February 4, 2025

Pravina Raghavan
Director
Community Development Financial Institutions Fund
U.S. Department of the Treasury
1500 Pennsylvania Ave., NW
Washington, DC 20220

Re: Notice of Information Collection and Request for Public Comment; OMB Number: 1559-0051

Dear Ms. Raghavan:

The American Financial Services Association (AFSA)[1] appreciates the opportunity to comment on the Small Dollar Loan Program Application (SDLP) and agrees with the Community Development Financial Institutions (CDFI) Fund and the Treasury Department that CDFI applicants should engage in responsible financing practices. In the request for comment, the CDFI asks specifically about the "prohibited practices" portion of the application. We strongly disagree, though, with how the application defines responsible financing practices and will address that argument in the below comments. Given the imminent change in administration, it would be prudent to delay finalizing the application until a new director is appointed.

In the request for comment, the CDFI Fund asks:

10. The SDL Program Application states that the Awards will not be made to Applicants that engage in the Prohibited Practices listed in Table 1. Are the Prohibited Practices appropriate to prevent predatory or abusive lending practices that low-income borrowers often face? Why are why not? Are there any Prohibited Practices that should be added, eliminated, or clarified? What are they?

The Prohibited Practices are not an appropriate way to prevent predatory or abusive lending practices. The SDLP application prohibits companies that provide "high-rate loans" from applying for the program. These loans are defined as "Loans that exceed the lower of the following two rates: (1) an all-inclusive 36% APR (using the methodology prescribed in 32 CFR 232.4 of the Military Lending Act (referred to as the Military Annual Percentage Rate [MAPR]; or (2) the interest rate limit as set by the state agency that oversees financial institutions in your state."[2]

[1] Founded in 1916, AFSA is the national 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, mortgages, direct and indirect vehicle financing, payment cards, and retail sales finance.
[2] 89 FR 97167

An MAPR cap is poor way to evaluate whether a loan is predatory or abusive. Rate caps reduce access to credit. The use of MAPR instead of APR undermines the purpose of the Truth in Lending Act (TILA) and obscures the true cost of credit. As such, AFSA is asking that this prohibition be eliminated.

As opposed to an arbitrary number, loans should be evaluated on whether consumers have choices in the products they can be confident will provide benefits and meet their needs, the products are affordable and do not trap borrowers in cycles of debt, loan terms must be understandable, with documents that include all costs, clear terms, and conditions, and, consumers must be confident that their personal information and sensitive data is protected and respected.

A. Defining high-interest loans as "prohibited" is poor policy.

As AFSA has consistently noted, including in our recent Consumer Credit Confidence Index survey,[3] consumers are taking serious hits to their paychecks and wallets with ongoing inflation, layoffs, and economic uncertainty. There is similar uncertainty in the consumer credit industry, which helps generate trillions of dollars in economic activity each year. The availability of capital for all Americans is an ever present concern.

Maligning a loan by labeling it as "prohibited" could decrease consumer confidence in a product that is highly regulated, supervised, and potentially the best choice for certain consumers. It also perpetuates bad policy.

The facts on rate caps of any kind are clear:[4] they are unworkable and actually harm the consumers policymakers are trying to help, by limiting the types of credit tens of millions of Americans depend on more than ever. Several academic studies have proven that the data backs up concerns about rate caps tightening access to credit to the Americans who need it the most.

Research shows the Illinois rate restriction decreased the number of loans to subprime borrowers by 38 percent and increased the average loan size to subprime borrowers by 35 percent.[5] , and further found that the rate cap:

1. Increased the short-term debt of some borrowers, perhaps because the borrowers no longer had access to their form of credit due to the new law. The analysis also indicates short term debt dissipated a year or 18 months after the bill's passage.
2. "[I]s not associated with a significant change in credit scores among Illinois consumers who used alternative financial services loans, relative to peers in states with high APR caps."
3. Neither improved nor damaged credit scores after the rate cap was implemented, relative to similar consumers in states with high APR caps.

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[3] https://www.caseforcredit.com/c3index/
[4] https://www.caseforcredit.com/multimedia/
[5] Bolen, J. Brandon and Elliehausen, Gregory and Miller, Jr., Thomas W., Credit for me but not for thee: The effects of the Illinois rate cap (June 29, 2023). Available at SSRN: https://ssrn.com/abstract=4315919 or http://dx.doi.org/10.2139/ssrn.4315919

According to the Federal Reserve's report[6] on the Economic Well-Being of U.S. Households and the FDIC National Survey of Unbanked and Underbanked Households[7], 19% of Americans are unbanked or underbanked and need strong competition in the nonbank market. In 2020, the Federal Reserve issued a report on small dollar lending. The report[8] found:

1. With a 36% Truth-in-Lending Act APR cap, consumers would not be able to get loans for less than $2,530.
2. Because installment lenders have substantial fixed costs, high interest rates are necessary to provide sufficient revenue to cover the costs of providing such loans. Despite the many changes in consumer credit markets, a large share of costs of small personal loans at consumer finance companies remains fixed. Technology does not eliminate the need to have employees available to originate loans, process payments, and collect delinquent accounts.
3. If small loan revenue is constrained by rate ceilings, only large loans will be provided.
4. Consumers who need a small loan or only qualify for a small loan would not be served.

Researchers at the World Bank recently conducted a comprehensive review on the theory and practice of interest rate caps, and found that they can be harmful in six ways[9]:

1. Increases in non-interest fees and commissions,
2. Reduced price transparency,
3. Lower credit supply,
4. Loan approval rates for subprime borrowers,
5. Lower number of financial institutions and reduced density, and
6. Adverse impacts on bank and institution profitability.

If the CDFI Fund continues to promulgate the argument that lending above a 36% MAPR is bad for the consumer, hard-working Americans could be steered away from access to safe and reliable credit that best fits their needs.

B. The MAPR obscures the true cost of credit and undermines the underlying purpose of TILA.

The concept of "All-In APR" (also known as "Military APR") expands the Truth in Lending Act (TILA) definition of Annual Percentage Rate (APR), to cover the cost of optional protection products that are unrelated to the cost of credit. When the novel definition of "All-In APR" is used for rate cap purposes, it has an exclusionary effect. It exacerbates financial inequalities by

[6] https://www.federalreserve.gov/publications/files/2023-report-economic-well-being-us-households-202405.pdf
[7] https://www.fdic.gov/household-survey
[8] https://www.federalreserve.gov/econres/notes/feds-notes/the-cost-structure-of-consumer-finance-companies-and-its-implications-for-interest-rates-20200812.html
[9] Ferrari, Aurora and Masetti, Oliver and Ren, Jiemin, Interest Rate Caps: The Theory and the Practice (April 3, 2018). World Bank Policy Research Working Paper No. 8398, Available at SSRN: https://ssrn.com/abstract=3155971

severely restricting the ability of higher-risk borrowers to access safe, affordable credit, without significantly affecting the better-off.

AFSA believes that the desire to attach the cost of optional protection products to the APR rate carried by a loan stems from outdated understanding of the nature of these products, which are an invaluable enhancement to the financial capability of those that choose them.

- AFSA members offer insurance and other non-loan financial services that are entirely voluntary for our customers.
- Loan terms and conditions are offered without regard to whether credit insurance is purchased; it makes no sense, therefore, to consider the cost of non-loan products to be an additional finance charge.
- AFSA members' optional protection products complement their loans, helping customers build financial stability, security, and resilience.
- Credit insurance is accessible, affordable, and popular with customers, who understand that it plays an important role in limiting their exposure to financial risk and the consequences of financial shock, including during the COVID-19 pandemic.

APR is a defined and well-understood term that has been the gold standard for comparing like credit products for decades. It is a useful tool for comparing like credit transactions by setting a single standard to determine the cost of credit in each proposed transaction. It was not intended to be (and is useless as) a tool to measure credit transactions that also include voluntary protection products that the consumer may choose to purchase.

TILA requires that creditors disclose not only APR, but also Amount Financed (the size or quantity of the credit product), Finance Charge (the absolute dollar cost of the credit) and the Total of Payments (the cash flow that will be required to service the credit over its stated life). The only way to make a valid comparison, and thereby make an informed choice, when making a loan or obtaining products on credit is to look at all four of these elements and determine which credit proposal what product is right for the individual consumer and the consumer's unique circumstances.

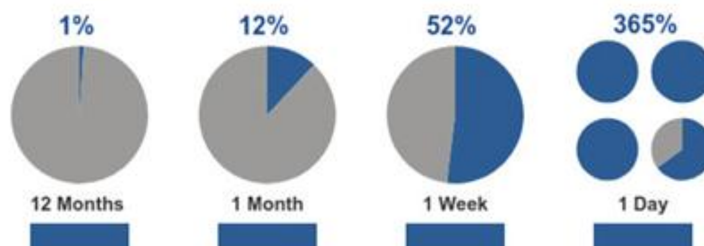
Why APR Can Be Misleading When Evaluating Loans

APR is a great tool to compare products of like terms and amounts, such as two credit card offers, or two 30-year mortgages, but it is a mathematical tool that has value only as a comparator.

What does APR really measure, cost or time?

Let's say you borrow $100 and agree to pay $1 interest. Seems fair, right?

What is the APR of the agreed upon $1 interest charge?



While the cost of credit remains exactly the same ($1.00), the APR varies dramatically based on the duration (or term) of the loan. Thus, APR cannot be relied upon as an indicator of loan affordability.

Because APR is valid only for comparing comparable credit transactions and relates ***only*** to the cost of the credit, APR has never been associated with the cost of goods, services, or insurance. This is why, in TILA, the cost of voluntary ancillary products like credit insurance are ***expressly excluded from the finance charge*** if the creditor provides the consumer with certain written disclosures, and hence, excluded from the APR. Calling 36% MAPR loans "prohibited" does not explain to the consumer what the true cost of the credit is and could steer consumers away from loans that include the option to purchase voluntary products that an individual can choose if they want or not.

The "prohibited practices" definition of "high-rate loans" does not explain what is included in the calculation of the MAPR. Imagine what would happen if TILA-type disclosures were required to be disclosed as a measure of the cost of other financial transactions or everyday consumer items. The results would be alarming for sure, but as just with traditional installment loans, misleading as to true cost. Consider these common examples:

EXAMPLE A: **Converting coins using a** **supermarket change machine*** Amount in coins: $100 Fee: 8.9% Fee Calculated as APR: **3,248.5%**	**EXAMPLE B:** **Cost of a bounced check*** Amount of check: $100 NSF Fee: $30 NSF charge calculated as APR: **10,950%**
EXAMPLE C: **Using an out-of-network ATM*** Typical withdrawal: $40 Fee for out-of-network ATM use: $2.50 Fee calculated as APR: 2,281%	**EXAMPLE D: Borrowing $100 from a friend and paying her back $101 the next day** Fee paid to friend: $1 Fee calculated as APR: **365%**
EXAMPLE E: Parking Ticket (Meter Violation)* Amount of Ticket: $25 Fee for late payment: $10 Fee calculated as APR: 14,600%	**EXAMPLE F: IRS Late Fee (1%)*** Taxes Owed: $800 Fee for late payment: $8.00 Fee calculated as APR: **365%**

** Note: Prices/fees provided are estimated. Calculations are based on an assumption of a one-day loan.*

Based on the SDL application language, even the Internal Revenue Service, the largest bureau of the Treasury, provides purportedly prohibited services. Stoking linguistic distrust based off of mathematical manipulation should not be the purpose of the SDL application. “High-Rate loans” should be removed from the list of prohibited practices as it does not provide the full picture of what is included in the price of the loan.

C. Conclusion.

We appreciate the CDFI and Treasury’s mission to ensure that SDLP applicants engage in fair lending practices. The criteria for measuring whether an applicant is engaging in responsible lending practices should not be whether the applicant lends above a 36% MAPR, but: whether it offers transparent, fully amortized loans that are repaid in substantially equal payments. The removal of the prohibition against purported high-rate loans would help continue to foster diversity of types, activities and geography; support the growth and reach of CDFIs; protect the CDFI brand; minimize burden on CDFIs; and promote efficiency. We encourage the Treasury Department and CDFI Fund to amend its application. Please contact me at cwinslow@afsamail.org or (202) 776-7300 with any questions or to set up a meeting.

Sincerely,

Celia Winslow
President-elect
American Financial Services Association