PEW'S SMALL-DOLLAR LENDING MODEL:
A SURE WAY TO ELIMINATE A VALUED CREDIT OPTION

The Pew Charitable Trusts attempts to appear interested in preserving consumers' access to credit in one state after the next. In reality, Pew has opted to disregard and ignore the very rational reasons consumers choose short-term, small-dollar "payday" loans from regulated consumer financial services providers and their overwhelming satisfaction with those services. Instead, they push a small-dollar lending regulatory model that dramatically limits and effectively eliminates consumers' credit options, with little concern for the consequences.

Pew's small-dollar lending proposal is not a model for states interested in preserving access to credit and advancing financial security; rather, it produces the exact opposite effect, endangering consumers' ability to obtain credit when they need it most.

The Pew Model for Credit Restriction

Pew, unlike most other opponents to non-bank consumer financial services, openly acknowledges that an interest rate cap on small-dollar loans – typically 36 percent – amounts to an effective ban on the service:

> "Restrictive states either do not permit payday lending or have price caps low enough to eliminate payday lending in the state. This rate cap often is 36 percent APR." – *"Payday Lending in America: Who Borrows, Where They Borrow, and Why," July 2012*
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> "Our research indicates a 36 percent interest rate and $20 application fee will be inadequate to support a robust small-loan program in a safe and sound manner." – *Nick Bourke, Pew Charitable Trusts, Comment to CFPB's Notice of Proposed Rulemaking on the Payday Alternative Loan Program, RIN 3133-AE84, August 3, 2018*

Instead, Pew proposes a model that it claims is viable for lenders and borrowers alike, but ultimately has the same detrimental consequences for consumers. It calls for replacing the traditional two-to-four-week small-dollar loan with a mandatory longer-term, small-dollar, multi-payment loan.

The Pew small-dollar, multi-payment model is not the result of consumer demand, the study of consumers' credit needs and borrowing habits, or consultation with policymakers who have spent decades debating and regulating consumer credit. It is not even a response to widespread consumer complaints about regulated consumer financial services providers, which remain low in state after state and nationally. Rather, it is the product of activists who have never needed to borrow a short-term, small-dollar loan, yet are ideologically opposed to others doing so. Such regulations constrict broad access to credit, imposing a confusing, one-size-fits-all approach with arbitrary restrictions that fails to consider consumers' varying needs and preferences and denies them the ability to choose the product that works for their personal financial situation.

Far from Fair, Workable, or Replicable

Pew's model, originally based on the regulatory framework enacted in Colorado over a decade ago, did not work in Colorado and has since proven to be unworkable elsewhere, leaving consumers without regulated credit options. As the following case studies demonstrate, such an untested regulatory approach has costs and negative consequences for Americans who need credit. This model consistently decimates regulated short-term, small-dollar lending and eliminates consumer choice – in direct contradiction to Pew's promises to preserve regulated small-dollar credit. **Pew's model succeeds only in the sense that it devastates consumers' financial options and forces them to inferior, riskier choices everywhere it is implemented.**

- **Colorado:** In 2010, Colorado eliminated two-week loans and mandated only longer-term installment loans, resulting in the closure of roughly half of the state's lenders. As a result, a leading lender in the state reported that more than a quarter of customers were paying their six-month loans off within the first 59 days, in order to re-borrow and avoid incurring monthly maintenance fees. The state's adoption of a 36 percent rate cap in 2019 further consolidated the number of regulated lenders in the state.

- **Ohio:** In 2019, Ohio implemented a new law eliminating two-week loans in favor of mandatory installment loans with a 28 percent interest rate cap. In the first six months after this restrictive lending law went into effect, the number of regulated lenders operating with licenses in the state dropped from 161 at the end of 2018 to only 30. Within the first year, many lenders were closing or consolidating their storefronts; one leading lender closed over 40 percent of its locations in that time, followed by additional closures. Further, anecdotal reports suggest that in the absence of regulated options, many Ohio consumers in need of small-dollar credit are turning to unlicensed, unregulated lenders online. These lenders evade state and federal laws, with higher costs and none of the consumer protections that regulated operators provide.

- **Virginia:** In 2020, the Commonwealth passed a mandatory longer term for small-dollar loans on top of existing state regulations, including an interest rate cap. As a result, many of Virginia's regulated consumer lenders closed their doors ahead of the law's January 2021 effective date, leaving residents with fewer regulated options amid the COVID-19 pandemic.

Strange Bedfellows Do Not Preserve Broad Access to Credit

In some states, Pew has aligned itself with subprime installment lenders to give the appearance that their model is workable and won't devastate consumers' credit options. But the fact is that, oftentimes, these installment loan providers have limited to no operations in the state to begin with; their only goal is to eliminate the existing competition with the intention of exploiting the resulting market void. These providers do not share consumer financial services providers' commitment to their consumers or their investment in the communities they serve.

Further, while these lenders claim they can operate under Pew's model or an interest rate cap, they typically do not provide broad access to credit, instead serving only a narrow band of subprime borrowers – those with credit scores between 610 and 640, whereas the average credit score for a person in need of non-bank credit is 579. If they can offer an equal or superior product for a lower cost in the existing competitive marketplace, consumers will choose them. However, it seems unlikely they are capable of meeting consumers' credit needs at the scale necessary for promoting widespread financial inclusion and stability.