The Center for Financial Services Innovation (CFSI) leads a network of financial services innovators committed to building a more robust financial services marketplace with higher quality products and services. CFSI recognizes that with inadequate savings and limited access to traditional lines of credit, millions of consumers turn to installment loans, a form of small-dollar credit, to meet their borrowing needs. Borrowers may use installment loans to support a planned purchase or cover unexpected expenses. CFSI stresses that for individuals struggling day-to-day, access to high-quality, small-dollar installment loans may be critical for building a path to financial health. Thus, CFSI emphasizes that there is a critical need for high-quality products designed for both borrower success and lender profitability.

As a way to identify practices in the small-dollar installment lending market that encourage quality and increase innovation, CFSI published a report in October 2015 entitled, "A Snapshot of Quality and Innovation among Small-Dollar Credit Installment Lenders." The report shares an analysis of 16 installment lenders that have adopted some of the high-quality practices CFSI recommends. The 16 installment lenders surveyed include banks, credit unions, and non-bank direct lenders.

According to the report, a high-quality small-dollar loan is one that: (1) is made with a high confidence in the borrower’s ability to repay, (2) is structured to support repayment, (3) is priced to align profitability for the provider with success for the borrower, (4) creates opportunities for upward mobility and greater financial health, (5) has transparent marketing, communications, and disclosures, (6) is accessible and convenient, and (7) provides support and rights for borrowers. CFSI ranked the degree of adoption by lenders of the first six of these guidelines at “high” or “medium.” Below are examples of how installment loans meet these guidelines.

1. Installment loans are made with a high confidence in the borrower’s ability to repay. The study showed a high degree of adoption regarding underwriting. Lenders employ advanced algorithms to make underwriting decisions, reduce rates for customers who demonstrate positive behaviors, and provide guidance about how to use their products successfully.

The report highlighted a non-bank installment lender, stating, “In addition to analyzing credit reports, Sun Loan uses a budget form as an underwriting template. Taking a personal approach, the prospective borrower and loan officer complete a budget together to document monthly income and expenses. Ability to repay, and therefore loan eligibility, is assessed based on a borrower’s free income.”

2. Installment loans are structured to support repayment. All the lenders surveyed offer fully amortizing loans and give borrowers some flexibility with choosing the amount or terms of their loan. For customers who are not paid on a traditional two-week cycle, some lenders customize repayment schedules to better match a borrower’s income schedule. Several lenders help struggling borrowers, particularly those who are facing income or employment changes,
reschedule or restructure their loan payments. A majority of the lenders surveyed provide prospective borrowers with access to a tool that helps them understand the cost of their loan. The tool may be a simple calculator or it may be a more complex feature that helps borrowers customize their loan terms.

(3) Installment loans are priced to align profitability for the provider with success for the borrower. Lenders ensure borrowers receive the most appropriate and lowest-priced loan for which they qualify. Moreover, lenders generally do not rely on penalty fees and interest rates or fees earned from refinancing as profit drivers. Many of the lenders surveyed offer reasonable grace periods (of at least 2 days), allowing customers to avoid late payment fees and penalty interest rates. Furthermore, all the lenders surveyed reduce rates for subsequent loans for customers who have demonstrated positive payment histories and maintenance of external credit, as reflected by their credit scores.

Interestingly, the report underscores the importance of providing consumers with the option of automatic payments. CFSI writes that automatic payments help borrowers avoid missed payments and the associated fees and charges. Of course, automatic payments should not be coercive, but a convenience for borrowers. CFSI highlights an incentive program by an installment lender. The lender allows consumers who opt-in for automatic payments to potentially qualify for larger loans at the same rate.

Also important, CFSI views ancillary products as a benefit to the borrower. The report states that lenders provide additional benefits to borrowers who demonstrate positive behavior. As an example, the report notes that nine lenders, more than half of the report sample, offer additional financial products to borrowers, including payment products, other loans, checking accounts, and ancillary insurance products.

(4) Installment loans create opportunities for upward mobility and greater financial health. A majority of the lenders in the sample report repayment to major credit bureaus. Reporting loan performance information is critical because it helps borrowers build credit. Many lenders surveyed in this report also offer valuable financial education and guidance.

(5) Installment lenders use transparent marketing, communications, and disclosures. The report found a high degree of adoption of practices related to disclosing the full cost of the loans to borrowers in a simple and clear language, with no hidden fees or misleading information. Additionally, all of the lenders surveyed for the report clearly communicate the risks of borrowing to their customers (e.g., their credit reports will be pulled, their employment may be verified, they will be liable for making payments, and there are consequences for nonpayment).

(6) Installment loans are accessible and convenient. Lenders make loan decisions in a timely fashion, balancing the borrower’s desire for quick access to funds with the lender’s commitment to responsible underwriting. All 16 lenders surveyed typically fund borrowers within one business day or less. There is a clear expectation set for prospective borrowers about how quickly they will receive a loan decision.
(7) Installment lenders are working to provide support and rights for borrowers. Lenders ensure that borrowers can obtain customer support easily and are treated respectfully and helpfully. Five of the lenders surveyed make their services and materials available in both English and Spanish. Seven other lenders have some bilingual capability (i.e., access to interpreters, bilingual staff). Depending on the region and available staff, some lenders have capability to communicate with clientele in other languages, including Hmong, Navajo, Chinese, and Punjabi.

In conclusion, the findings of this report show how some high-quality lending practices have been adopted by a sample of installment lenders. Of course, as with anything, there are still improvements that this innovative group of lenders can adopt over time.