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No Loan For You, Too!

The Unintended Consequences of Price Controls on Consumer Access to Credit

D. Dowd Muska, Patrick M. Brenner,
Jack Radomski & Brandt Kringlie

In the end, we will remember not the words of our enemies, but the silence of our friends.

– Martin Luther King, Jr.

This paper, in its entirety, can be found at **https://southwestpolicy.com/sppi04**

855.411.7774 | southwestpolicy.com | info@southwestpolicy.com
PO Box 1746 | Bernalillo, New Mexico 87004

Southwest Public Policy Institute | *Better living through better policy*

SOUTHWEST PUBLIC POLICY INSTITUTE

The Southwest Public Policy Institute (SPPI) is a research institute built to explore and build on sound, data-driven policies regarding education, crime, and economics that will encourage positive change in the American Southwest.

Many think tanks have fallen victim to the mentality of communicating only to the echo chamber: they only target individuals that agree with partisan messaging. SPPI's approach enables us to reach new audiences by micro-targeting constituents on issues like finance, energy, education, or public safety.

With SPPI's data-first approach and the inclusion of every state in the American Southwest in our efforts, there is tremendous potential for reinvigorating traditional American values with one motto: WE AGREE. By removing the stigma from conversations with constituents and addressing issues with solutions to solve problems, we truly believe that we can help move the American Southwest in a positive direction and set an example for the entire region to follow.

Our focus includes fostering innovative policy alternatives at the regional, state, and community levels to enhance individual initiative and entrepreneurship, broadening the role of volunteerism in confronting public problems and the sense of community among the public, government, and business.

The division in America comes from the unwillingness to communicate with one another and to discuss the problems and the issues in front of us. By working together, exchanging ideas, and bringing solutions to problems we face, we can accomplish what public servants are meant to do: deliver ***better living through better policy***.

INTRODUCTION

The Southwest Public Policy Institute continues its ongoing probe of short-term, small-dollar lending. While the industry's products are regularly derided as "payday loans" and erroneously referred to as "predatory" by politicians, ideologues, and activists on both the left and the right, our research – building on the work of many others – offers a compelling counterweight to the one-sided narrative that dominates discussions. Herewith, we present the first update to the March 2023 policy investigation *No Loan For You!*[1]

As state and federal authorities grapple with usury and interest rate cap limitations due to advancements in financial technology, some states like New Mexico and Illinois are implementing solutions that exacerbate the issues they aim to address. We know that "well-intentioned interest rate caps can lead to less credit availability."[2] The "solution" is spreading, with South Carolina attempting passage of similar price control legislation this year.

Three months ago, the Institute exposed the challenges faced by unbanked and underbanked borrowers in New Mexico, where a significant "reform" of short-term, small-dollar lending became law on January 1, 2023. Our investigation cut a new path in the state, with a "secret shopper" experiment originally focused on banks. Now, we include credit unions. In addition, we extend our inquiry of traditional banks to a new state, far from the Land of Enchantment in more ways than one. We begin with our latest results, from Minnesota.

IT'S NOT JUST THE WEATHER

The project commenced in New Mexico, and we believe that one of the best ways to examine our findings there is to test our results in a very different state. So we picked Minnesota.

On the surface, the Land of Enchantment and the Gopher State have obvious differences, from temperature to international borders to time zones. But the greatest distinctions are found when one scrutinizes socioeconomic factors.

For the 2019-20 school year, the portion of "public school 9th-graders who graduate within 4 years of starting 9th grade with a regular diploma or, for students with the most significant cognitive disabilities, a state-defined alternate high school diploma" in New Mexico is 77 percent – tied with Arizona for the worst mark in the nation. Minnesota's share was 84 percent.[3] New Mexico's violent-crime rate is three and a half times worse than Minnesota's.[4] There is not a dramatic disparity in the cost of living, median household income in the Gopher State is an impressive 43.8 percent higher.[5] At 56.8 percent in April, New Mexico has one of the lowest labor force participation rates in America. Minnesota, at 68.1 percent, had one of the highest.[6] The supplemental poverty rate – a figure that "extends the official poverty measure by taking account of many of the government programs designed to assist low-income families and individuals that are not included in the official poverty measure" – is 10.6 percent in New Mexico; in Minnesota, it is 5.1 percent.[7]

According to the U.S. Census Bureau, the share of the New Mexico population that is "Hispanic or Latino" is 50.1 percent, vs. 5.8 for Minnesota. The "American Indian and Alaska Native alone" cohort is 11.2 percent in New Mexico; in Minnesota, 1.4 percent. At 2.7%, the share of New Mexicans who are "Black or African American alone" is well under half the comparable figure for Minnesotans at 7.4%.[8] Clearly, the states are about as different as they possibly could be.

Differences aside, states across the country are facing down an oncoming gale.

YOU DON'T KNOW JACK (OR BRANDT)

Jack Radomski and Brandt Kringlie are undergraduates at the University of Minnesota. Like many college students, "well-qualified borrower" describes neither young man. Often burdened with education debt, limited work experience,

low incomes from part-time jobs and/or student aid, and a lack of well-established credit history, young adults pursuing higher education are not desirable customers for most lenders.

But it's easy to envision scenarios in which Jack, Brandt, and their fellow students face financial crises – urgent automobile repairs, for example, or the need for unplanned travel due to an illness in the family. When bad luck strikes, what are their options?

For the Institute, Jack and Brandt attempted to secure short-term, small-dollar loans from various banks in the Minneapolis-Saint Paul metropolitan area. Both students visited four major lenders: U.S. Bank, Wells Fargo, Bank of America, and Huntington Bank. Both encountered difficulties and were ultimately unable to obtain the loans advertised by all four banks.

Jack's experience began at U.S. Bank, where he successfully opened a checking account but was deemed ineligible for a short-term, small-dollar loan due to his new-account status. At Wells Fargo, he faced challenges finding the Flex Loan option both on the website and app, leading to his inability to apply for it. Bank of America's Balance Assist loan also eluded Jack, as he was informed he would receive an email with further details, but no immediate approval was granted. Finally, at Huntington Bank, he discovered that he was not eligible for the Standby Cash program based on the absence of the option in his account's "Hub" section.

Similarly, Brandt's efforts were unsuccessful. At U.S. Bank, he encountered the most helpful assistance – but was ultimately denied a Simple Loan due to specific qualifications, such as the required length of account ownership and a sufficient number of direct deposits. Wells Fargo's Flex Loan remained elusive to Brandt as he couldn't find the loan option on the website and concluded that he did not meet the eligibility criteria.

Huntington Bank's Standby Cash Program was also unattainable for Brandt, as he couldn't locate the application option on his account and the bank's help tool proved unhelpful. Lastly, Bank of America's Balance Assist loan required a checking account duration of over a year, making Brandt ineligible despite successfully opening an account.

Both Jack and Brandt found jarring inconsistencies between the banks' advertisements and the actual requirements for accessing emergency loans. Their experiences mirrored that of Patrick Brenner, who failed to secure approval of a

short-term, small-dollar loan at U.S. Bank, Wells Fargo, and Bank of America in the Albuquerque metro area.

Meanwhile, Patrick is still incurring monthly checking account maintenance fees from Bank of America, U.S. Bank, and Wells Fargo as he waits to establish a 12-month checking account history with those banks as the prerequisite for their emergency credit products. Those twelve months will result in incurred fees of $83.40 from U.S. Bank, $59.40 from Bank of America, and $129.12 from Wells Fargo. None of these fees will be included in the total cost of the sub-36% short-term loan, an unfair advantage leveraged by the banks to include margin-padding fees in ancillary products.

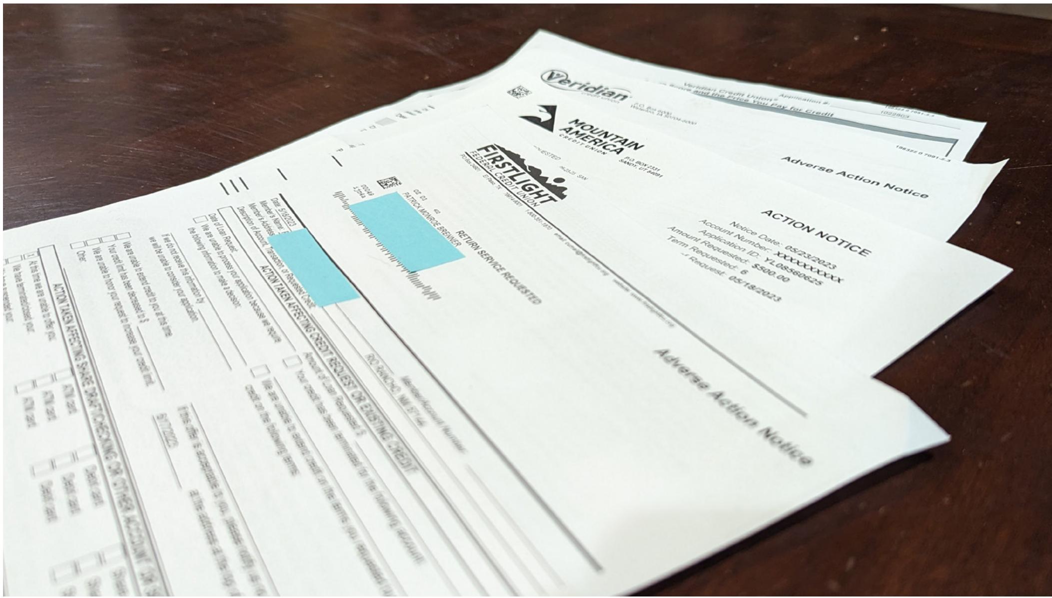
But unlike Jack and Brandt, Patrick is a married father of three with a mortgage, a full-time job, and a lengthy credit history. Thwarted by three major banks, he moved on to over a dozen local credit unions.

MEMBERS ONLY

According to the National Credit Union Administration, a payday alternative loan (PAL) "is a free-market solution that responds to the need for small-dollar lending in the marketplace." PALs, the government bureaucracy claims, "can make a difference by helping borrowers build or repair credit records, allowing them to graduate to other mainstream financial products," encouraging "responsible lending that allows consumers to address immediate needs while working towards fuller financial inclusion."[9]

Over the course of three weeks, Patrick applied for a PAL from Guadalupe Credit Union, Otero Federal Credit Union, U-1st Community Federal Credit Union, Four Corners Credit Union, Everyone's Federal Credit Union, Internationalites Federal Credit Union, FirstLight Federal Credit Union, American Southwest Credit Union, Mountain America Credit Union, Del Norte Credit Union, Veridian Credit Union, U.S. Eagle Federal Credit Union, and Nusenda Credit Union. He's also an existing member of Navy Federal Credit Union and Pentagon Federal Credit Union, where membership is restricted to military personnel and their families.

Finding credit unions that offered PALs was burdensome. The results were disappointing. Patrick was successful only twice. U.S. Eagle Credit Union granted conditional approval pending established membership. Patrick was already a member at the other, Nusenda, with an auto loan in good standing for about 12



Patrick's adverse action notices from the credit unions pile up.

months at the time of his application.

Thirteen of the 15 credit unions – 86 percent – denied Patrick's loan application, do not offer a PAL, or denied his membership application. For Del Norte Credit Union, the denial occurred in a branch. When prompted for access to the PAL criteria, the banker was informed by a manager that the document was for "internal use only" but required existing membership for a considerable length of time and a corresponding checking account. Veridian Credit Union supplied an adverse action notice, citing "credit application incomplete" as the principal reason for denial. But the online application form for Veridian did not allow submission unless requisite form fields were completed, making the "credit application incomplete" result something of a mystery.

First Light Federal Credit Union sent an adverse action notice, citing "you are not eligible for membership in this credit union" as the principal reason for credit denial. Mountain America Credit Union's Adverse Action Notice spelled out a similar reason for denial: "credit application incomplete", and we surmise that the reason the applications are marked as incomplete is that Patrick was not an existing member of the credit union at the time the application was submitted. But it's anyone's guess.

American Southwest Credit Union (ASCU) only recognized that the application was transmitted: "Thank you for your application. A loan officer will need to review your application and contact you with any questions." That was the last correspondence Patrick received from ASCU, which was the same day he applied: May 18, 2023. Guadalupe Credit Union (GCU) responded similarly: "One of our

loan officers will be in contact once your application has been reviewed." GCU was never heard from again.

Internationalites Federal Credit Union used membership criteria to exclude Patrick from loan options. "[M]embership is not open to the general public. Membership is only open to employees of the City of Carlsbad, Mosaic Potash Carlsbad Inc., Intrepid Potash and family members listed below." Everyone's Credit Union featured a less-than-stellar consumer experience: "You have followed an outdated link. Please return to https://www.everyonesfcu.com/ for home banking access."

The only bright, shining example was Nusenda. The application process was simple, transparent, and accessible. The rate was 17%. Repayment would occur in three payments over 90 days. Upon agreeing to the note and submitting the application, the loan funds were immediately available in Patrick's Nusenda savings account. It was a streamlined and hassle-free process.

But Nusenda was the exception to the rule.

And Patrick is also the exception to the rule: he's not unbanked or underbanked and was already a member at Nusenda for over a year, the only credit union where he definitively obtained a specialized emergency loan.

At the outset, he was by all measures both a well-qualified borrower and a customer of traditional banking. Yet he stands in stark contrast to the general population: in New Mexico's largest city, "**a third of the households** … do little or no mainstream banking, substantially higher than the national average."[10] So what if "six of the eight largest banks now offer affordable small loans"?[11] One of every three families in Albuquerque doesn't use any bank at all.

So when Pew Charitable Trusts says "All payday loan borrowers are already bank or credit union customers with checking accounts," it's clear that they have rejected reality and substituted their own. But Pew also asked a great question: "What would consumers do if payday loans went away?"[12] Their answer was dismally disappointing: "Choose other options such as asking friends".

Who are the actual borrowers? This is one of the most important questions of which to be cognizant when considering consumer access to specialized emergency credit. Policymakers are forgetting this.

THE PERFECT STORM

Americans currently hold over $1 trillion in credit card debt, with the average interest rate on new cards reaching 24 percent, the highest since the Reagan era. The typical American household carries around $10,000 in credit card debt. Paying off this debt is challenging, with a monthly payment of $250 and 24 percent interest, taking until 2030 to repay and costing a total of $20,318, assuming the card is not used again. The nation's credit card debt has increased by $250 billion in two years, reaching $986 billion according to the Federal Reserve, although some estimates put it at $1.2 trillion.[13]

The pandemic initially led to a decrease in credit card balances, but spending has since increased, and the Federal Reserve has raised interest rates. Simultaneously, Americans have been depleting the savings that they accumulated during the pandemic as high prices and the end of relief programs have taken a toll on their finances. According to estimates from Goldman Sachs, Americans have already spent about 35% of the extra savings they acquired during the pandemic, and it is projected that by the end of the year, approximately 65% of that money will be exhausted.

In 2020 and 2021, government stimulus and reduced spending allowed households to accumulate $2.7 trillion in extra savings, but the reversal of these factors, along with soaring inflation, has led to the depletion of savings for many households. As a result, people are cutting back on spending and relying on credit cards, while also tapping into their savings to stay afloat. Economists expect that the saving rate will rise modestly by the end of the year but emphasize the circumstances that caused the depletion of savings are unlikely to repeat. Lower-income households have been hit hardest, with their savings being depleted at a faster rate than higher-income households.[14]

SHATTERING THE SPIN

The Pew Charitable Trusts, the Center for Responsible Lending (CRL), the National Community Reinvestment Coalition (NCRC), and the National Consumer Law Center (NCLC) have all presented a narrative that misrepresents the nature and impact of alternative financial institutions. These organizations seem intent on gaslighting specialized emergency lenders and distorting the reality of consumer lending options. It is important to address these misconceptions and exemplify the crucial role that alternative lenders play in meeting the credit needs

of individuals facing financial challenges.

When all else fails, manipulate the data. And that's exactly what they're doing.

Pew's assertion that credit unions are providing small-dollar loans to more consumers than ever before is either based on a fundamental misunderstanding of the data or a compromising desire for it to be successful. Loan volume increased, but the number of loans issued by credit unions actually decreased by 7.3% in 2022 compared to 2019. The increase in loan volume was due to the average loan amount rising from $700 to $1,000.[15] Admittedly, this would allow credit unions to generate more revenue on the loan. The real question is, are credit unions *actually* fulfilling their missions as claimed in the Pew narrative?

While many credit unions have offered low-cost, small-dollar loans in the past, members often chose other options due to the inconvenience, like in Patrick's experience, of in-person applications and uncertainty about eligibility and loan timing. Despite the increase in small-dollar lending by credit unions and the record volume achieved, only a limited number of credit unions currently offer automated small installment loans or lines of credit.

In "pursuit of their mission", twelve credit unions have been piling on the adverse action notices, and it has taken its toll on Patrick's credit. Before undertaking this investigation, Patrick's credit score was over 800. As of June 9, it's 706. While the banks used alternative approval criteria for their short-term loan applications, the credit unions all subjected Patrick to hard credit inquiries, an effect that will last two years.

The very people intended to be beneficiaries of the "protection" of interest rate caps have been left without access to credit previously relied on. These consumers are well-informed and often prefer the specialized financial products offered by alternative lenders. Rather than conveying the bigotry of low expectations, these consumers should be trusted with their own decisions.

CONCLUSION

A consumer credit crisis is looming: inflation is up, there are no more loans, there are no more savings. With an uncertain economic future, access to both specialized emergency credit and liquidity, in general, is more important now than ever before. Rather than inhibiting access to nontraditional credit options

that activists simply don't understand, the primary objective should be to expand choices for middle- and low-income families.

Patrick, Brandt, and Jack have been met with frustration as they challenged themselves to capture a specialized emergency loan offered by ill-suited traditional financial institutions so often touted by anti-“predatory” credit alarmists. While P., B., and J. don't actually need the loans, millions of other consumers do. Instead of borrowers being met with the product they know and want, the cancerous spread of rate caps and price controls has led to the only possible outcome: no loan for you, and no loan for you, too.

NOTES

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