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PROPOSED RULE TO EXPAND CREDIT PRODUCTS SUBJECT TO MILITARY LENDING ACT

The Department of Defense ("DoD") has issued a proposed regulation to extend the credit products covered by the Military Lending Act ("MLA") and the DoD's implementing regulation. The DoD has proposed that the definition of "consumer credit" under the MLA track the federal Truth in Lending Act's definition of "consumer credit." "Consumer credit" means credit extended to a covered borrower primarily for personal, family or household purposes and that is subject to a finance charge or payable by written agreement in more than four installments. Under the proposed rule, the MLA would extend existing regulation to long-term payday loans, consumer installment loans, credit cards and other open-end credit products offered to covered borrowers.

Currently, the DoD's regulations apply only to (i) payday loans with a term of 91 days or less and an amount financed that does not exceed \$2,000, (ii) vehicle title loans with a term of 181 days or less and (iii) refund anticipation loans. The regulations exclude from the definition of "consumer credit" residential mortgages, credit to purchase a motor vehicle, credit to purchase personal property when the credit is secured by the property and any credit products exempted under Regulation Z except for the state-requested exemption. The DoD's proposed regulations would not alter the existing exemptions.

The MLA and its implementing regulations give "covered borrowers" certain protections in "consumer credit" transactions. "Covered borrowers" means at the time the consumer becomes obligated on a consumer credit transaction the consumer is (i) a regular or reserve member of the armed forces, serving on active duty under a call or order that does not specify a period of 30 days or fewer, or such a member serving on active guard and reserve duty or (ii) the member's spouse, the member's child or an individual for whom the member provided more than one-half of the individual's support for 180 days immediately preceding an extension of consumer credit. The protections for "covered borrowers" include (i) a 36% Military Annual Percentage Rate ("MAPR") limitation; (ii) required oral and written pre-consummation disclosures; and (iii) prohibitions on certain contracts terms, including mandatory arbitration clauses, a waiver of rights clause or pre-payment

penalties. The proposed rule would require creditors to provide these protections to covered borrowers on a wider array of credit products and would amend the content of the mandatory pre-consummation disclosure.

The DoD has included two revisions in the proposed rule that purportedly benefit creditors: First, the proposed rule contains a safe harbor from liability for creditors who unilaterally verify whether a borrower is a "covered borrower" in the DoD's publicly available online MLA Database. The MLA Database safe harbor would replace the covered borrower identification statement that a creditor must give to an applicant to indicate whether he or she is a covered borrower. Second, credit card issuers would be able to exclude bona fide, reasonable and customary fees that represent costs tied to specific products or services for credit card accounts from the MAPR. The proposed rule offered a foreign transaction fee as an example of the type of fee that would be excluded from the MAPR under the proposed rule. The proposed rule allows a creditor to prove that a fee is reasonable by comparing the amount of the bona fide fee to an average amount for a substantially similar fee charged by 5 or more creditors each with at least \$3 billion in outstanding loans on U.S. credit card accounts at any time during the 3-year period preceding the time such average is computed.

By issuing the proposed rule, the DoD aims to close "loopholes" in the MLA's regulations while creating a system that the DoD hopes does not unduly impede the availability of credit to servicemembers. The MLA empowers the DoD to issue implementing regulations but gives other federal agencies enforcement powers.

Expansion of the MLA could have broad implications, not solely for servicemembers and their dependents, but also for non-covered borrowers. The proposed rule raises not only practical operational concerns but also concerns regarding the ability to offer products where discrimination between covered borrowers and non-covered borrowers is prohibited. The inclusive 36% MAPR raises issues of indirect rate regulation that may have serious implications for the availability of credit for subprime and other non-prime customers.

The DoD posed 26 specific questions to the public in the proposed rule. The comment period for the proposed rule ends November 28, 2014. □

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