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# The Wrong Kicks on Route 36

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Members of Congress in the House and Senate recently introduced versions of the "Veterans and Consumers Fair Credit Act," designed to extend to all consumers the interest rate caps currently in place for active-duty service members and dependents. This proposed legislation is modeled after the 2015 update to the 2007 Military Lending Act (MLA), and mandates a nationwide 36 percent interest rate cap on consumer credit.

Supporters of a 36 percent interest rate cap compare it to a "speed limit on small-dollar loans." Not so. It is an abrupt "pavement ends" sign for millions of Americans. As with all price controls, interest rate caps have predictable outcomes. Interest rate caps create shortages and make credit less available for millions of families.

Small-dollar credit products serve millions of people. According to the FDIC, nearly 33 million families have no or only limited access to bank credit. A recent study by the Federal Reserve Bank of New York suggests millions more may be "credit insecure." That is, they tend to max out their credit limit, have a low credit score, and have a history of late payments. Also, 45 million primarily young, low-income, and minority Americans have poor or thin credit histories. They are ineligible for prime credit cards and bank loans.

A primary function of credit is to smooth consumption. More than a third of households making under $50,000 experience month-to-month spikes and dips in their income. Small-dollar credit products help them deal with unforeseen expenses. The choice for these consumers is between using small-dollar credit products and simply going without.

In theory, how would a 36 percent interest rate cap eliminate consumer choices? It costs money to produce small-dollar loans. Reducing revenue too much makes loans unprofitable, and lenders will obviously not supply unprofitable loans. This includes installment loans, payday loans, and even pawn shops. Borrowers' option to use small-dollar credit products is not outlawed, but there is no supply for payday and pawn loans, and no amounts available lower than $4,000 for traditional installment loans at those rates.

A 36 percent cap on payday loans for active military, their spouses, and dependents has been in place since the MLA passed in 2007. Its proponents argued at the time that payday lenders near military bases were taking advantage of inexperienced borrowers in uniform, causing them financial distress which compromised their performance. The MLA banned payday loans for military members on those grounds. In 2015, the MLA cap was extended to all forms of credit, including pawn loans — which had been exempt in the 2007 Act.

More than ten years later, though, evidence has accumulated that the MLA has had no benefit and might even hurt those it was intended to help. For example, in 2017, researchers found that access to payday loans did not increase bad outcomes, such as involuntary separations and the denial of security clearances as a result of financial distress. Their analysis “suggests no significant benefits to servicemembers from the MLA.” A 2016 study showed access to payday loans made it easier for military personnel to buy food and other goods before their biweekly paycheck.

If the MLA has not helped service members, why extend it? The MLA is a cautionary tale — not a model — for consumer credit regulation. It seems ripe for repeal, not ready to extend to all consumers.

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