March 3, 2022

The Honorable Michelle Lujan Grisham
Governor
State of New Mexico
490 Old Santa Fe Trail
Room 400
Santa Fe, NM 87501

Re: HB 132

Dear Governor Lujan Grisham:

On behalf of the American Financial Services Association (AFSA)[1], we recognize your long effort to lower APR caps for small loans in your state has been successful. When it goes into effect next year New Mexico will become one of just four states to adopt a rate cap that comprehensively includes non-Truth in Lending Act (TILA) type considerations in the calculation. In fact, the definition of APR in New Mexico is so unique that it creates a **New Mexico-only definition of rate**. We remain concerned about the effects the rate cap will have on access to safe, affordable small-dollar credit in New Mexico, particularly those consumers who need credit most, and we have two ongoing areas of concern we'd like to bring to your attention for consideration as the new law is implemented.

ONGOING CONCERN #1: New Mexico-Only Definition of Rate

For over 50 years, the federal Truth in Lending Act (TILA) has provided a standard of how to calculate the annual percentage rate (APR) of loans, ensuring that all references to APR are consistent and require little interpretation. This allows consumers to have a clear understanding of the terms of credit and to compare similar loan products. Whereas TILA expressly excludes the costs of voluntary products and charges paid in comparable cash transactions from the APR calculation, HB 132's definition broadly includes "any ancillary product or service sold *or any fee charged in connection or concurrent with the extension of credit*."

In practice, this problematic definition will require the inclusion of fees that are unrelated to the extension of credit but concurrent with the credit transaction and even post-origination fees that **cannot be predicted or calculated in advance** because they are only incurred depending on the actions of the borrower.

[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 traditional installment loans, direct and indirect vehicle financing, mortgages, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans.

This definition is so broad that even a loan with a **zero percent TILA APR could violate the New Mexico-only definition**. Examples of various scenarios unique to New Mexico are outlined below:

- **Example 1:** A parking fee at the financial institution paid by the consumer when they get the loan. That is a "fee charged" and "concurrent" with the extension of credit. In New Mexico only, should this be included in the rate calculation?
- **Example 2:** A late fee for non-payment. That is a "fee charged in connection" with the extension of credit. If there is no loan, there is no late fee. Potential late fees are already disclosed to consumers in a loan agreement, but how can this be calculated into a New Mexico-only APR since only the actions of the consumer will dictate whether a late fee is ever incurred.
- **Example 3:** A non-sufficient funds (NSF) bank charge for a bounced check. That is a "fee charged in connection" with the extension of credit. If there is no loan, there is no NSF fee. But like example 2 above, only in New Mexico is this something where a creditor will apparently be expected to do an impossible task: calculate a fee that doesn't exist at the time of the loan into a rate. There is no way to do this.
- **Example 4:** Robert takes out an $8,000 loan and never pays a penny back, so the creditor sues him. The creditor wins and is awarded attorneys fees. Those fees are "in connection" with the extension of credit. No loan, no lawsuit, no attorneys fees. How is this calculated?
- **Example 5:** Tonya takes out a $6,000 one-year loan at ZERO PERCENT TILA APR. She never pays it back. She incurs $200 in monthly late fees, the creditor sues and is eventually awarded court fees and attorneys fees of $2,000. This ZERO PERCENT APR LOAN NOW VIOLATES THE LAW because $2,200 is more than 36%. This loan now violates New Mexico law. But the creditor **could not have known at the time of the loan that Tonya would not pay back the loan**. How can a creditor consider something in a rate calculation that has not occurred and likely will never occur?

These examples are just a few that we'd like to have a serious dialog about with your office. We know this could not have been the intention of the legislature—to a create a trap where no loan can be made by a regulated lender, even at zero percent APR. The solution is simple: follow the example of every other state in the country except Illinois, South Dakota, and Connecticut and use TILA (or another state's version of TILA) as the method for calculating rate in New Mexico.

We must assume that this definition was written by a zealous opponent of voluntary protection products sometimes sold in conjunction with loans. If our assumption is correct, then let's please use the interim before this law goes into effect to have a serious and frank discussion about these products. Please invite the voluntary protection product industry to the table to explain what these products are, how they're sold, and what they do to protect consumers. We hope you agree that is the most appropriate and honest way to address this issue—not sneaking it in and calling it "rate" when the Truth in Lending Act clearly rejects that notion.

ONGOING CONCERN #2: Access to Affordable Small-Dollar Credit Will No Longer Be Available in New Mexico

For over 100 years, 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 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.

The idea that banks and credit unions will pick up the slack from established licensed non-bank lenders is a pipedream. Regular attempts by private entities and government at all levels aimed at catalyzing the provision of small-dollar loans by credit unions simply retread a well-worn path to the unmistakable conclusion: banks and credit unions cannot successfully balance their business models with the provision of safe and affordable credit for non-prime borrowers, and loans for small dollar amounts cannot be made profitably at 36%.

Local credit unions made a big splash in the legislature by claiming they would commit to filling in the gap—and we noticed they briefly opposed the bill when they would have been asked not to comply with it but simply to report whether they can make true on their claim by providing to the state the same data that state-licensed financial already provide. But their own national organizations recognize these loans won't be made. In fact, the Credit Union National Association (CUNA) and the National Association of Federally-Insured Credit Unions (NAFCU) last summer filed comments in opposition to a similar rate cap proposed at the federal level. The associations noted in their comments that:

> [T]he adoption of a 36 percent all-in cap will essentially require lenders to offer larger, longer duration loans because these loans are "easier" to fit under the cap precisely due to their increased size and duration. **This effectively encourages borrowers to take on more debt or, for many borrowers with lower creditworthiness, pushes them out of the market for small dollar credit altogether**.[2]

As the United States Federal Reserve noted, creditors do not break even at 36% unless a loan is in excess of approximately $2,500.[3] New Mexico's current average loan size is under $1,000.

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[2] CUNA & NAFCU, *Joint Letter to the Senate Committee on Banking, Housing and Urban Affairs*, July 28, 2021, available at https://www.cuna.org/content/dam/cuna/advocacy/letters-and-testimonials/2021/072921_Senate%20Banking_MLA%20Rate%20Cap%20(2).pdf (emphasis added).

[3] "A loan amount of $2,530 is necessary to break even at 36 percent." *The Cost Structure of Consumer Finance Companies and Its Implications for Interest Rates: Evidence from the Federal Reserve Board's 2015 Survey of Finance Companies*, FEDS Notes, The Board of Governors of the Federal Reserve System, August 12, 2020 available at https://www.federalreserve.gov/econres/notes/feds-notes/the-cost-structure-of-consumer-finance-companies-and-its-implications-for-interest-rates-20200812.htm. AFSA notes that the break-even figure is for a 36% TILA APR. The amount of a loan would presumedly need to be larger in a state, like New Mexico will be starting next year, with an APR definition that includes items beyond TILA rate as "rate."

Small loans are a critical source of credit, allowing individuals and families to build or repair their credit, consolidate debts, free up funds to deal with emergencies, and take advantage of opportunities that would otherwise be missed.

In sum, we humbly request a technical fix to the new law to address the myriad problems created in the law's New Mexico-only definition of APR. And we register our ongoing concern about the loss of availability of very small dollar loans after the law goes into effect on January 1, 2023.

We ask to work with your office in the interim to address both of these concerns. If you have any questions or would like to discuss this further, please do not hesitate to contact me at your convenience.

Sincerely,

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