LARGER LOANS NEED LOWER RATES

A 50-STATE SURVEY OF THE APRS ALLOWED FOR A $10,000 LOAN

National Consumer Law Center
Fighting Together for Economic Justice

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Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services; and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state governments and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness.

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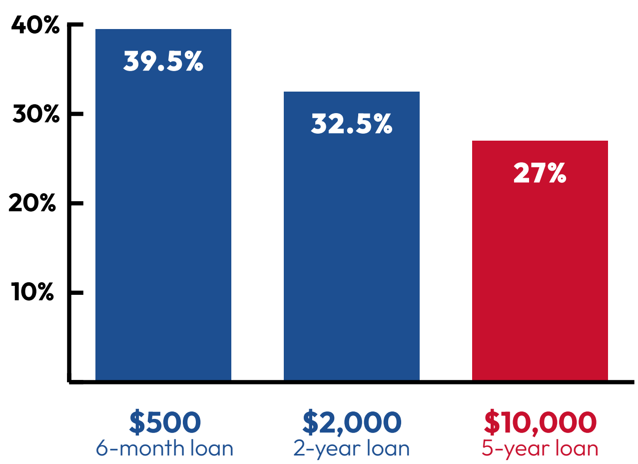
INTRODUCTION

Everything that is wrong with a high-cost loan is only made worse when the loan is larger and longer. A larger, longer high-cost loan can be a deeper, longer debt trap than a payday loan.

Interest rate caps are therefore just as important, and indeed more so, for larger, longer loans as for small dollar loans. And, since the borrower will pay the interest on a larger amount over a longer period of time, the rate cap should be substantially *lower* than the cap for a smaller, short-term loan. An interest rate that is reasonable for a small loan can lead to explosive and unaffordable interest on a larger loan.

While 36% has become the widely accepted metric for an affordable small dollar loan,[1] most states understandably do not permit that rate for larger loans. The great majority of states cap the interest rate and fees for a five-year $10,000 loan, and in these states the median cap is an Annual Percentage Rate (APR) of 27%. By contrast, the median is 39.5% for a 6-month $500 loan and 32% for a 2-year $2,000 loan. But even 27% is a high rate, especially for larger loans, and 20 states plus the District of Columbia impose lower rate caps on a $10,000 loan.



This report surveys the interest rates and loan fees allowed by all 50 states and the District of Columbia for an unsecured 5-year installment loan of $10,000. It updates our 2018 report, *A Larger and Longer Debt Trap? Analysis of States' APR Caps for a $10,000 Five-Year Installment Loan*.[2] Our APR calculations include all the costs that the borrower may be required to pay to obtain and use the extension of credit, including application fees, investigation fees, document preparation fees, transaction fees, "points," annual fees, and monthly fees. The appendix to this report details our methodology. More detail about high-cost installment lending can be found in other reports in this series.[3]

WHY APRS FOR LARGER LOANS SHOULD BE CAPPED WELL BELOW 36%

Lower interest rates are important for larger loans for several reasons. The rate is applied against a larger amount, generating more interest. Larger loans tend to have longer terms, and thus interest accumulates over a longer period of time. In addition, high payments are harder to sustain over a longer period of time, so the borrower is more likely to experience income or expense shocks during the loan term. As a result, affordability becomes more problematic than for the same payment over a shorter time period.

While a 36% cap is better than no cap or an even higher cap, it is still too high for a loan of this size and length. It means that a borrower who repays a $10,000 loan over five years will pay more than *double* the amount borrowed—the $10,000 principal plus $11,680 in interest.

Raising the APR from 20.5% to 36% on a 5-year $25,000 loan adds $14,076 in interest.

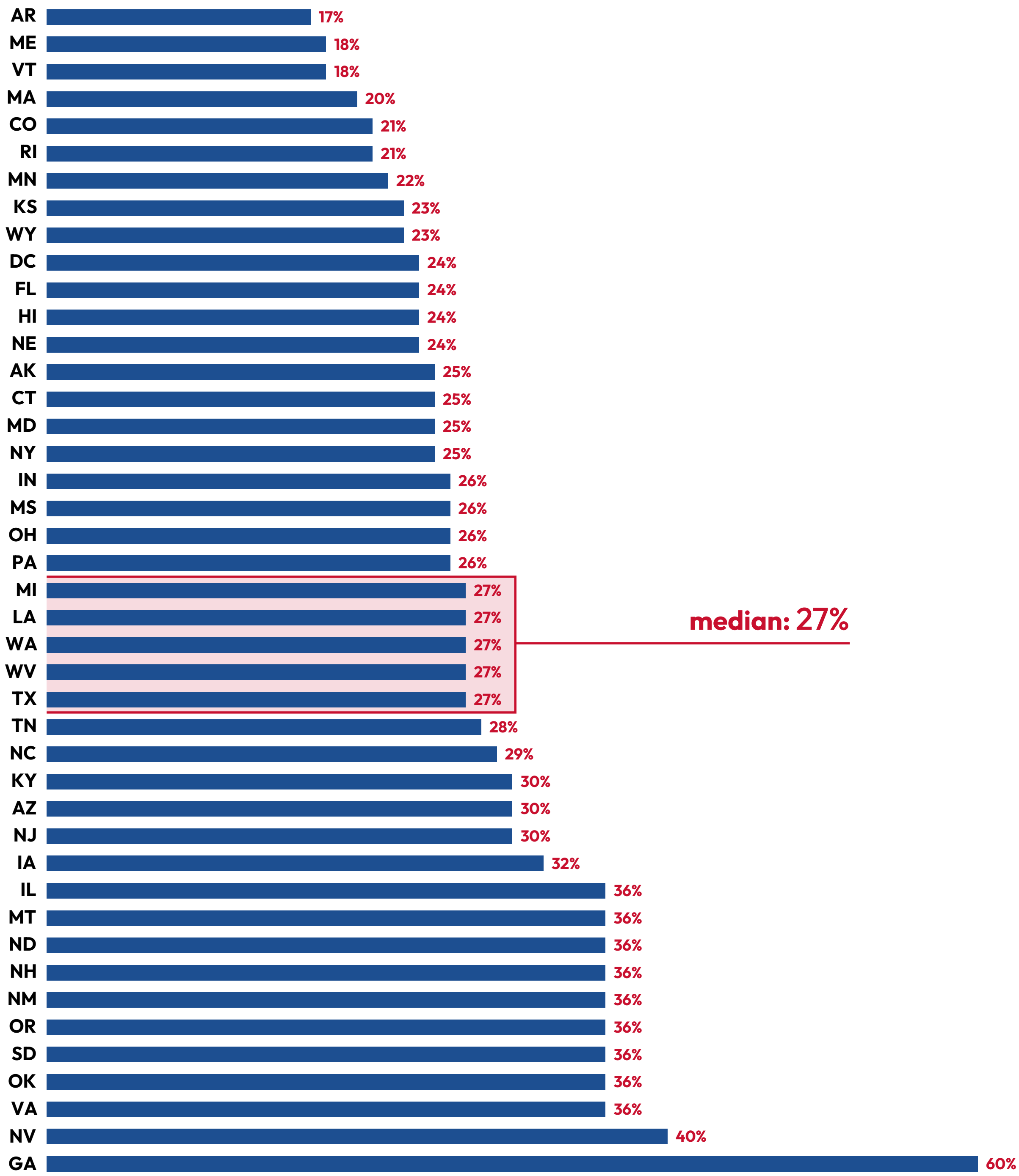
If states raise their rates to 36%, the difference in the amount that the consumer ends up paying can be stark. For example, a bill introduced in Florida in 2023 would have raised the permissible interest on a $25,000 loan from a blended 20.5% APR to 36% APR. For a $25,000 loan payable over five years, that change would have added $14,076 to the cost of the loan. Fortunately, the governor vetoed the bill.

Longer terms on larger loans also heighten the impact that higher interest rates have on a consumer's ability to make progress in repaying the principal. For a loan with a short term, the amortization schedule is not particularly important to the consumer. As long as the payments are affordable, a consumer will fully repay a three-month, $500 loan at 36% in three months. But if a $10,000, 5-year loan carries 36% interest, after a full year of payments the consumer will have paid $4,335, yet will have reduced the principal by only $870, and will still owe more than $9,000. A large remaining balance can discourage a consumer. It also limits the consumer's options to get help paying off the loan should it prove unaffordable over that long term.

Unfortunately, some states apply their interest rate limits only to loans up to a certain size. The belief when their laws were adopted may have been that consumers who took out these larger loans were sophisticated parties who could look out for themselves. But a loan that was enormous decades ago no longer is so uncommon. Loans as large as $10,000 to $30,000 or larger are offered for credit card debt consolidation and many other purposes. Even a $100,000 loan is not a huge amount when used for home remodeling or higher education. Consumers who take out these loans need protection against unaffordable interest.

HOW THE STATES RATE

Forty-two states and the District of Columbia cap the interest rate for a 5-year, unsecured installment loan of $10,000 from a licensed non-bank lender, including all fees that the consumer must pay to get the loan, at a median cap of 27% APR.



The APR is 24% or less for 13 of these states—Arkansas, Colorado, District of Columbia, Florida, Hawaii, Kansas, Maine, Massachusetts, Minnesota, Nebraska, Rhode Island, Vermont, and Wyoming.

The APR is 25% to 27% for 13 states—Alaska, Connecticut, Indiana, Louisiana, Maryland, Michigan, Mississippi, New York, Ohio, Pennsylvania, Texas, Washington, and West Virginia.

The APR cap is 28% to 36% for 15 more states—Arizona, Iowa, Illinois, Kentucky, Montana, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Oklahoma, Oregon, South Dakota, Tennessee, and Virginia.

Nevada and Georgia are outliers among the states that cap interest rates for this sample loan. Nevada allows APRs up to 40%, and Georgia has the highest rate cap in the country, an eye-popping maximum of 60% APR. At that rate, a Georgia consumer can be charged $21,699 in interest for a five-year $10,000 loan—the epitome of a debt trap.

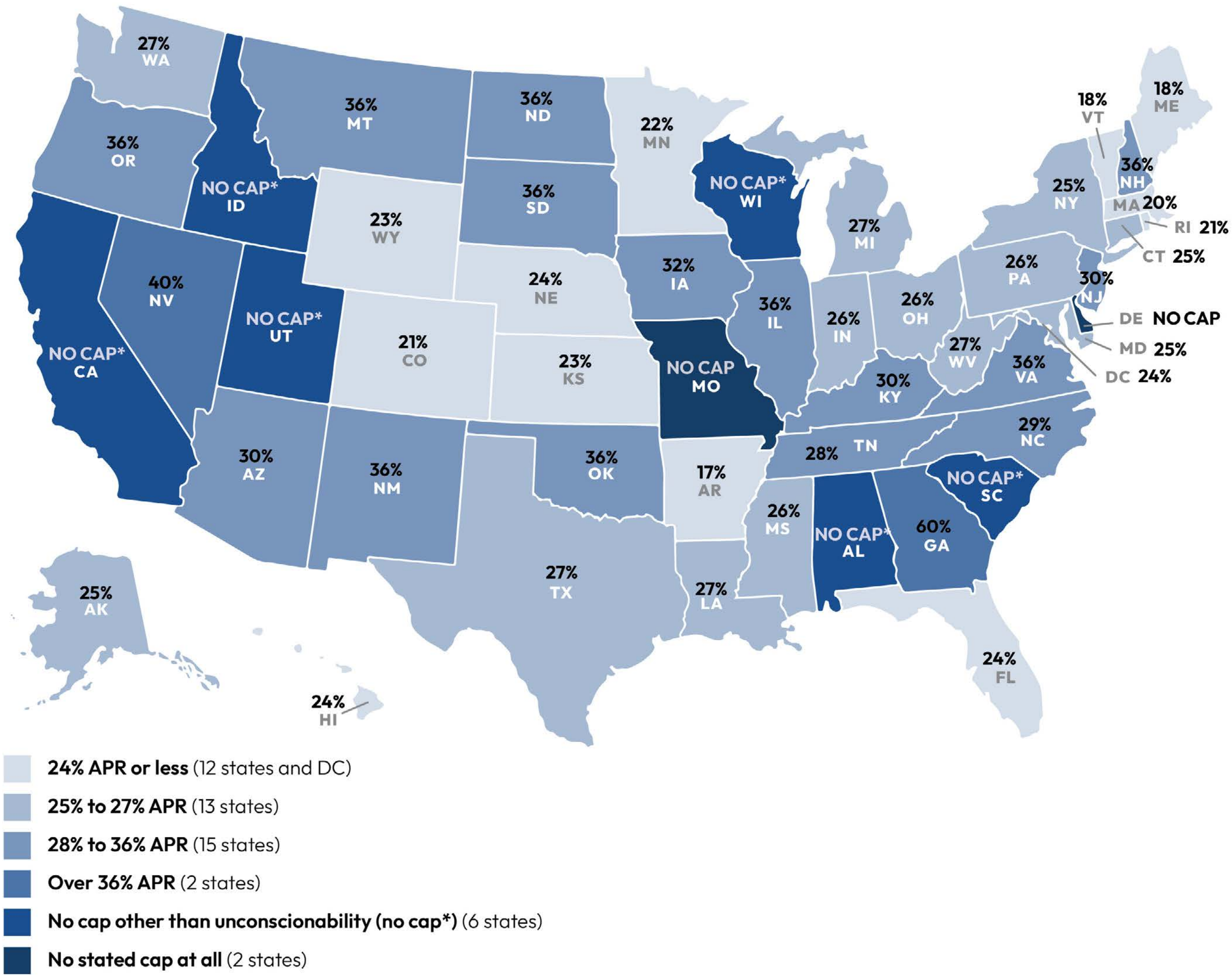
Six states do not place any numerical cap on the interest rate and fees for a loan of this size – Alabama, California, Idaho, South Carolina, Utah, and Wisconsin. They only require that the interest and fees not be unconscionable—in other words, that they not shock the conscience.

Two states, Delaware and Missouri, have no interest rate limit at all and not even a bar on unconscionability for a 5-year $10,000 installment loan.[4]

The map on the next page shows the APR allowed by each state for a $10,000, 5-year unsecured installment loan by a licensed non-bank lender, including all fees that the consumer must pay to get the loan.

Map: APRs Allowed for $10,000 Five-Year Loan

Showing the maximum APRs allowed for non-bank lenders



Notes: *Delaware's lending laws do not have a statutory prohibition of unconscionability, but at least one decision from a lower court in Delaware, James v. Nat'l Fin., L.L.C., 132 A.3d 799 (Del. Ch. 2016), applies a general concept of unconscionability to interest rates.*

SIGNIFICANT CHANGES IN THE STATES SINCE 2018

Twelve states—Indiana, Kentucky, Michigan, Minnesota, Michigan, Minnesota, North Dakota, New Mexico, Ohio, Oklahoma, Tennessee, Virginia, and Texas—made significant changes to their lending laws since our 2018 report.

The most dramatic changes were in Ohio, New Mexico, North Dakota, and Virginia. Ohio closed a loophole that had resulted in widespread evasion of its rate caps. In New Mexico, North Dakota, and Virginia, loans of this size had no cap at all on the interest rate and fees. All three states have now imposed a 36% rate cap, improving the protections for consumers, though the rate is still too high for a large loan. (Virginia's law now also allows a "processing fee" of up to $150).

Another seven states—Indiana, Kentucky, Michigan, Minnesota, North Carolina, Oklahoma, Tennessee, and Texas—increased their rate caps. Four of those states—Indiana, Michigan, Minnesota, and Texas—made relatively small increases of no more than one percentage point by applying inflation adjustments to fee caps.

Kentucky and Oklahoma, however, significantly increased their rate caps. Kentucky increased its interest rate cap for a 5-year $10,000 loan from 24% to 29%. Kentucky also allows a $150 origination fee. Taking both the interest and the fee into account, it now allows a 30% APR for this loan, increased from 24% in 2018. That change adds almost $2,000 in interest to a $10,000, 5-year loan.

Oklahoma's increase was even bigger. Oklahoma's maximum rate increased from 25% APR to 36% APR as of February 2024 primarily due to new legislation adding the Federal Funds rate to the pre-existing maximum rates.[5] Raising rates from 25% APR to 36% APR adds over $4,000 in interest to a $10,000, 5-year loan.

Oklahoma's maximum rate increased from 25% APR to 36% APR, which adds over $4,000 in interest to a $10,000, 5-year loan.

RECOMMENDATIONS

To protect consumers from high-cost lending, states should:

- **Cap APRs well below 36% for large loans, with rates decreasing as amounts increase.** For example, Rhode Island caps rates at 36% for loans up to $300, at 30% for loans up to $800, at 24% for loans up to $5,000, and at 21% for larger loans. (Even 21% is very high for especially large loans and for secured loans.) A general 36% interest rate cap is an improvement over no rate cap at all, but states should not raise interest rates on larger loans to that level.
- **Prohibit loan fees or strictly limit them** to prevent fees from being used to undermine the interest rate cap and acting as an incentive for loan flipping.

- **Include all payments in the APR calculation, whether or not they are deemed "voluntary."** Some lenders have tried to disguise fees as purportedly voluntary "tips," expedite fees, or donations.
- **Ban the sale of credit insurance and other add-on products**, which primarily benefit the lender and increase the cost of credit. At a minimum, include their cost in the APR.
- **Prevent loopholes for open-end credit.** Rate caps on installment loans will be ineffective if lenders can evade them through open-end lines of credit with low periodic interest rates but high fees.
- **Examine consumer lending bills carefully.** Predatory lenders often propose bills that obscure the true interest rate, for example, by presenting it as 24% per year plus 7/10ths of a percent per day instead of 279%. Or the bill may list the per-month rate rather than the annual rate. Get a calculation of the full APR, including all interest, all fees, and all other charges, and reject the bill if it is over 36%.
- **Include anti-evasion provisions** to prevent lenders from laundering their loans through out-of-state banks to evade state rate caps or disguising their loans as sales, wage payments, or other devices.

In addition, states should make sure that their loan laws address other potential abuses. States should:

- Require lenders to evaluate the borrower's ability to repay any credit that is extended.
- Prohibit mechanisms, such as security interests in household goods and post-dated checks, that coerce repayment of unaffordable loans.
- Require proportionate rebates of all up-front loan charges when loans are refinanced or paid off early.
- Limit balloon payments, interest-only payments, and excessively long loan terms.
- Employ robust licensing and reporting requirements, including default and late payment rates, for lenders.
- Include strong enforcement mechanisms, including making unlicensed or unlawful loans void and uncollectible and providing a private right of action with attorneys' fees.
- Tighten up other lending laws, including credit services organization laws, to prevent evasions.

See NCLC's webpages on Payday and Installment Loans, Rent-a-Bank Lending, and Fintech Credit for more information on state lending laws and efforts to evade them.

APPENDIX: METHODOLOGY

Our APR calculations include all the costs that the borrower may be required to pay to obtain and use the extension of credit, including application fees, investigation fees, document preparation fees, transaction fees, "points," annual fees, and monthly fees. We have not included any fees that can be charged only for mortgage loans or loans with other security interests since the report focuses solely on unsecured, non-real estate lending. Nor have we included fees, such as late charges or dishonored check charges, that are imposed only if some future, unanticipated event occurs. Late fees can be disguised finance charges, however, so policymakers and regulators should place strict limits on them and be alert for abuses.

Our APR calculations also do not include charges for add-on products, such as credit insurance, which are covered by a complex set of insurance and lending laws. However, fees for add-on products can greatly swell the cost of a loan, so they are important topics for policymakers to address. Indeed, the Military Lending Act (MLA), which places a 36% APR cap on loans to members of the military and their families, requires the APR to take into account not just interest and fees but also credit insurance charges and other add-on charges. The MLA is also far more accurate than the federal Truth in Lending Act as a disclosure of the cost of open-end credit such as credit cards. Because of this, the MLA APR is the gold standard, both for purposes of cost comparison and for purposes of legal rate limits.

All APRs in this report are rounded up or down to the nearest whole number. All dollar amounts are likewise rounded to the nearest whole dollar. Unless state law specifies otherwise, we have assumed that origination fees are added to the $10,000 principal before the interest is calculated.

Where state laws are ambiguous, we have searched for judicial decisions or guidance from the state consumer credit regulator. In the absence of definitive interpretations, we have used our best judgment in determining the requirements of these laws. Errors should be brought to the attention of the authors.

ENDNOTES

1. *See* Lauren Saunders, National Consumer Law Center, Why Cap Interest Rates at 36%? (2021), https://www.nclc.org/resources/why-cap-interest-rates-at-36/.
2. Available at https://www.nclc.org/wp-content/uploads/2022/09/2018-installment-loans-rpt.pdf.
3. *See* Carolyn Carter, Lauren Saunders, Margot Saunders, National Consumer Law Center, *Predatory Installment Lending in the States: How Well Do the States Protect Consumers Against High-Cost Installment Loans?* (2023), https://www.nclc.org/resources/predatory-installment-lending-in-the-states-how-well-do-the-states-protect-consumers-against-high-cost-installment-loans-2023/; Lauren Saunders, Margot Saunders, & Carolyn Carter, *Misaligned Incentives: Why High-Rate Installment Lenders Want Borrowers Who Will Default* (2016), https://www.nclc.org/resources/misaligned-incentives-why-high-rate-installment-lenders-want-borrowers-who-will-default/; Carolyn Carter, Lauren Saunders, Margot Saunders, & Andrew Pizor, *Installment Loans: Will States Protect Borrowers from a New Wave of Predatory Lending?* (2015), https://www.nclc.org/resources/installment-loans-will-states-protect-borrowers-from-a-new-wave-of-predatory-lending/. See also National Consumer Law Center, *Consumer Credit Regulation* (3d ed. 2020), updated at www.nclc.org/library.
4. At least one decision from a lower court in Delaware, *James v. Nat'l Fin., L.L.C.*, 132 A.3d 799 (Del. Ch. 2016), applies a general concept of unconscionability to interest rates, but Delaware's consumer loan laws do not include an explicit prohibition of unconscionable terms.
5. Oklahoma also applied an inflation adjustment to its cap on closing fees.

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