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# Department of Defense Military Lending Act

## Summary of Amended Regulations (Final Rule)



Common Purpose. Uncommon Commitment.

Revised May 4, 2016

In 2007, Congress passed the Military Lending Act (MLA), which was designed in part to address predatory lending practices with military members and their dependents. The Department of Defense (DoD) initially published regulations implementing the MLA that applied only to three types of consumer credit: (1) closed-end payday loans for less than 91 days and less than \$2,000, (2) closed-end vehicle title loans with terms of 181 days or less, and (3) closed-end tax refund anticipation loans.

Among other requirements, a creditor could not charge a military annual percentage rate (MAPR) that exceeded 36%. Importantly, the MAPR was broader than the annual percentage rate (APR) under Regulation Z because the MAPR included costs that were not included in the APR. Based on this narrow scope of products, many credit unions were not impacted by the MLA.

On July 22, 2015, the DoD amended its regulations to expand the scope of credit transactions covered under the MLA and impose various additional obligations on credit unions (Final Rule). The Final Rule generally applies to all consumer credit transactions that are subject to Regulation Z, except: (1) purchase money credit that is secured by a vehicle or personal property, (2) residential mortgages, and (3) commercial transactions.

If the Final Rule applies to the credit transaction, a credit union will have to take various steps to ensure compliance, including:

- Determining whether the applicant(s) are protected by the Final Rule;
- Ensuring that the credit union does not charge a MAPR that exceeds 36%; and
- Providing various disclosures and complying with other lending limitations.

The DoD expanded the Final Rule to include new types of credit and to include fees/premium for credit-related add-on products sold in connection with the credit transaction in the MAPR. However, nothing in the Final Rule prohibits the sale of payment protection products as long as the MAPR does not exceed 36%.

### **When do credit unions have to comply with the Final Rule?**

While the Final Rule was effective on October 1, 2015, credit unions generally must comply with the Final Rule by October 3, 2016, for all credit transactions except credit cards. For credit cards, compliance is required by October 3, 2017.

### **Which members are covered by the Final Rule?**

The Final Rule covers members of the armed forces who are on active duty at the time credit is extended, and dependents of members of the armed forces who are on active duty at the time credit is extended.

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The Final Rule provides two safe harbor methods for credit unions to determine if a member is covered by the Final Rule:

- (1) the credit union relies on information from the DoD's database (<https://mla.dmdc.osd.mil>) (or
- (2) the credit union relies on information in a consumer report obtained from a nationwide consumer reporting agency meeting certain criteria.

The credit union must maintain appropriate records to receive the safe harbor.

### **Is my credit union required to ask all members if they are a military family and/or ask for documentation up front?**

The Final Rule applies broadly to creditors, including a credit union that is engaged in the business of extending consumer credit. Thus credit unions should incorporate in their lending process a method that will ensure compliance with the Final Rule. To do so, the Final Rule does not restrict a credit union's ability to determine if a member is a Covered Borrower; a credit union can create its own method. The safest way to ensure compliance is following one of the two safe harbor methods detailed in the Final Rule, in section 232.5(b).

Under the safe harbor, a credit union does not have to ask the borrower for any information. The credit union can rely upon information obtained from the DoD database or a consumer reporting agency.

This requirement is a one-time obligation for each specific transaction; there is no ongoing requirement to monitor whether the member becomes a covered borrower. However, you must re-verify covered borrower status for each new loan.

### **What should my credit union be looking at on the report produced by a consumer reporting agency?**

The Final Rule provides a safe harbor presumption of compliance if the creditor obtains the nationwide consumer reporting agency's report on the applicant, reviews the report for any status, code or indicator that the applicant is a covered borrower, and documents within its records that these steps were taken. Our impression is that the consumer reporting agencies will update their systems by the Final Rule's mandatory compliance date of October 3, 2016, to contain the necessary information, but we are not able to speak for the nationwide consumer reporting agencies.

### **What is included in MAPR?**

The MAPR generally is calculated the same way as the APR (for closed-end credit) and the effective APR (for open-end credit) under Regulation Z, but the MAPR includes charges that would be excluded from the APR, such as credit insurance premiums, debt cancellation or suspension fees and certain application and participation fees. The MAPR contains detailed and complex exceptions for application fees and "bona fide" fees for certain credit card accounts.

### **How does the Final Rule impact a firm offer of credit?**

The Final Rules applies to credit transactions that are originated from a firm offer of credit. To determine if a member is covered by the Final Rule, the credit union must develop or process a firm offer of credit that (among the criteria used by the credit union for the offer) includes the status of the member as a covered borrower. The credit union may rely on this determination only if the member responds to the offer within 60 days. If the member responds to the offer later than 60 days, then the credit union may not rely upon the initial determination. Instead, the credit union must re-check to determine if the member is a covered member and protected by the Final Rule.

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### **Does the Final Rule apply to all types of credit?**

The Final Rule does not apply to all types of credit. Please note that the Final Rule does not apply to purchase money credit that is secured by a vehicle or personal property being purchased (it would apply, though, to a refinance transaction and to non-purchase money credit). The Final Rule also does not apply to credit secured by a dwelling.

### **Are CUNA Mutual Group's Credit Insurance, Debt Protection, Guaranteed Asset Protection and Mechanical Repair Coverage products included in the MAPR?**

A credit union must initially determine what type of credit it is extending. If a credit union is extending credit covered by the Final Rule, the following will apply:

Credit Insurance, Debt Protection, and Guaranteed Asset Protection: The Final Rule clearly requires a credit union to include these in the MAPR.

Mechanical Repair Coverage: The Final Rule provides that the MAPR must include "any fee for a credit-related ancillary product sold in connection with the credit transaction." Unfortunately, the Final Rule does not clearly define or otherwise explain what is included in this definition. While there is ambiguity, the safest approach would be to include the cost of the Mechanical Repair Contract in the MAPR.

### **Which disclosures must a credit union provide?**

The Final Rule does not require the credit union to disclose the specific, numeric MAPR. The credit union must provide the following general, written disclosure regarding the MAPR:

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).

A credit union also must give this disclosure orally or provide a toll-free number on the application form or in a written disclosure which a covered borrower may call to obtain the oral disclosure.

### **Does the MAPR impact a credit union's data processor and/or Loan Origination System?**

A credit union's data processor and/or Loan Origination System will need to be able to calculate the MAPR. CUNA Mutual Group will be available to work with your credit union's system provider to answer questions they may have about the MAPR.

### **What share may our credit union take a security interest in?**

The DOD's final rule restricts the security interest in a covered borrower's shares to only those shares that are deposited into an account that was opened in connection with the consumer credit transaction, and deposited after the extension of

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credit is made. Credit unions may not take a security interest in all of the covered borrower's shares to secure a loan subject to the Military Lending Act.

**Can we add a Military Lending Act disclosure statement to our normal loan agreement?**

Credit unions should carefully analyze their strategy for MLA compliance, including the documentation that will be used for loans covered by MLA. Providing the required MLA disclosures is one aspect of complying with the rule, but there are many other factors to consider. Several types of contract terms are prohibited by the rule, including taking a broad security interest in all of the borrower's shares in the credit union. For this reason, you may be unable to use your standard loan agreements with an added MLA disclosure statement for your MLA-covered loans. The consequences for violating the Act are severe, including a voided loan agreement, fines, punitive damages, civil liability, and potentially imprisonment. These consequences apply regardless of how the rule is violated. If the loan agreement contains a prohibited term, if the MAPR disclosure statement is not provided, or if the MAPR exceeds 36%, the same consequences apply.

**If the MAPR exceeds 36% what are our options?**

The preamble to the DOD final rule states that for open-end credit, if the MAPR exceeds 36% for a given billing cycle, the credit union may choose to waive fees for that billing cycle to bring the MAPR below 36%. The rule does not provide other examples and does not specifically address closed-end credit. Several groups have requested additional guidance from DOD on this topic.

**Do we have to provide the specific MAPR number to the member?**

No, the final rule does not require the credit union to provide the covered borrower with the numeric Military Annual Percentage Rate that applies to the transaction. Instead, the model statement regarding the MAPR must be provided before or at the time the covered borrower becomes obligated on the transaction.

**How is the Military Lending Act different from the Servicemembers Civil Relief Act?**

The Military Lending Act and the Servicemembers Civil Relief Act are two separate laws with separate compliance requirements. The Military Lending Act applies to loans that are granted while the borrower is on active duty, or is a dependent of a person who is on active duty. In contrast, the Servicemembers Civil Relief Act applies to loans that were granted before the borrower entered active duty service. The two Acts also provide different protections to borrowers, and they should be viewed as two entirely separate sets of compliance requirements.

**Does the toll-free number have to be dedicated to providing MLA oral disclosures?**

No. The credit union may provide its general toll-free number on the application or disclosure statement and comply with the Military Lending Act oral disclosure requirement. The toll-free number is not required to be dedicated solely to MLA compliance.

**What are the penalties for failing to comply?**

Failing to comply with the MLA can lead to significant penalties including fines and imprisonment, the credit agreement, note, or other contract is void from inception, and civil liability including punitive damages and attorneys' fees.

**What if I have more questions?**

We understand your credit union may have additional questions over the coming months regarding the impact of the Final Rule. For questions, please contact us at [dodmla@cunamutual.com](mailto:dodmla@cunamutual.com).