March 9, 2021

The Honorable Heather Sanborn
Chair, Joint Health Coverage, Insurance and Financial Services Committee
3 State House Station
State House, Room 320
Augusta, ME 04333-0003

The Honorable Denise Tepler
Chair, Joint Health Coverage, Insurance and Financial Services Committee
2 State House Station
State House, Room 333
Augusta, ME 04333-0002

Re: LD 522 – An Act to Cap Interest Rates for Consumer Debt

Dear Chairs Sanborn and Tepler:

I write on behalf of the American Financial Services Association ("AFSA")[1] to express our grave concerns with LD 522, which would institute a 15 percent rate cap for all loans and other forms of consumer credit in the state. LD 522 would leave Maine consumers worse off and cut off access to credit for those most in need.

Rate Caps Cut Off Access to Credit

The finance charge on any specific loan is largely a combination of the individual borrower's risk profile (i.e. the likelihood the loan will be repaid in full at the end of the term), and, importantly, the fixed costs (e.g. overhead) for the lender. Because smaller loans generate a lower return with the same fixed costs, the finance charge must necessarily be higher in order to even recoup the cost of making the loan and break even. If rates are arbitrarily capped at 15 percent, small loans will be stuck well below the break even point and lenders will no longer be able to provide small loans to consumers who need them. These effects will stretch across other credit markets as well, potentially leaving borrowers without access to vehicle loans or open-ended credit. While wealthier or more sophisticated borrowers among Maine's elite may be able to find other sources of credit or afford larger loan sizes, lower income individuals will likely be left in credit deserts and forced to turn to more dangerous, or illegal, options like loan sharks.

Because our members report to credit bureaus, they help thousands of Maine adults graduate out of subprime credit scores each year—so we deeply understand the effects of this bill. This will have a ripple effect in those communities where unregulated lenders will operate and proliferate, debt costs will increase as will overall debt loads, and long-term wealth will decline when people lose access to both affordable credit and means to improve their credit scores. Elite borrowers will remain unaffected.

[1] Founded in 1916, the American Financial Services Association (AFSA), based in Washington, D.C., is the primary trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including direct and indirect vehicle financing, traditional installment loans, mortgages, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans.

Traditional Installment Loans are Safe and Affordable Credit

For short-term, small-dollar loans, the quality, affordability, and soundness of the loan is best judged by its structure not its interest rate. This is because interest rates on small amounts and short-term loans can be misleading as to cost. Annual percentage rate (APR) is a function of time and the loan term, rather than a measure of the dollar cost of a loan. For decades, traditional installment lenders have consistently provided consumers with reliable, community-based small-dollar credit that is accessible and affordable, giving borrowers a tried-and-tested mechanism to safely manage their household credit. Traditional installment loans (TILs) are widely acknowledged by consumer groups and others as a safe and affordable form of credit, carrying with them significant socio-economic benefits for individuals, families, and communities. This appreciation for TILs as tools of financial capability and even mobility, hinges on the fact that TILs are repaid in regularly scheduled, equal payments of principal and interest. Furthermore, unlike payday loans, TILs require an underwriting process that includes a calculation of the borrower's ability to repay a loan out of their monthly budget and also report loan performance directly to credit bureaus, which is vital for Maine borrowers looking to build a credit history and increase their financial mobility.

In fact, TILs have repeatedly been recognized as safe payday alternatives by government officials at both the federal and state levels. For instance, the National Black Caucus of State Legislators (NBCSL) have passed several resolutions in support of TILs, including one in 2016 that stated:

> NBCSL supports the expansion of Traditional Installment Loans as an affordable means for borrowers to establish and secure small dollar closed end credit while preventing cycle of debt issues inherent with non-amortizing balloon payment loans.[2]

This was also demonstrated recently by the willingness of the federal Consumer Financial Protection Bureau (CFPB) to exclude TILs from the provisions of its Payday Lending Rule.

Efforts by banks and credit unions to replicate small-dollar lending universally fail, even when propped up by government incentives. While banks and credit unions can be more selective about the borrowers they serve by limiting loans to existing members or customers, there is still no way that depository institutions can source, underwrite, and service small-dollar loans for all consumers at rates lower than installment lenders. Small loans are a critical source of credit, allowing a consumer to access sums of money that help them to deal with unforeseen circumstances. With additional credit options, individuals and families may build or repair their credit, consolidate debts, free up funds to deal with emergencies and take advantage of opportunities that would otherwise be missed.

We urge you to consider the reasons above and conclude that lower rate caps are not a solution for Maine and accordingly reject LD 522. Thank you in advance for your consideration of our

---

[2] NBCSL Resolution BED-16-21, *A Resolution Promoting Safe and Affordable Lending Practices*, available at https://nbcsl.org/public-policy/docs/file/56-resolution-bed-16-21.html

comments. If you have any questions or would like to discuss this further, please do not hesitate to contact me at 202-469-3181 or mkownacki@afsamail.org.

Sincerely,

Matthew Kownacki
Director, State Research and Policy
American Financial Services Association
919 Eighteenth Street, NW, Suite 300
Washington, DC 20006-5517

cc: Members of the Joint Health Coverage, Insurance and Financial Services