How Virginia's 2020 Fairness in Lending Act Reforms Small-Dollar Loans

Law closes regulatory loopholes, caps interest rates, and provides lessons for other states

Overview

After years of legislative efforts to foster a safe and viable market for small loans, Virginia lawmakers in 2020 passed bipartisan legislation—the Fairness in Lending Act (S.B. 421/H.B. 789)—to prohibit loans with large final payments, known as balloon payments, and bring down prices. The law rationalizes what had been a disparate regulatory structure, governed by a patchwork of laws that allowed payday and auto title loans with unaffordable payments and unnecessarily high costs, and exposed borrowers to financial harm, including repeated borrowing and high rates of vehicle repossession. Previous research by The Pew Charitable Trusts showed that before the reforms, companies routinely charged Virginians three times more than customers in lower-cost states.[1]

Virginia lawmakers balanced concerns about the availability of small-dollar credit with the urgency of stopping harmful lending practices, a challenge that officials in other states also have struggled with. Virginia's evidence-based approach builds on successful reforms previously enacted in Colorado and Ohio that maintained widespread access to credit and measurably improved consumer outcomes by closing loopholes, modernizing outdated statutes, and prohibiting balloon payments. Legislators designed the act to reflect "three key tenets of responsible lending: affordable payments, fair prices, and reasonable time to repay."[2]

Pew's analysis of the act confirmed that, under the legislation, lenders can profitably offer affordable installment loans with structural safeguards, saving the typical borrower hundreds of dollars in fees and interest with estimated total consumer savings exceeding $100 million annually. (See Table 1.) This brief examines how Virginia reformed its laws to achieve a more modern, vibrant, and consumer-friendly small-loan market. Virginia's success offers replicable lessons for policymakers in other states struggling with high-cost, unaffordable loans.

Table 1

Virginia's Small-Credit Pricing Yields Significant Consumer Savings

Loan examples from before and after reform

Loan	Before reform	After reform	Resulting savings
$300 over 3 months	$222	$90	$132
$500 over 5 months	$595	$171	$424
$1,000 over 12 months	$1,400	$500	$900
$2,000 over 18 months	$7,136	$1,068	$6,068

Sources: Pew analysis of market data; "Virginia Fairness in Lending Act" (2020), https://lis.virginia.gov/cgi-bin/legp604.exe?201+ful+CHAP1258

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The problem: Outdated laws allowed abusive practices, prevented safer, lower-cost lending

Virginia was one of 35 states that allowed payday loans and one of 22 that permitted high-cost auto title loans secured by a borrower's vehicle, loans that cater primarily to consumers with damaged credit scores who need help paying regular bills or expenses. However, these loans have well-documented pitfalls, including excessive costs, unreasonably short repayment terms, and unaffordable payments that consume so much of borrowers' incomes that they must repeatedly reborrow or risk losing their cars or the funds in their checking accounts.[3] According to regulatory data, the average title loan of $1,116 required a total repayment of more than $2,700 over 12 months.[4]

Virginia, like many states, had a patchwork of consumer lending statutes that had been enacted or revised at different times. This piecemeal approach created an uneven competitive landscape for lenders and meant that high-cost credit could be issued according to any one of four statutes, effectively at the lender's discretion. (See Table 2.) Many payday and title lenders offered "open-end" loans, which had unlimited repayment terms like credit cards, at annual percentage rates (APRs) of 299% or more. In addition, the state's Credit Services Business Act included language that high-cost lenders have relied on to justify charging brokerage fees that would otherwise be illegal under state interest rate caps. Given Virginia's array of inconsistent laws, revising just one at a time would not have been sufficient to protect consumers; lenders would have been able to simply switch to operating under a different statute.

At the same time, Virginia's outdated policies made it impossible or unprofitable for lower-cost lenders, such as nonbank installment lenders and financial technology companies, to offer affordable small-dollar installment loans and compete in the commonwealth with conventional payday and title lenders.[5] For example, before reform, a lender could charge prices that resulted in APRs of more than 300% for a balloon-payment payday loan, but installment lenders, whose prices are three or four times lower, were effectively prohibited from offering a similarly sized loan. As a result, installment and other lower-cost lenders could not operate profitably in Virginia, so they did not do business in the state.

The solution: Modern statutes established efficient protections, enabled affordable installment loans

The Virginia Fairness in Lending Act was sponsored by Senator Mamie Locke (D-Hampton) and Delegate Lamont Bagby (D-Henrico), had more than 50 legislative co-patrons from both parties, and received support from diverse stakeholders, including consumer advocates, community organizations, faith leaders, lower-cost installment lenders, and the state attorney general.[6] High-cost lenders opposed the reform, claiming that they would not be able to operate at the required lower prices, despite contrary evidence from other markets, but both chambers ultimately passed the legislation on a bipartisan basis.[7] Governor Ralph Northam (D) signed the act into law at a ceremony on Aug. 3, 2020; it becomes effective Jan. 1, 2021.[8]

Table 2

Virginia's Small-Dollar Credit Market Reform Solves Common Problems

Key features of the Fairness in Lending Act

Problem	Solution
Evasion. High-cost lenders operated using their choice of four statutes or without a state license. No regulation governed interest rates for installment loans above $2,500 or lines of credit. Unlicensed online lending operated freely via statutory loopholes and no regulation governed fees that could be charged for brokering loans.	All high-rate lenders must acquire a license under Virginia statutes (Chapters 15, 18, or 22). These licenses are available to all lenders, whether they operate through stores or online or issue secured or unsecured loans. Loans issued in violation of state law are deemed uncollectible, strengthening enforcement against evasion.
Unaffordable loans. Short-term balloon-payment loans consumed 20% of the typical Virginia borrower's paycheck, resulting in repeated borrowing.	Research-based safeguards for affordable installment payments set flexible durations, typically of four months or more, and allow for a wide range of loan sizes. Lenders may not require balloon payments.
Excessive cost. Payday lenders charged three times more in Virginia than they did in other states, such as Ohio and Colorado. Borrowers often paid more in fees and interest than they originally received in credit.	Evidence-based pricing limits—36% interest plus limited fees—are viable for lenders and maintain widespread access to credit. Simple rules ensure easy lender compliance and APRs that decline automatically as loan sizes increase. For short-term installment loans (formerly "payday loans"), total costs may not exceed 50% of the loan amount or 60% for loans of more than $1,500; for example, for a $1,000 loan, a borrower cannot be charged more than $500 in fees and interest.
Harm. Aggressive collection practices put borrower checking account funds and vehicles at risk; 1 in 8 title loan borrowers had a vehicle repossessed.	Loans secured with checks, electronic repayment plans, or a vehicle title must have affordable payments and lower prices and cannot employ harmful repossession and collection practices. Loan-servicing partnerships are subject to enhanced regulation, and high-cost loan brokering is prohibited.

Note: The Virginia Fairness in Lending Act of 2020 (H.B. 789/S.B. 421) takes effect on Jan. 1, 2021.

Sources: The Pew Charitable Trusts, "Virginia's Payday and Title Lending Markets Among the Nation's Riskiest" (2019), https://www.pewtrusts.org/en/research-and-analysis/fact-sheets/2019/10/virginias-payday-and-title-lending-markets-among-the-nations-riskiest; Pew analysis of Virginia law

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The modernized statutes enable numerous business models for lending to customers with thin or damaged credit histories and require loans to have affordable payments, transparent terms, and fair prices, regardless of the collateral or whether they are made at a retail location or online. This set of standards creates a level playing field, enabling varied companies, including payday, title, installment, or financial technology firms, to compete in Virginia, expands consumer choice, and protects borrowers from harmful practices. (See Table 3.)

Table 3

Virginia Fairness in Lending Act of 2020 Reforms Statutes to Protect Consumers, Maintain Access to Credit

Key features of H.B. 789/S.B. 421

	Statute		
	Open-end credit	**Consumer finance companies**	**Short-term loans (formerly "payday lenders")***
Market implications	Preserves mainstream open-end credit while preventing high-cost lenders from using this statute.	Enables regulated installment lending, in-store and online, from nonbank consumer finance companies, financial technology firms, or employer-based loan programs. Available to borrowers with no or low credit scores.	Replaces balloon-payment payday loans with short-term small installment loans for borrowers with thin or damaged credit histories. These loans feature affordable payments, reasonable time to repay, and lower prices that are still viable for responsible lenders. Allows widespread access to credit not only from payday lenders already operating in Virginia, but also from lower-cost companies that previously did not lend in the state.
Loan size	No limit	$300 to $35,000	$2,500 maximum
Annual interest rate	36%	36%	36%
Fees	Annual participation fee of up to $50; no other fees	Loan processing fee of $50 or 6% of the initial principal, whichever is greater, not to exceed $150	Monthly fee up to 8% of original loan amount, not to exceed $25
Minimum duration	Open-ended	Six months with substantially equal installment payments	Four months with substantially equal installment payments†
Other safeguards	Loans made in violation of the statute are void and uncollectible; enhanced enforcement authority for state attorney general	Loan processing fee can be charged no more than twice a year; loans made without a license or using evasive practices are void and uncollectible; enhanced enforcement authority for state attorney general	Total costs capped at 50% of the loan amount or 60% for loans of more than $1,500; loans made without a license or using evasive practices are void and uncollectible; enhanced enforcement authority for state attorney general

* Before reform the "short-term loan" statute was titled "payday lenders" and authorized balloon-payment loans with APRs exceeding 300%.

† The four-month minimum term does not apply if monthly installment payments are limited to 5% of gross or 6% of net borrower monthly income.

Note: State lawmakers also chose to keep the existing vehicle title loan statute, applying almost identical reforms as the short-term loan statute with minor variances including a six-month minimum loan term (rather than four), a $15 maximum monthly fee (rather than $25), and protections against repossession. The law also amended the Credit Services Businesses Act to prevent the brokering of high-rate loans. For a more comprehensive summary of the Virginia Fairness in Lending Act, see http://pewtrusts.org/en/research-and-analysis/fact-sheets/2020/10/virginia-fairness-in-lending-act-of-2020-reforms-small-credit.

Sources: "Virginia Fairness in Lending Act" (2020), https://lis.virginia.gov/cgi-bin/legp604.exe?201+ful+CHAP1258; Virginia Code Title 6.2, Chapter 3, Section 6.2-312, https://law.lis.virginia.gov/vacode/title6.2/chapter3/section6.2-312; Virginia Code Title 6.2, Chapter 15, https://law.lis.virginia.gov/vacode/title6.2/chapter15; Virginia Code Title 6.2, Chapter 18, https://law.lis.virginia.gov/vacode/6.2-1800; Virginia Code Title 6.2, Chapter 22, https://law.lis.virginia.gov/vacode/6.2-2200/; Virginia Code Title 59.1, Chapter 25.1, Section 335.1, https://law.lis.virginia.gov/vacode/title59.1/chapter25.1/section59.1-335.1/

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Lessons for other states

Lawmakers in 32 states have struggled to appropriately regulate payday lending to balance the interests of consumers and responsible lenders.[9] Frequently, legislative proposals with bipartisan support have been derailed because of concerns about restricting consumers' access to credit.[10] However, research has shown that policymakers can foster a viable market for loans with safeguards and lower costs without reducing the availability of small-dollar credit, and Virginia's evidence-based approach illustrates how states can adopt robust consumer protections while establishing a level playing field for businesses. Other states can achieve comprehensive high-cost lending reform by prohibiting balloon-payment products and requiring that all loans can be paid back in affordable, amortizing installments, establishing reasonable pricing by limiting interest rates to 36% plus a monthly fee of up to 8% of the loan amount, capped at $25, capping total loan costs, setting minimum loan terms of four months, and preventing lenders from evading those safeguards.

Conclusion

As a result of the Fairness in Lending Act, the small-dollar loans issued in Virginia will cost approximately three times less than before reform. The act builds on successful reforms from other states, and though various state laws differ, they share common fundamental elements including closing loopholes, prohibiting balloon payments, and modernizing statutes to enable widespread access to credit according to uniform rules that ensure affordable installment payments for borrowers and a level competitive playing field for lenders. By embracing fair lending reforms like those enacted in Virginia and Ohio, lawmakers in other states that allow high-cost loans can save consumers millions of dollars each year while ensuring widespread access to credit.

Endnotes

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