November 7, 2019

The Honorable Maxine Waters
Chairwoman
U.S. House Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Patrick McHenry
Ranking Member
U.S. House Committee of Financial Services
2004 Rayburn House Office Building
Washington, D.C. 20515

Re: Opposition to the Veterans and Consumers Fair Credit Act

Dear Chairwoman Waters:

On behalf of the Online Lenders Alliance (OLA), the center for lending, technology, and innovation representing the growing online lending industry, I wanted to submit to the Committee our very serious concerns regarding the Veterans and Consumers Fair Credit Act, which we understand may be considered in the near future. We are concerned that we do not properly understand or are able to anticipate the unintended consequences resulting from this legislation. This bill has the potential for consumers to seek out products that are less regulated pose a greater harm and may put them in greater financial hardship. It would be a failure to consider or understand the negative ramifications for millions of non-prime individuals and families. This legislation would remove access to credit for millions of Americans and leave them without options. It is because of this we urge the committee to halt this legislation until there is more independent research done to better understand the impact of this bill.

When OLA was founded over a decade ago, our mission was simple: to promote a diverse and responsible marketplace for access to innovative online financial services through education, communication, collaboration and advocacy.

We work tirelessly to ensure consumers are protected and to better understand the diversity of credit products available to them. This focus on consumer protection is what separates us from others within our industry.

OLA’s strict standards are what created the OLA seal, which indicates that consumers can trust the company they are working with to be committed to the highest standards of conduct and dedicated to ensuring the best possible experience for their customers. OLA companies are compliant with federal laws that protect consumers from fraudulent activity. In addition, we have established and maintain the OLA consumer hotline, which allows consumers to report issues with bad actors in the marketplace and speak with a live operator who can help them navigate the online lending market.
We also work with a third party to police the industry at large for fraudulent activity or violations of our Best Practices. When fraud or improper behavior is uncovered, OLA promptly reports the violation to the authorities. Our most recent Policing the Internet report shows that more than 1 million websites have been crawled. Our focus on consumer protection is one reason that the proposed Veterans and Consumers Fair Credit Act is so alarming.

What is most alarming, though, is that there is no independent research examining the real-life impacts of rate caps and their impact on consumers. This point was clearly indicated by Garry Lacy Reeder II, Vice President for Policy and Innovation at the Center for Financial Services Innovation, an organization that operates independently. In his written testimony ahead of the April 30th hearing before your Committee, when talking about bank-issued SDC, “CFSI recognizes that there is often a trade-off between cost and availability. We encourage policymakers to allow institutions to experiment along the cost and availability spectrum, including for products with pricing above 36% APR.” At the same hearing, Todd Ortique McDonald, Vice President and Board Director at the Liberty Bank & Trust Company, who was representing the National Bankers Association, indicated that they are only able to provide services to non-prime consumers when they have assistance from the Community Development Financial Institutions Fund.

On the surface, the Military Lending Act operates in an efficient and appropriate manner. However, it is vital that additional independent studies are done to clearly understand its wide-ranging impacts. Involvement from the Department of Defense (DoD) must include data procured by the credit bureaus to see how many servicemembers are denied credit. Initial reports from DoD suggest that credit card debt has increased and that servicemembers are susceptible to costly overdraft fees as a result of the MLA – adverse effects that we would be wise to avoid replicating on a wider population.

Millions of additional, non-military Americans live paycheck to paycheck. Nearly 40% of American families don’t have enough savings to cover a $400 emergency expense as noted by the Federal Reserve System’s Board of Governors in the Report on the Economic Well-Being of U.S. Households in 20181. Sadly, when faced with this kind of expense, credit cards aren’t an option for every consumer and the small dollar amount needed doesn’t come close to meeting the minimum threshold to obtain a bank loan. This leaves many Americans without options at a time when they need help the most. While regulations like this are often hailed as credit inclusion, in reality it is an illusion for consumers.

Consumers with higher incomes and strong credit histories can borrow from banks, leverage an asset, or tap into savings during a crisis, but Americans without prime credit scores don’t enjoy the same access. According to a recent study by the Fair Isaac Corp, 46 percent of consumers have FICO scores below 700, effectively shutting them out of the traditional bank-loan market. They do, however, turn to consumer finance loans to meet their unique needs and understanding both the costs and benefits of the products.

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Restrictive Rates Constrain Access to Credit

Restrictive rate caps can significantly impinge on credit availability – and non-prime consumers are disproportionally hurt.

- According to a study from the World Bank\(^2\), “while some forms of interest rate caps can indeed reduce lending rates and help to limit predatory practices by formal lenders, interest rate caps often have substantial unintended side-effects. The side-effects included: increases in non-interest fees and commissions; reduced price transparency; lower number of institutions and reduced branch density; and adverse impacts on bank profitability, in addition to the lack of access for smaller and riskier borrowers.”

- A study\(^3\) by researchers at the Mercatus Center of George Mason University showed that restrictive rate caps in Arkansas resulted in a large portion of residents on the state border seeking loans in neighboring states while interior residents were consigned to a credit desert. “Of the 26,654 installment loans in the dataset that are outstanding in Arkansas, 96.7 percent were held by Arkansas residents who live in counties adjacent to one of the six bordering states. Despite comprising about 55 percent of the state’s population, residents of interior counties held just 3 percent of the outstanding installment loans,” the study found.

- The Military Lending Act’s 36 percent APR cap has limited access to credit, has forced military members to conceal their status, and has forced spouses to conceal their marriages to servicemembers so that they can qualify for a loan. Recently, a consumer activist wrote that alternatives are not ideal, and that military has had to “employ a variety of strategies to address cash flow shortfall...including payment plans with utilities, credit cards, pawn loans, financial assistance from a local nonprofit, loans from religious institutions, building savings and income and turning to friends and family.”\(^4\)

Experience demonstrates that restrictive rate caps will limit consumer access to credit, especially for non-prime borrowers, as well as reducing credit options and limiting competition.

36 Percent Rate Cap is not Workable

\(^2\) Aurora Ferrari, Oliver Masetti, Jiemin Ren “Interest Rate Caps, The Theory and The Practice,” Finance, Competitiveness and Innovation Global Practice, World Bank Group, April 2018


A wealth of experience points to the reality that setting a 36 percent rate cap, which equates to just 3 percent per month, is simply not economically viable for lenders, therefore making access to credit for non-prime borrowers non-existent.

- A decade ago, the Federal Deposit Insurance Corporation (FDIC) oversaw a Small Dollar Loan Pilot Program that sought to keep rates below 36 percent APR. Once the program ran its course, many lenders stopped offering these loan products to nonprime borrowers because they were simply not economical for the financial institutions.5

- In 2018, U.S. Bank began offering a small-dollar, short-term loan product. The program has a limited scope to U.S. Bank customers with a current bank account. Even with the pricing advantages of lower capital costs and additional risk mitigation employed by U.S. Bank, in order for the program to be sustainable, **U.S. Bank is charging interest rates between 71 percent and 88 percent APR — more than double the proposed 36 percent APR cap.**

These experiences demonstrate that even under the most favorable circumstances, lenders are unable to provide small-dollar, short-term credit when operating under a 36 percent rate cap.

**APR can be a Misleading Measure of Loan Cost**

While it has been noted that 39 states have adopted APR caps, that figure can be misleading when looking at unsecured consumer financial lending. The National Consumer Law Center (NCLC) count of 39 states with interest rate and fee caps was based on a **$10,000 five-year loan**. These are decidedly not reflective of unsecured consumer finance loans (which average under $5,000) and are unlikely to be made to non-prime unsecured borrowers. Some lenders focus on higher principal, longer-term loans, often with qualifying standards that exclude many non-prime borrowers. Significantly, these larger and longer-term loans can be more profitable, despite carrying the same or lower APR. That is why APR can be a misleading measure when determining the cost of a loan to a borrower.

**APR Cap Not Proven Helpful, May be Harmful**

There has been little follow up study on the impact of rate caps on credit access for non-prime consumers. Here are some additional facts that OLA believes the committee should know:

- A Federal Reserve staff report studied the consequences of 36 percent APR results on North Carolina and Georgia and found that residents bounced checks, were late on paying bills and ultimately filed more bankruptcies.6

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6 Payday Holiday: How Households Fare after Payday Credit Bans. Donald P. Morgan and Michael R. Strain Federal Reserve Bank of New York Staff Reports, no. 309 November 2007; revised February 2008 [https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr309.pdf](https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr309.pdf)
• A Federal Reserve Staff working paper states “Consumer finance loans would not be available to many higher risk, nonprime consumers in low rate states because such loans would be unprofitable.”

• In her book, The Unbanking of America, Professor Lisa Servon describes her experience working at a check cashier in the Bronx, where New York’s maximum APR is 25 percent. Consumers looking for a loan reported having to go to a loan shark or participating in an unregulated lending circle.

**Conclusion**

OLA is worried about the unintended consequences of this bill. It does not make sense to force one-size fits all APR pricing and disregard the costs involved with serving non-prime consumers with the short-term unsecured credit they demand and need. Without a doubt, this bill will block creditworthy Americans who deserve access to credit from obtaining it. We urge you to pursue policies that expand capital access, not those that will result in removing credit options for millions of Americans.

We respectfully request a more robust independent study and review to better understand the effect of an overarching rate cap before we exclude more than 100 million Americans from access to credit. We would also appreciate the opportunity to work with you on this important issue where we can find common ground, as well as to provide input on this legislation. If you have questions or need additional information, please feel free to contact me at mjack@oladc.org.

Sincerely,

Mary Jackson
President and CEO

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