Consumers' Research
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DEFENDING CONSUMERS

March 20, 2025

The Honorable Lyman Hoffman
Co-Chair
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable Bert Stedman
Co-Chair
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable Donny Olson
Co-Chair
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable Jesse Kiehl
Co-Chair
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable Kelly Merrick
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable James Kaufman
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

The Honorable Mike Cronk
Senate Finance Committee
Alaska State Senate
Juneau, AK 99801

Dear Co-Chair Hoffman, Co-Chair Stedman, Co-Chair Olson, Co-Chair Kiehl, Senator Merrick, Senator Kaufman, and Senator Cronk:

Alaska legislators are considering SB 39, a bill that adds new restrictions to consumer lending, including the imposition of an all-in 36 percent interest rate cap. The measure would mean that lenders would be prohibited from offering loans, regardless of their length or the risk posed by the borrower, with a rate above 36 percent, including fees, which the law interprets as adding to the financing cost.

Lawmakers have proposed similar bills that simply run afoul of the research. About three years ago, Illinois lawmakers presumably thought they were helping borrowers by limiting the all-in rates lenders could charge as well. But did they? Did this rate cap improve consumer welfare and protect the underprivileged from so-called predatory lenders? And, importantly, did this rate cap make small-dollar loans more affordable?

Working with a fellow academic (Brandon Bolen) and an economist from the Federal Reserve (Greg Elliehausen), we addressed these questions and other findings in a recent study. In that study, we documented the measurable effects on Illinois borrowers after the 36 percent all-in rate cap went into effect.

We examined the number and size of unsecured installment loans over a twelve-month period—six months before the imposition of the all-in cap and six months after. We sorted credit bureau data into credit score buckets by county or county groups for Illinois and Missouri, which we chose as a comparison state because it had no legislated rate cap. In Missouri, the competitive market sets borrowing rates.

Basic economic theory predicts that interest rate caps have effects that differ across groups of borrowers. A rate cap will affect borrowers with poor credit differently than those with a strong credit history. In our study, we found that the all-in 36 percent rate cap impacted subprime borrowers, those with credit scores below 600, most significantly.

Using widely accepted, well-known statistical techniques, we estimated how the number of loans made after the cap was imposed and compared it to an estimated number of loans that would have been made without the cap. According to our model, in the period following the imposition of the 36 percent cap, the number of loans to subprime borrowers fell by 38 percent. Meanwhile, the average loan size increased by 35 percent from where it would have been without the cap.

Additionally, we estimated that the total dollars loaned to subprime borrowers fell about 14 percent, or about $26 million. The deepest subprime borrowers, those with the fewest credit alternatives, were the most affected: the dollars lent to them fell by about 26 percent. This amount may sound trivial to some; however, this amount of money is significant to the Illinois families denied access to credit. We estimated that roughly 34,000 Illinois families now have even fewer credit options because they lost access to unsecured installment loans.

We also examined the results of a survey of actual installment loan borrowers in Illinois who lost access to credit after the 36 percent rate cap imposition. Ninety-three percent of the respondents said their pre-cap loans helped them manage their financial situation. Seventy-nine percent of borrowers surveyed responded that they would like the option to return to their previous lender operating under pre-cap conditions.

The proponents of an all-in 36 percent rate cap may all think they are doing a great thing for working families, but their good intentions stand in stark contrast to the cold facts observed when rate caps like the one they propose, have been imposed. Legislators claim they care about consumers who are struggling financially, but if their struggles lead them to miss payments and pay bills late, the result is a lower credit score, further limiting their access to credit. Such was the case when Illinois instituted its version of Alaska's proposed rate cap, which harmed Illinois borrowers with low credit scores while providing additional credit access to borrowers with

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higher credit scores.

I urge you to study the actual impacts of imposing this rate cap and I urge you to look for other ways to measure the cost of short-term loans before you move forward. Imposing an interest rate cap has actual effects that differ from the intentions of lawmakers. A 36% all-in interest rate cap is especially harmful to the very consumers the law is intended to protect.

For example, a one-year, $1,000 installment loan at a 36% all-in rate has a monthly payment of about $100. Thus, the lender receives $200 on the $1,000 principal, i.e., not $360. If the rate is doubled to 72%, the payment increases to about $120 month, or about $5 more per week. In this case, the lender receives about $440 on the $1,000 principal. Rates like 36% and 72% sound jarring, but I urge you to think in terms of dollar amounts paid for the loan.

Suppose an Alaskan has a need for a $1,00 loan. Installment lenders will likely not make $1,000 loans under a 36% all-in cap. The $200 received on this repaid loan is not enough revenue to cover operating costs as well as the cost of loans that are not repaid. The net effect is that the cap will legislate $1,000, and smaller, loans out of existence. Some Alaskans will lose access to installment credit, but they still need credit. Where will they go?

Sincerely,

Tom Miller Jr., PhD
Professor of Finance and *Jack R. Lee*
Chair in Financial Institutions and Consumer Finance
Mississippi State University College of Business
Senior Research Fellow
Consumers' Research

Cc:

The Honorable Cathy Giessel, Majority Leader, Alaska State Senate
The Honorable Gary Stevens, President, Alaska State Senate
The Honorable Mike Shower, Minority Leader, Alaska State Senate

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