

SPECIAL REPORT

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Military Lending Act Proposed Rulemaking

by Gina Carter, Marci Kowski and Jack Carver

On Sept. 29, 2014, the U.S. Department of Defense (DoD) proposed a new rule that would significantly expand the Military Lending Act (MLA), with potentially significant consequences for credit unions and other financial institutions that offer credit to service members and their dependents.¹ Comments for the proposed rule are due Nov. 28, 2014.

MLA Today

MLA is a regulation promulgated by the DoD to protect service members and their dependents from predatory or unfair lending practices. Concerned that lenders were violating the spirit of the regulation in their attempts to circumvent MLA in their dealings with service members and their dependents, the DoD has proposed a significant expansion of the regulation to offer greater protection.

Changes to MLA Limit on APR

The primary change of the proposed regulations is the expansion of the existing MLA annual percentage rate (APR) limit of 36% to far more types of credit that credit unions may offer to service members and their dependents. In its current form, MLA's limit on APR applies only to three specific "closed end" transactions: payday loans with a term of 91 days or fewer in which the amount financed does not exceed \$2,000, closed-end vehicle title loans with a term of 181 days or fewer, and closed-end tax refund anticipation loans. If the proposed regulations are enacted, however, this limit would also

apply to *all* forms of payday loans, vehicle title loans, refund anticipation loans, deposit advance loans, installment loans, unsecured open-end lines of credit, and credit cards. The new regulation will not, however, include mortgage loans.

APR measurement under MLA is different from that under the Truth in Lending Act and other traditional calculations of APR, because MLA mandates that many fees and charges normally excluded from APR must be included in its calculation. Example of fees that must be included in the 36% calculation include: fees for "credit-related ancillary products" that are sold in connection with the credit transaction, application fees and annual fees, finance charges "associated with" the credit offered, credit insurance premiums, and fees for debt cancellation or debt suspension agreements. As a result, if these products are sold, the actual interest rate that may be charged will be substantially reduced.

Special Changes for Credit Cards

Acknowledging that "imposing the [MLA 36% APR limitation] on credit card products likely would result in dramatic changes to the terms, conditions, and availability" of credit cards to service members and their dependents, the DoD proposed special rules for calculating the effective interest rate on credit cards. The proposed rules allow that any reasonable "bona fide" fees charged by credit card providers may be excluded from the 36% calculation. Although the proposed rule envisions a "flexibly adaptable standard," it offers a safe harbor provision for credit card providers to meet the bona fide standard by



Credit Union Law Team Members

Gina Carter
Team Leader

Brian D. Anderson
Benjamin P. Brunette
Gretchen E. Cleveland
Daniel W. Gentges
Melinda S. Giftos
Thomas P. Godar
Frank A. Gumina
Edward J. Heiser
Tiffany L. Hutchens
Jerard J. Jensen
Marci V. Kowski
Lisa R. Lange
Daniel J. McGarry
Kenneth R. Nowakowski
Arthur T. Phillips
Melissa C. Selinger
Michael W. Taibleson
Kim Marie Wynn

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¹ Limitations on Terms of Consumer Credit Extended to Service Members and Dependents, 79 Fed. Reg. 58,602 (Sept. 29, 2014).

comparing the fees they charge with similar fees charged by “five credit card issuers, each of whom meet the threshold of \$3 billion in outstanding credit card loans.”

Other Significant Impacts of the Proposed Rule

In addition to the expansion of the interest limit cap, there are other facets of the proposed rule that, if enacted, will present credit unions and other lenders with new challenges. Principal among these are the revisions to the requirement that lenders use appropriate methods to discern whether any potential borrower is a covered borrower under MLA. Although this requirement exists under MLA in its current form, it would be expanded to cover all forms of credit potentially covered under the new rule, and lenders would no longer be able to merely rely on certifications from borrowers that they are not covered by MLA. The DoD offers the “MLA Database,” which lists all covered borrowers, as a means to conclusively establish whether a borrower is covered, but the database has proved cumbersome for many in the industry.

Other MLA requirements in addition to the APR limit would be expanded to the new forms of credit covered by the proposed rule. This means that for

all forms of credit the DoD has proposed to have covered by the revised rule, credit unions and other lenders offering credit to service members will be prohibited from requiring arbitration and prepayment penalties, and will be required to deliver special disclosures before consummation of the transaction.

The Future Under the Proposed Rule

These proposed changes, if enacted, would increase significantly the risk of litigation associated with lending to service members or their dependents. If the revisions are enacted, they would create by virtue of the 2013 MLA amendments that established a new civil liability provision allowing private rights of actions for MLA violations, a regulation with far greater scope and increased consequences for non-compliance.

For more information, please contact Credit Union Law Team leader Gina Carter at (608) 234-6058 or gcarter@whdlaw.com, or Consumer Financial Services Team member Marci Kawski at (608) 234-6051 or mkawski@whdlaw.com.



Whyte Hirschboeck Dudek S.C.

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MILWAUKEE OFFICE

555 East Wells Street, Suite 1900
Milwaukee, WI 53202-3819
414.273.2100

MADISON OFFICE

33 East Main Street, Suite 300
P.O. Box 1379
Madison, WI 53701-1379
608.255.4440

CHICAGO OFFICE

161 North Clark Street
Suite 4700
Chicago, IL 60601-3206
312.523.2080

www.whdlaw.com