DEBT COLLECTION RESTRICTIONS AND THE EFFECT ON ACCESS TO CREDIT

Restrictions on the ability of creditors to collect on delinquent loans increases lending risk and diminishes credit access, as lenders are forced to lend only to the least risky borrowers.

Restrictions meant to protect consumers by limiting their liability for repayment have the unintended consequence of reducing safe and affordable credit options for the very people the *restrictions are aimed at protecting, as Federal Reserve and other research demonstrates:*

1. *Using the Courts for Private Debt Collection: How Wage Garnishment Laws Affect Civil Judgments and Access to Credit (2023)*[i]

This working paper from the CFPB Office of Research Working Paper Series, released just last month, notes:

- "Changes in garnishment produce meaningfully large changes in available credit, especially for low credit score consumers."
- "It appears that creditors are more likely to lend when they can recover more after a default, which is a function of both wages and how much can be garnished from the wages."
- "Wage garnishment appears to affect access to credit more strongly for below 700 credit score consumers, who are also the most likely to have a civil judgment."

2. *Access to Credit and Financial Health: Evaluating the Impact of Debt Collection* (2017)[ii]

This paper, from the New York Federal Reserve, finds that restricting collection activities leads to a clear decrease in access to credit and to a deterioration in household indicators of financial health, including credit scores. Specifically:

- A significant decrease in auto and credit card originations
- A sizable and significant increase in delinquent credit card and non-traditional finance balances
- A small but statistically significant reduction in credit scores
- A larger decrease in credit access for borrowers with low credit scores

3. *Less Mainstream Credit, More Payday Borrowing? Evidence from Debt Collection Restrictions* (2022)[iii]

Supplemental to the above paper, author Julia Fonseca published further findings in the *Journal of Finance* that found "*debt collection restrictions cause consumers to borrow more from payday lenders, suggesting that mainstream and alternative credit are substitutes, especially for borrowers with limited access to mainstream credit.*"

4. *Debt Collection Agencies and the Supply of Consumer Credit* (2020)[iv]

This paper, from the Philadelphia Federal Reserve, focuses on credit cards and reaches many of the conclusions in the papers listed above. It also looks at wage garnishment control, and its effects on credit access. The results suggest that increases in state-level garnishment exemption rates are associated with:

- Lower recovery rates on charged off unsecured credit card loans made by credit unions.
- Lower recovery rates concentrated on smaller credit unions.
- Fewer revolving lines of credit per capita
- Higher interest rates charged by credit unions on unsecured credit card loans.
- Higher average balance on active revolving lines of credit.
- Lower TransUnion credit scores.
- Higher share of consumers with accounts in collection.

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[i] *Using the Courts for Private Debt Collection: How Wage Garnishment Laws Affect Civil Judgments and Access to Credit (2023)* (Consumer Financial Protection Bureau)

[ii] *Access to Credit and Financial Health: Evaluating the Impact of Debt Collection* (2017) (NY Fed)

[iii] *Less Mainstream Credit, More Payday Borrowing? Evidence from Debt Collection Restrictions (2022)* (Journal of Finance)

[iv] *Debt Collection Agencies and the Supply of Consumer Credit* (2020) (Philadelphia Fed)

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