

Attention! Military Lending Act Compliance

This is being provided for informational purposes only, and not as legal advice. As the employer or user of consumer reports, it is your responsibility to ensure compliance with all of the relevant federal, state and local laws governing this area, including, but not limited to, the FCRA. We strongly recommend that prior to use, you consult with your own attorney.

It's time to add to your growing compliance checklist for 2016.

In July of 2015, the Department of Defense ("DoD") published a [Final Rule](#) ("Final Rule") to amend its regulation implementing the Military Lending Act ("MLA"). See 10 U.S.C. § 987. First enacted in 2006 under the part of the John Warner National Defense Authorization Act for Fiscal Year 2007, the MLA's aim was to provide protections against predatory lending practices targeted at U.S. military service members and their spouses and dependents. But while it once applied only to a short list of credit products, the newly implemented regulations have greatly expanded its coverage.

The Final Rule expands coverage of the current regulation to include many non-mortgage related credit transactions covered by the Truth in Lending Act ("TILA"), as implemented by Regulation Z.4 See 15 U.S.C. § 1601, *et seq.* It provides safe harbor methods for identifying borrowers covered by the Final Rule, prohibits the use of certain practices, and amends the content of the required disclosures. The Final Rule also contains new provisions about administrative enforcement, penalties and remedies.

The changes with the Final Rule encompass new types of creditors and credit products, including credit cards. While the DoD was responsible for implementing the Final Rule, enforcement will be led by the Consumer Financial Protection Bureau ("CFPB").

The Final Rule became effective on October 1, 2015, and compliance is required by October 3, 2016. Compliance with the rules for credit cards, however, is delayed until October 3, 2017.

As initially implemented in 2007, the MLA (among other things):

- Limited the APR (including fees) for covered products to 36 percent;
- Required certain military-specific written and oral disclosures, and;
- Prohibited creditors from requiring a service member to submit to arbitration in the event of a dispute.

It also initially applied to three narrowly-defined "consumer credit" products:

- Closed-end payday loans;
- Closed-end vehicle title loans; and
- Closed-end tax refund anticipation loans.

Now there are several key changes under the Final Rule:

First, the definition of "consumer credit" covered by the regulation was expanded to more closely align with the definition of credit in the TILA and Regulation Z. This means MLA now covers a large group of creditors, and a much more wide range of credit transactions.

The Final Rule defines "creditor" as an entity or person engaged in the business of extending consumer credit. It includes their assignees. A creditor is engaged in the business of extending consumer credit if the creditor considered by itself and together with its affiliates meets the transaction standard for a creditor under Regulation Z. See 12 CFR § 1026.2(a)(17)(v).

Unless an exception applies, the definition now encompasses any credit offered or extended to a “covered borrower” primarily for personal, family or household purposes, that is subject to a finance charge or is payable by a written agreement in more than four installments. This applies to both closed-end and open-end credit, and includes, but is not limited to, installment loans, small dollar loans, pay advance loans, boat loans, single payment loans, lines of credit, credit cards accounts, and other consumer credit transactions, including overdraft lines of credit with finance charges, per Regulation Z. See 12 CFR § 1026.4(c)(3). Only a few credit products are exempted. The Final Rule does not apply to five categories of transactions:

- A residential mortgage transaction, which is any credit transaction secured by an interest in a dwelling (A dwelling-secured transaction includes a transaction to finance a dwelling’s purchase or initial construction; a refinance transaction; a home equity loan or line of credit; and a reverse mortgage. It does not include a timeshare interest);
- A transaction expressly for financing the purchase of a motor vehicle secured by the purchased vehicle;
- A transaction expressly for financing the purchase of personal property secured by the purchased property;
- Any credit transaction that is an exempt transaction for the purposes of Regulation Z (other than a transaction exempt under 12 CFR § 1026.29, which addresses State-specific exemptions) or otherwise is not subject to disclosure requirements under Regulation Z; and
- Any transaction in which the borrower is not a covered borrower.

Under the Final Rule, the term “covered borrower” includes full-time active duty Service members and those under a call or order of more than 30 days. It also includes National Guard members pursuant to an order to full-time National Guard duty for a period of 180 consecutive days or more for the purpose of organizing, administering, recruiting, instructing, or training the reserve components, as well as members of a reserve component of the Army, Navy, Air Force, or Marine Corps. The Final Rule also protects a covered Service member’s dependents. The Final Rule defines “dependent” by reference to subparagraphs (A), (D), (E), and (I) of 10 U.S.C. § 1072(2). Although that provision refers to dependents of former members, 12 CFR § 232.3(g)(4) provides that the term “covered borrower” does not include dependents of a consumer who no longer is a covered member of the armed forces.

Under the Final Rule, “dependents” are:

- A Service member’s spouse;
- A Service member’s child who is under the age of 21 or meets certain other conditions;
- A Service member’s parent or parent-in-law residing in the Service member’s household who is (or was, at the time of the Service member’s death, if applicable) dependent on the Service member for more than one-half his or her support; and
- An unmarried person who is not a dependent of a member under any other subparagraph over whom the Service member has custody by court order and who meets certain other conditions.

Second, one of the most significant and challenging changes is the calculation of the Military Annual Percentage Rate (“MAPR”). Under the MLA, covered credit transactions are capped at a 36% MAPR. The rules controlling how to determine what must be included in the MAPR are very detailed, with a distinct section for credit cards. Briefly, the MAPR covers all interest and fees associated with the loan, and now must also include charges for most ancillary or “add-on” products such as credit default insurance

and debt suspension plans. For closed-end credit, the MAPR will be a one-time calculation made prior to or at the time the loan is made. For open-end credit transactions, the MAPR must be calculated for each billing cycle. With this change, ancillary product fees can quickly exceed the 36% MAPR limit.

The Final Rule excludes from the finance charge used for the MAPR an application fee imposed in connection with a short-term, small amount loan extended under certain conditions. The exclusion applies once in a rolling twelve-month period. See 12 CFR § 701.21(c)(7)(iii).

The Final Rule maintains the current rule's restriction on using allotments to repay credit; using pre-dispute mandatory arbitration agreements for covered transactions; requiring waivers of Servicemembers Civil Relief Act ("SCRA") protections; and using burdensome legal notice requirements. See 50 U.S.C. App. §§ 501-597b.

Finally, the Final Rule implements MLA provisions prescribing penalties and remedies and providing for administrative enforcement for violations. A person who violates the MLA is civilly liable for any actual damages, with a \$500 minimum per violation; "appropriate" punitive damages; "appropriate" equitable or declaratory relief; and any other relief provided by law. The person is liable for the costs of the action, including attorneys' fees, with an exception if the action was filed in bad faith and for the purpose of harassment. Creditors who make mistakes resulting from some bona fide errors may be relieved from liability. The Final Rule provides for administrative enforcement the same as under TILA.

Third, creditors need to screen each and every applicant who applies for any credit product (that is covered under the MLA) to confirm they are not an active duty service members, or a spouse, or dependent of an active duty service member. Previously, creditors could simply ask applicants this information. But under the revised Final Rule, creditors are only granted legal "safe harbor" from liability if they employ one of two methods for conducting a covered-borrower check: (1) access the DoD's database (the Defense Manpower Data Center, database known as the "DMDC"), which details active duty status; or (2) obtain active duty status information in within a consumer report, accessed from a nationwide consumer reporting agency ("CRA"). The Final Rule also permits the consumer report to be obtained from a "reseller" that obtains such a report from a CRA. MLA status for dependents under the age of 18 must be verified directly with the DMDC.

This document is intended to provide general information about the Final Rule, but only a detailed review of the Final Rule, and consultation with your own legal counsel, can provide comprehensive and definitive information regarding its requirements. Citations provided reflect 32 CFR Part 232 as amended effective October 1, 2015.
