



The Military Lending Act





Background

In 2006, the Department of Defense (DOD) issued the *Report on Predatory Lending Practices Directed at Members of the Armed Forces and their Dependents*.¹ The report found that military families were prime targets for predatory lenders likely due to their financial inexperience, steady income but little savings, and possibly flawed or no credit history.

The original *Report* indicated some very interesting findings with regards to predatory loan types, and how they relate to military personnel. The *Report* found that an overwhelming number of service members obtained payday loans and other types of loans that contain predatory features. It noted the strong presence of predatory lenders around military bases providing fast and easy access to cash for servicemembers and their dependents. Additionally, the convenience and ease of these types of loans is appealing to servicemembers stationed outside of the United States, as these type of loans are easily obtained via Internet stores that can be accessed while based anywhere in the world.

The *Report* found that the type of loans identified (specifically payday lending, internet lending, car title lending, military installment loans, rent to own, and refund anticipation loans) had similar characteristics. These loans charge high fees for small dollar loans with APRs typically in the triple digits. Oftentimes, the short-term nature results in the servicemember being unable to pay the loan in full when it comes due, resulting in multiple renewals and extensions that incur more fees without decreasing the principal, and putting the borrowers in a worse position than they were previously. In addition, deceptive marketing is frequently used; often going as far as to imply that some loans are sanctioned by the military.

As a result, the *Report* concluded that a focus should be placed on three areas:

- Education
- Alternatives to predatory loans
- Effective policies/statutes

From these areas of focus, the Military Lending Act – or “MLA” – was born.

The Original MLA

Initially implemented in 2007, the scope of the MLA was limited. The original legislation applied to active duty military, active National Guard, or Reserve personnel and their dependents. It capped the interest rate at 36% and enacted a number of protections. However, it narrowly covered three products:

1. Closed-end payday loans for no more than \$2,000 and with a term less than 91 days;
2. Closed-end auto title loans with a term of 181 days or fewer; and
3. Closed-end tax refund anticipation loans.

All other types of loans were omitted from the Act.

In 2011, the Annie E. Casey Foundation requested that the Consumer Federation of America revisit the MLA and see if its initial goals were being met.² The study found that although the MLA did have some success in meeting its intended goals, the most concerning finding was that the limited coverage of the initial rule gave predatory lenders the ability to manipulate the loan terms, amounts, and/or loan types so that they would fall outside of the scope of the rule. In short, the recommendation was for the Department of Defense (DOD) to revisit the MLA and to close the gaps that allow for unscrupulous, yet legal, workarounds.

¹http://archive.defense.gov/pubs/pdfs/Report_to_Congress_final.pdf

²<http://www.consumerfed.org/pdfs/Studies.MilitaryLendingAct.5.29.12.pdf>



The MLA Revamped

The Foundation's recommendations were not taken lightly. The DOD conducted a three-year study to ensure that the necessary changes were put in place. As directed by Congress, the DOD consulted with the Federal Trade Commission, as well as the financial regulatory agencies, to determine where any shortfalls existed.

In 2013, the MLA was amended to transfer enforcement to the CFPB, with other regulatory agencies making the MLA enforceable in the same manner as Regulation Z. The previous version of the Act did not specify who was responsible for enforcing the rules. The 2013 amendment also included civil liability provisions that allowed for private actions to be filed in federal court expanding the legal protections for servicemembers.

The DOD issued a final rule on July 21, 2015, which greatly expanded the coverage and the protections afforded to servicemembers in an attempt to put an end to the gaps. The final rule was effective October 1, 2015, but will apply to most consumer credit transactions **that are consummated after October 3, 2016 and after October 3, 2017 for credit cards.**

Coverage

The amended MLA defined consumer credit to be more in line with Regulation Z definitions, and expanded the coverage to a wider range of credit products. Just like Regulation Z, MLA protections apply to consumer credit, which is defined as "credit offered or extended to a covered borrower primarily for personal, family, or household purposes, and that is subject to a finance charge or payable by a written agreement in more than four installments." The scope not only expands the reach of the current categories by removing the dollar and term limitations, it also reaches further beyond the three narrowly defined categories of credit to include most types of consumer credit. Exemptions for residential mortgage loans and vehicle purchase money loans remain in the amended rule and are not subject to the provisions of the MLA.

The MLA applies to all active duty servicemembers and their dependents at the time of establishing credit. The rule applies to credit established while on active duty, not before or after. If the account was opened while the servicemember was not on active duty, the servicemember is not considered a covered borrower under the MLA.

Through October 3, 2016, the creditor may rely on the servicemembers statement regarding their military status. After this date, the creditor has discretion in how they determine the applicant's eligibility, and may verify the status from DOD's database found at <https://mla.dmdc.osd.mil/> or rely on information obtained from a nationwide consumer reporting agency.

MLA Protections

Military Annual Percentage Rate

As with the initial rule, the Military Annual Percentage Rate (MAPR) is capped at 36%. Though this number seems extreme, when compared to the triple figure rates these types of loans historically cost, the protection is evident. The MAPR calculation is similar to the APR calculation under Regulation Z, including all interest and finance charges. However, certain fees are required to be included in the calculation even if they would not be considered a finance charge under Regulation Z including:

- Credit insurance premiums and fees for debt cancellation or debt suspension agreements;
- Fees for credit-related ancillary products sold in connection with the credit transaction or account;
- Finance charges associated with the consumer credit; and
- Certain application fees and participation fees, including annual fees.

Disclosure Requirements

In addition to the disclosures required under Regulation Z for consumer loans, the MLA requires the creditor to provide a statement of the MAPR that is applicable to the loan prior to consummation. The MLA outlines model language that may be used for this purpose:

"Federal law provides important protections to members of the Armed Forces and their dependents relating to extensions of consumer credit. In general, the cost of consumer credit to a member of the Armed Forces and his or her dependent may not exceed an annual percentage rate of 36 percent.

This rate must include, as applicable to the credit transaction or account: The costs associated with credit insurance premiums; fees for ancillary products sold in connection with the credit transaction; any application fee charged (other than certain application fees for specified credit transactions or accounts); and any participation fee charged (other than certain participation fees for a credit card account)."

The disclosures must also include a clear description of the payment obligation. Regulation Z account opening disclosures for open-end disclosures, and payment schedules for closed-end credit, would satisfy this requirement.

Rollovers, Renewals, and Refinancing

To protect servicemembers from being stuck in expensive loans where fees continue to incur, but principal refuses to be paid down, the MLA prohibits rollovers, renewals, or refinancing. There are limited exceptions. If the new loan will be beneficial to the servicemember or his/her dependent, the MLA allows for it. The rule also carves out an exemption for federal or state regulated banks, thrifts, or credit unions.

Mandatory Arbitration Clauses/Legal Provisions

The MLA offers protection for servicemembers and their dependents in the event of a dispute. Creditors cannot require a service member or his or her dependent to submit to arbitration or burdensome legal conditions in the event of a dispute. In addition, the creditor cannot require the servicemember to waive any rights under the Servicemember Civil Relief Act or other state or federal laws.

Mandatory Allotment

The creditor cannot require the servicemember to agree to automatic paycheck reduction in order to repay the loan or require a direct deposit of the salary as a condition for qualifying for the loan. In addition, the creditor is prohibited from taking a security interest after the extension of credit in an account established in connection with the consumer credit.

Prepayment Penalty

The borrower must be able to pay back a loan early, in whole or in part, without being subject to a prepayment penalty.

Summary

The Military Lending Act is vital legislation in the attempt to curb the abuses active duty servicemembers and their dependents face more commonly than most realize. The initial legislation left room for improvement as unscrupulous creditors found ways to work around the rules, leaving servicemembers as victims. The amended rule attempts to close those loopholes by aligning the rule with the current definitions of consumer credit with Regulation Z and removing the dollar amount and term limitations. The DOD, CFPB, and other regulatory agencies will continue to ensure access to alternative types of loans and ensure access to education on those alternatives for all servicemembers and their dependents. Servicemembers are also free to file a complaint on these predatory lenders that continue to attempt to work outside the parameters set forth by the MLA.



For additional information on the MLA please view [BAI course 20084/C/M – Servicemember Issues](#), and be on the lookout for additional [BAI resources](#) in the future.