which customers will pay back their loans. Salesmen, many of whom come from positions at banks and other lending companies, use proprietary software called Automated Risk Evaluator (ARE) to assess customers' financial vital signs, ranging from credit scores from major credit agencies to amounts spent on alimony and cigarettes.

Unlike traditional dealers, Byrider doesn't post prices—which average $10,200 at company-owned showrooms—directly on its cars. Salesmen, after consulting ARE, calculate the maximum that a person can afford to pay, and only then set the total price, down payment, and interest rate. Byrider calls this process fair and accurate; critics call it "opportunity pricing."

So how did Byrider figure that Tsosie had $300 a month left over from her small salary for car payments? Barely a step up from destitution, she now lives in her own cramped apartment in a dingy two-story adobe-style building. Decorated with an old bow and arrow and sepia-tinted photographs of Navajo chiefs, the apartment is also home to her new husband, Joey A. Garcia, a grocery-store stocker earning $25,000 a year, his two children from a previous marriage, and two of Tsosie's kids. She and Garcia are paying off several other high-interest loans, including one for his used car and another for the $880 wedding ring he bought her this year.

Asked by BusinessWeek to review Tsosie's file, Byrider's Brotherton raises his eyebrows, taps his keyboard, and studies the screen for a few minutes. "We probably should have spent more time explaining the terms to her," he says. Pausing, he adds that given Tsosie's finances, she should never have received a 24.9% loan for nearly $8,000.

That still leaves her $900 in Byrider's till. "No excuses; I apologize," Brotherton says. He promises to return the money (and later does). In most transactions, of course, there's no reporter on the scene asking questions.

A QUARTER-CENTURY ago, Byrider's founder, the late James F. Devoe, saw before most people the untapped profits in selling expensive, highly financed products to marginal customers. "The light went on that there was a huge market of people with subprime and unconventional credit being turned down," says Devoe's 38-year-old son, James Jr., who is now chief executive.

The formula produces profits. Last year, net income on used cars sold by outlets Byrider owns averaged $828 apiece. That compared with only $223 for used cars sold as a sideline by new-car dealers, and a $31 loss for the typical new car, according to the National Automobile Dealers Assn. Nationwide, Byrider dealerships reported sales last year of $700 million, up 7% from 2005.

"Good Cars for People Who Need Credit," the company declares in its sunny advertising, but some law enforcers say Byrider's inventive sales techniques are unfair. Joel Cruz-Esparza, director of consumer protection in the New Mexico Attorney General's Office from 2002 to 2006, says he received numerous complaints from buyers about Byrider. His office contacted the dealer, but he never went to court. "They're taking advantage of people, but it's not illegal," he says.

Officials elsewhere disagree. Attorneys general in Kentucky and Ohio have alleged in recent civil suits that opportunity pricing misleads customers. Without admitting liability, Byrider and several franchises settled the suits in 2005 and 2006, agreeing to inform buyers of "maximum retail prices." Dealers now post prices somewhere on their premises, though still not on cars. Doing so would put them "at a competitive disadvantage," says CEO Devoe. Sales reps flip through charts telling customers they have the right to know prices. Even so, Devoe says, buyers "talk to us about the price of the car less than 10% of the time."

Tsosie recently purchased a 2001 Pontiac from another dealer. She's straining to make the $277 monthly payment on a 14.9% loan.

Nobody, poor or rich, is compelled to pay a high price for a used car, a credit card, or anything else. Some see the debate ending there. "The only feasible way to run a capitalist society is to allow companies to maximize their profits," says Tyler Cowen, an economist at George Mason University in Fairfax, Va. "That will sometimes include allowing them to sell things to people that will sometimes make them worse off."

Others worry, however, that the widening income gap between the wealthy and the less fortunate is being exacerbated by the spread of high-interest, high-fee financing. "People are being encouraged to live beyond their means by companies that are preying on low-income consumers," says Jacob S. Hacker, a political scientist at Yale.

Higher rates aren't deterring low-income borrowers. Payday lenders, which provide expensive cash advances due on the customer's next payday, have multiplied from 300 in the early 1990s to more than 25,000. Savvy financiers are rolling up payday businesses and pawn shops to form large chains. The stocks of five of these companies now trade publicly on the New York Stock Exchange (NYX) and NASDAQ (NDAQ). The investment bank Stephens Inc. estimates that the volume of "alternative financial services" provided by these sorts of businesses totals more than $250 billion a year.

Mainstream financial institutions are helping to fuel this explosion in subprime lending to the working poor. Wells Fargo & Co. (WFC) and U.S. Bancorp (USB) now offer their own versions of payday loans, charging $2 for every $20 borrowed. Based on a 30-day repayment period, that's an annual interest rate of 120%. (Wells Fargo says the loans are designed for emergencies, not long-term financial needs.) Bank of America's revolving credit line to Byrider provides up to $110 million. Merrill Lynch & Co. (MER) works with CompuCredit to package credit-card receivables as securities, which are bought by hedge funds and other big investors.

Once, major banks and companies avoided the poor side of town. "The mentality was: Low income means low revenue, so let's not locate there," says Matt Fellowes, a researcher at the Brookings Institution in Washington, D.C. Now, he says, a growing number of sizable corporations are realizing that viewed in the aggregate, the working poor are a choice target. Income for the 40 million U.S. households earning $30,000 or less totaled $650 billion in 2004, according to Federal Reserve data.

John T. Hewitt, a pioneer in the tax-software industry, recognized the opportunity. The founder of Jackson Hewitt Tax Service Inc. (JTX) says that as his company grew in the 1980s, "we focused on the low-hanging fruit: the less affluent people who wanted their money quick."

In the 1990s, Jackson Hewitt franchises blanketed lower-income neighborhoods around the country. They soaked up fees not just by preparing returns but also by loaning money to taxpayers too impatient or too desperate to wait for the government to send them their checks. During this period, Congress expanded the Earned-Income Tax Credit, a program that guarantees refunds to the working poor. Jackson Hewitt and rival tax-prep firms inserted themselves into this wealth-transfer system and became "the new welfare office," observes Kathryn Edin, a visiting professor at Harvard University's John F. Kennedy School of Government. Today, recipients of the tax credit are Jackson Hewitt's prime customers.

"Money Now," as Jackson Hewitt markets its refund-anticipation loans, comes at a steep price. Lakissisha M. Thomas learned that the hard way. For years, Thomas, 29, has bounced between government assistance and low-paying jobs catering to the wealthy of Hilton Head Island, S.C. She worked most recently as a cashier at a jewelry store, earning $8.50 an hour, until she was laid off in April. The single mother lives with her five children in a dimly lit four-bedroom apartment in a public project a few hundred yards from the manicured entrance of Indigo Run, a resort where homes sell for more than $1 million.

Thomas finances much of what she buys, but admits she usually doesn't understand the terms. "What do you call it—interest?" she asks, sounding confused. Two years ago she borrowed $400 for rent and food from Advance America Cash Advance Centers Inc. (AEA), a payday chain. She renewed the loan every two weeks until last November, paying more than $2,500 in fees.

This January, eager for a $4,351 earned-income credit, she took out a refund-anticipation loan from Jackson Hewitt. She used the money to pay overdue rent and utility bills, she says. "I thought it would help me get back on my feet."

A public housing administrator who reviews tenants' tax returns pointed out to Thomas that Jackson Hewitt had pared $453, or 10.4%, in tax-prep fees and interest from Thomas' anticipated refund. Only then did she discover that various services for low-income consumers prepare taxes for free and promise returns in as little as a week. "Why should I pay somebody else, some big company, when I could go to the free service?" she asks.

The lack of sophistication of borrowers like Thomas helps ensure that the Money Now loan and similar offerings remain big sellers. "I don't know whether I was more bothered by the ignorance of the customers or by the company taking advantage of the ignorance of the customers," says Kehinde Powell, who worked during 2005 as a preparer at a Jackson Hewitt office in Columbus, Ohio. She changed jobs voluntarily.

State and federal law enforcers lately have objected to some of Jackson Hewitt's practices. In a settlement in January of a suit brought by the California Attorney General's Office, the company, which is based in Parsippany, N.J., agreed to pay $5 million, including $4 million in consumer restitution. The state alleged Jackson Hewitt had pressured customers to take out expensive loans rather than encourage them to wait a week or two to get refunds for free. The company denied liability. In a separate series of suits filed in April, the U.S. Justice Dept. alleged that more than 125 Jackson Hewitt outlets in Chicago, Atlanta, Detroit, and the Raleigh-Durham (N.C.) area had defrauded the Treasury by seeking undeserved refunds.

Jackson Hewitt stressed that the federal suits targeted a single franchisee. The company announced an internal investigation and stopped selling one type of refund-anticipation loan, known as a preseason loan. The bulk of refund loans are unaffected. More broadly, the company said in a written statement prepared for BusinessWeek that customers are "made aware of all options available," including direct electronic filing with the IRS. Refund loan applicants, the company said, receive "a variety of both verbal and written disclosures" that include cost comparisons. Jackson Hewitt added that it provides a valuable service for people who "have a need for quick access to funds to meet a timely expense." The two franchises that served Thomas declined to comment or didn't return calls.

VINCENT HUMPHRIES, 61, has watched the evolution of low-end lending with a rueful eye. Raised in Detroit and now living in Atlanta, he never got past high school. He started work in the early 1960s at Ford Motor Co.'s hulking Rouge plant outside Detroit for a little over $2 an hour. Later he did construction, rarely earning more than $25,000 a year while supporting five children from two marriages. A masonry business he financed on credit cards collapsed. None of his children have attended college, and all hold what he calls "dead-end jobs."

Over the years he has "paid through the nose" for used cars, furniture, and appliances, he says. He has borrowed from short-term, high-interest lenders and once worked as a deliveryman for a rent-to-own store in Atlanta that allowed buyers to pay for televisions over time but ended up charging much more than a conventional retailer. "You would have paid for it three times," he says. As for himself, he adds: "I've had plenty of accounts that have gone into collection. I hope I can pay them before I die." His biggest debts now are medical bills related to a heart condition. He lives on $875 a month from Social Security.

Around the time his health problems ended his work as a bricklayer eight years ago, Humphries picked up a new hobby, computer programming. The shelves of the tidy two-room apartment where he lives alone, in a high-rise on Atlanta's crime-ridden South Side, are crammed with books on programming languages Java, C++, and HTML. He spends most days at his PC on a wooden desk nestled in the corner.

When his computer broke down in 2005, Humphries fretted that he would never be able to afford a new one. A solution appeared one night in a TV ad for a company with a catchy name. BlueHippo offered "top-of-the-line" PCs, no credit check necessary. He telephoned the next day.

He remembers the woman on the other end describing the computer in vague terms, but she was emphatic about getting his checking account information. She said BlueHippo would debit the account for $124, and Humphries then would owe 17 payments of $71.98 every other week. At the time, $800 would have bought a faster computer at Circuit City Stores, (CC) but he didn't have the cash.

It wasn't until a week after placing his order that he realized that BlueHippo's terms meant he would pay $1,347.66 over nine months, Humphries says. He called to cancel. The company told him that would take as many as 10 days, he says. When he called again, a week later, a customer-service representative said cancellation would take an additional 15 days. "I sensed then that I had my hand in the lion's mouth," Humphries says. During his next call, a phone rep told him BlueHippo had a no-refund policy. He would lose his $124, even though he had never received a computer.

Humphries takes some responsibility for this frustrating encounter. "I should have done my homework" before ordering, he says. But he also believes he was "strong-armed" out of $124. He was angry enough to send a detailed complaint to the attorney general of Maryland, where BlueHippo is based. That led to his becoming a lead plaintiff in a private class action pending in California against the company. The suit alleges that scores of customers were similarly duped. BlueHippo denies the allegation and says it treats all customers fairly.

The attorneys general of New York and West Virginia are investigating the company, and the Illinois AG has filed a consumer-protection suit in that state. In response to a Freedom of Information Act request by BusinessWeek, the Federal Trade Commission says it has accumulated 8,000 pages of consumer complaints about BlueHippo. The FTC is investigating whether the company has engaged in deceptive practices.

Chief Executive Joseph K. Rensin started BlueHippo four years ago at the same Baltimore address where he had operated a company called Creditrust Corp. Creditrust, which bought other companies' bad customer debts, enjoyed some success but ultimately slid into Chapter 11 bankruptcy proceedings. In 2005, Rensin and his insurer agreed to pay $7.5 million to settle shareholder allegations that he made misleading statements in an attempt to inflate Creditrust's stock. Rensin and the company denied acting improperly.

Rensin established himself anew with BlueHippo, whose cartoon mascot adorns a sign in the lobby of its Baltimore building. Most of the 200 employees inside answer phones. Call-center training materials reviewed by BusinessWeek refer to BlueHippo's prime prospects as families, "typically $25k/yr income & less" who "have had trouble getting credit."

BlueHippo sells well-known brands such as Apple Inc. (AAPL) computers and Sony Corp. (SNE) televisions. Gateway Inc. (GTW) became a major supplier in December, 2003. "We've clearly been aware of their business model from the get-go," says Gateway spokesman David Hallisey. More recently, Gateway became troubled by customer complaints and decided earlier this year to sever ties with BlueHippo. Given its knowledge all along about BlueHippo's methods, why did the separation occur only this year? Hallisey explains: "We're publicly traded and trying to make a profit, so that's a consideration."

Three former workers say BlueHippo typically tries to commit consumers to regular electronic debits, then, as in the Humphries case, stalls when they cancel orders or ask about receiving shipment. Many customers give up, according to these employees. Refusing refunds, the company keeps whatever money it receives, whether or not it ships a computer, the trio of former employees say. "We knew we were misleading people. They weren't getting their computers," says Quinn Smith, a former call-center salesman who says he was fired last December after complaining about these practices. Smith has provided information to the plaintiffs in the California class action but isn't a party to the suit.

Rensin declined to comment. In a written statement, the company denied any impropriety. It said it ships purchases when promised, though it acknowledged that consumers who can purchase products outright "are better off" doing so, rather than using its "hybrid" layaway and installment financing. The company confirmed that it refuses refunds but said customers may "use any funds paid to purchase other items from BlueHippo." It added that its prices are relatively high because of the "added risk of dealing with customers who have poor credit." In contrast to its training materials, the company said its typical customer earns more than $40,000 a year.

A few months after his BlueHippo experience, Humphries did buy a new computer. He borrowed $400 from a friend and bought a General Quality PC from Fry's Electronics, a retail chain. The loan covered the purchase of a 17-inch flat-screen monitor, a DVD burner, and a desktop computer with a 40-gigabyte hard drive. Humphries tightened his belt and paid his friend back in $100 installments over four months, interest-free.

JUST LIKE EVERYONE else, the working poor find their mailboxes stuffed with "pre-approved" credit card offers. Luisa and Rose Ajuria have trouble saying no. The Ajuria sisters live in a brown-brick bungalow on Chicago's financially pressed South Side. They care for a niece named Caroline and five cats. Neither sister studied past high school or married. "Momma said I wasn't college material," says Luisa, 57. She and Rose, 54, lived most of their lives under the strict supervision of their father, Manuel, who died in 1993. A Mexican immigrant and former sheet-metal press operator, he dutifully paid all the bills. Every week, Luisa handed him her paycheck from Warshawsky & Co., an auto-parts seller where she worked as a supervisor.

The sisters now manage their finances themselves—by their own admission, badly. Their father had paid off the $60,000 mortgage. But twice in the past six years, Luisa refinanced the cluttered bungalow, using the money to pay bills and repair aging fixtures in two bathrooms and the kitchen of the 75-year-old house. Now there's a new $140,000 mortgage, with Wells Fargo charging 8% interest. The $1,130 monthly payments eat up more than half of Luisa's paycheck from her current job as a secretary at the IRS. If she also made full payments on a $9,000 home-equity line of credit from HSBC Finance Corp. (HBC) and a half-dozen credit-card accounts, they would consume the rest. In total, Luisa owes creditors $169,585. "I don't read things. I just sign them," she says.

The debt has forced the Ajurias to consider selling their house and moving to an apartment. But it hasn't stopped companies from offering more credit. Last year, Rose received a come-on for a Tribute MasterCard. She was surprised a company would offer her credit, since she brings in only about $7,500 a year in disability benefits and wages as a part-time worker at an adult-day-care center. She signed up for the card.

Caroline, the 32-year-old niece, who is agoraphobic and rarely leaves the house, quickly ran up $1,268 in charges on the Tribute card, shopping online for Christmas and birthday gifts. Of her newest card, Rose says: "I regret this one. Truly, I do."

Terms of the Tribute MasterCard are a world away from the money-back and frequent-flier offers familiar to more prosperous cardholders. Marketed by Atlanta-based CompuCredit, a giant in the subprime card business, Tribute MasterCard offers no such fringe benefits. Rose Ajuria's card carries an interest rate of 28%, compared with about 10% on a typical card. Since she's paying only a nominal $10 a month, the debt her niece incurred is growing swiftly. "I think we've painted ourselves into a corner," Rose says. Many Tribute MasterCard customers pay a lower 20% interest, but CompuCredit typically charges them a $150 annual fee, a separate $6 monthly fee, and a one-time payment of $20 required before using the card.

This is the sort of choppy water where many of CompuCredit's customers paddle—and where the company manages to find profits. CompuCredit was co-founded 11 years ago by David G. Hanna, scion of a family that made a fortune in debt collection. Its 55-member analytics team has devised models to assess more than 200 categories of customer data, from the duration of past credit-card accounts to the number of bad debts. The algorithms apparently work: Last year, CompuCredit reported earnings of $107 million on $1.3 billion in revenue.

Whether the company will make money on Rose Ajuria's account is uncertain at this point. CompuCredit says that customers offered the Tribute MasterCard at 28% generally have middling credit histories and that it is willing to work with those who have trouble paying their bills.

Executives say the company clearly discloses interest rates and imposes fees up front so consumers won't be surprised later. But in February CompuCredit disclosed that the FTC and the FDIC had launched separate civil investigations into the marketing of one of its other credit cards. The company denies any wrongdoing. As a goodwill gesture, it says it has stopped charging late fees and interest on accounts more than 90 days past due.

On its Web sites and in its marketing brochures, CompuCredit says it helps customers "rebuild credit" by reporting all of their loan payments to credit bureaus, unlike traditional payday lenders. Not that altruism drives the operation, says co-founder Hanna. "We're not going to chase somebody where we can't make money."

EVEN FOR THOSE WHO climb above the lowest rungs of the economic ladder, a legacy of debt can threaten to undercut progress. Connie McBride, a 44-year-old computer programmer who lives near Tacoma, Wash., grew up in foster homes and has led an adult life notably lacking in stability. She has held decent jobs but sometimes has subsisted on food stamps. She earns $47,000 a year as a freelance programmer, working from the weather-beaten aluminum trailer she rents for $590 a month. Wind whistles through small holes in the walls, and she keeps warm in the winter by feeding a wood-fired stove on a cracked cement foundation.

McBride showed an early aptitude for math and received a GED at age 16. In the late 1980s, she studied computer science at Washington State University, sometimes arriving for class with her three young children. "Taking those classes, given my life, I felt this was the only way out," she says.

She graduated in 1992, owing $45,000 on student loans. That debt became her main financial burden, she says. The 9.5% interest rate isn't particularly steep, but she tended to view the payments as less pressing than putting food on the table or paying rent. Late fees piled up. Today she owes $159,991, up from $117,000 only 18 months ago. When dunning notices arrive, she tosses them in the stove.

Personal bankruptcy proceedings in 2003 dissolved dozens of McBride's liabilities. But by law her debt to student lender SLM Corp. (SLM), better known as Sallie Mae, wasn't affected. Every month, $450 is garnisheed from her wages, reducing her take-home pay to $1,338. The garnishment doesn't even cover interest and penalties, let alone the principal. Says McBride: "There's no way this thing will ever be paid off."

New obligations are piling up. She pays $385 a month on a 21% car loan. And now she's buying baby supplies. McBride says her adult son can't deal with his 4-month-old daughter, who has medical problems. McBride can't bear the thought of her granddaughter going to a foster home. So she is postponing nonessential expenditures such as fixing a badly chipped front tooth.

McBride acknowledges her mistakes. "My life is full of bad decisions," she says. But if she had started out with the funds for college, she wonders whether she would at least be able to afford an apartment and a trip to the dentist. "If you have money to begin with, you don't have these issues or these kinds of bills," she says. "You don't have to worry about the rent or pay double for a car."

With Ben Elgin and Mara Der Hovanesian