

# **Lending to Military Members: The Servicemembers Civil Relief Act and Military Lending Act Final Rule**

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# Servicemembers Civil Relief Act (“SCRA”), 50 U.S.C. App. §§ 501, et seq., Overview

- **Purpose:** Protect servicemembers and enable them to devote their entire energy to the defense needs of the United States.
- **Protections:** The SCRA gives servicemembers relief from obligations and liabilities they may have incurred prior to entering active military service.

# What Does the SCRA Govern?

- Consumer Credit Transactions
  - Mortgages, retail installment contracts (RICs), loans, leases
- Default judgments
- Rental agreements
- Telephone service contracts
- Storage units
- Insurance
- Taxes



# Who is Protected by the SCRA?

- **Servicemembers**
  - A member of the Armed Forces, which include all members of the Army, Navy, Air Force, Marine Corps, and Coast Guard
- **Reservists Called to Military Service**
  - Upon receipt of written orders to report for military service
- **Certain Other Individuals**
  - Servicemember's Co-borrowers
  - Servicemember's Dependents
  - All Commissioned Officers on active service with the Public Health Service or National Oceanic and Atmospheric Administration
  - U.S. Citizen serving with allied forces

# Active Duty Military Service

- **The SCRA's protections generally only apply to servicemembers on active duty military service**
- **What is active duty military service?**
  - Armed Forces: Active duty means full-time duty in the active military service of the United States, and includes annual training duty
  - National Guard: Service under a call to active service for a period of more than 30 consecutive days for purposes of responding to a national emergency declared by the President (a call under Title 32)
    - If a member of the National Guard is called to full time active duty (a call under Title 10), they are treated like any other active duty servicemember

# Determining Active Duty Status

- A creditor should review and maintain the servicemember's records, which may be obtained from the Secretary of Defense at the Defense Manpower Data Center ("DMDC")
  - DMDC is maintained by the Secretary of Defense in part to enable creditors to easily ascertain whether a borrower is a servicemember on active duty military service or has been called to military service

# Examples of SCRA's Protections for Servicemembers

- (1) Reduction of interest rate to 6%
- (2) Protections from default judgment
- (3) Protection from extra-judicial collection of judgments
- (4) Stay of judicial proceedings
- (5) Protections against repossessions
- (6) Protections from eviction
- (7) Allowance of residential lease terminations
- (8) Allowance of vehicle lease terminations
- (9) Allowance of cellular telephone contract terminations
- (10) Mortgage foreclosure protections

# SCRA Protections Relevant to Banks

- **Interest Rate Reduction to 6%**

- Servicemembers have the right to have their creditor reduce the rate of interest for any obligation bearing interest at a rate in excess of 6% per year, which was incurred by a servicemember before the servicemember entered military service, to a maximum rate of interest of 6%
- The servicemember must affirmatively apply for the rate reduction by providing a written notification of his or her active duty service and a copy of his or her military orders



# SCRA Protections Relevant to Banks (cont'd)

- **Default Judgment Prohibitions**

- 1) **Affidavit Requirement**

- Must inform the court whether debtor is in military service

- 2) **Right to a Stay of the Proceedings**

- 90 day stay for active duty servicemembers
- No fees or charges may accrue during the stay

- 3) **Right to Vacate or Set Aside Default Judgments**

- Courts may also stay the execution of any judgment or order entered against the servicemember, or vacate or stay an attachment or garnishment of the servicemember's property or money or any debts owed to the servicemember

# SCRA Protections Relevant to Banks (cont'd)

- **Allowance of Motor Vehicle Lease Terminations**
  - A servicemember who is a lessee on a covered lease may terminate the lease at any time after:
    - The lessee's entry into military service; or
    - The date of the lessee's military orders

# SCRA Protections Relevant to Banks (cont'd)

- **Protections against Repossession / Foreclosure**
  - Once a servicemember enters military service, a breach of contract occurring before or during the period of military service may not be the basis for:
    - 1) The rescission of the contract
    - 2) The termination of the contract
    - 3) The repossession or foreclosure of the collateral without a court order
  - This prohibition applies to any contract for the purchase or lease of real or personal property

# Major SCRA Consent Orders

- Capital One, N.A.
- Bank of America, N.A.
- Sallie Mae Bank

# Capital One, N.A. Consent Order

- The DoJ alleged SCRA violations including:
  - Wrongful foreclosures
    - \$125,000 penalty for each wrongful foreclosure
  - Wrongful repossessions
    - \$10,000 penalty for each wrongful repossession
  - Default judgments without disclosure of servicemember status
  - Improper denials of the 6% interest limitation
  - Insufficient granting of rate reductions to 6%
    - \$5,000,000 fund for rate reduction violations

# Capital One, N.A. Consent Order

- Assignee liability
  - Capital One purchased portfolios of RICs in which some accounts involved repossessions conducted by the portfolio seller prior to the sale
  - The DoJ required Capital One to pay \$10,000 for each of these accounts even though Capital One did not conduct the repossession
- Inadequate SCRA Policies and Procedures
  - Must search DMDC and reduce rate to 6% even if servicemember failed to provide orders

# Bank of America, N.A.

## Consent Order

- The OCC alleged SCRA violations including:
  - Failure to provide rate reduction to 6% when service-members provide written evidence of active duty.
  - Wrongful repossessions
  - Improper litigation practices related to default judgments
    - Improper procedures for filing and notarizing affidavits
  - Inadequate SCRA policies and procedures

# Bank of America, N.A. Consent Order (cont'd)

- The remedies included:
  - Mandated improvements to each aspect of BoA's SCRA compliance systems to ensure that:
    - Default judgments are compliant with the SCRA,
    - Servicemembers' property is not repossessed or foreclosed upon in violation of the SCRA, and
    - Rate reductions are calculated properly to 6%.
  - In addition to various remediation and compliance requirements, BoA was also subjected to a \$30 million civil money penalty.



# Sallie Mae Bank Consent Order

- Resulted from an FDIC examination of the Bank's compliance with the SCRA and a companion investigation by the DoJ related to the treatment of servicemembers
- FDIC and DoJ alleged that the Bank:
  - Failed to sufficiently notify servicemembers regarding their SCRA eligibility
  - Failed to provide complete SCRA relief to servicemembers after having been put on notice of these borrowers' active duty status

# Sallie Mae Bank

## Consent Order (cont'd)

- The remedies included:
  - Civil money penalties totaling \$6.6 million
  - Restitution of approximately \$30 million to harmed borrowers
  - \$60 million settlement fund with the DOJ to provide remediation to servicemembers.
    - The DOJ also took separate action against the entities with regard to violations of the SCRA
  - The Bank must also take affirmative steps to ensure that servicemembers are properly treated under the SCRA

# SCRA Enforcement Action Take Aways

- You must have a thorough SCRA compliance management system with detailed policies and procedures ensuring compliance
- The DoJ's points of emphasis appear to be complaint driven and focus on:
  - (1) Default judgments
  - (2) Proper reduction of the rate to 6%
  - (3) Proper repossessions
  - (4) Proper foreclosures
  - (5) Assignee collection of accounts where the assignor committed an SCRA violation

# The Military Lending Act

- The Department of Defense has issued a final rule modifying how the Military Lending Act (“MLA”) is implemented
  - Expansion of scope
  - New substantive requirements
  - New safe harbor protection

# MLA Scope

- The Military Lending Act currently covers only certain types of loans
  - Closed-end payday loans of 91 days or less with amount financed of \$2,000 or less;
  - Closed-end vehicle title loans with a term of 181 days or less; and
  - Closed-end tax refund anticipation loans.

# MLA Scope (cont'd)

- MLA will soon cover:
  - All payday loans
  - Motor vehicle title loans
  - Tax refund anticipation loans
  - Deposit advance loans

# MLA Scope (cont'd)

- MLA will soon cover:
  - Installment Loans subject to TILA
    - Excludes residential mortgage loans and purchase money loans for motor vehicles and personal property
    - Includes non-purchase money motor vehicle secured loans and refinancing loans of purchase money motor vehicle secured loans
  - Unsecured Open-End Lines of Credit (including overdraft lines of credit)
  - Credit Cards

# MLA Interest Rate Limit

- Military Annual Percentage Rate (“MAPR”) restriction limits rate to 36%; calculation includes:
  - Credit insurance premiums
    - Single and monthly premiums
  - Debt cancellation/suspension agreement fees
  - Fees for other credit-related ancillary products
  - Application fees for non-depository entities
    - Depository entity application fees are included except for certain short term, small dollar loans that may be permitted by the chartering regulator
  - Participation fees (some permitted for open-end credit)



# MLA Interest Rate Limit (cont'd)

- 36% MAPR limit calculation excludes non-enumerated charges excluded from the finance charge under TILA
  - Late charges
  - Taxes
  - Etc.

# MLA Substantive Prohibitions

- Lender cannot rollover or refinance a covered loan it previously made to the borrower
  - Banks are exempt from this prohibition
- No mandatory waiver of borrower's rights
- No mandatory arbitration
- No mandatory notice required by borrower prior to litigation
- Limits on use of checks or ACH transfers

# MLA Substantive Requirements (cont'd)

- Prohibition on the use of motor vehicle titles as security for loans by non-depository institutions
  - Effectively prohibits motor vehicle refinancing or non-purchase money loans by non-banks
  - However, banks are exempt from this prohibition
- No mandatory payment by military allotment
- Prepayment penalties are prohibited

# MLA Disclosure Requirements

- The following disclosures are required:
  - Statement of the MAPR
    - Model language
  - Regulation Z required disclosures
  - Clear description of the payment obligations of the borrower

# MLA Disclosure Requirements (cont'd)

- Creditors must provide the disclosures in both written and oral form
  - Written form must be retained by borrower
  - Oral disclosures may be provided in person or by means of a toll-free telephone number provided to the borrower for that purpose on the application form or the written disclosures

# MLA Safe Harbor

- Creditors must verify the borrower's status in one of two ways in order to be protected by the safe harbor
  - Review of MLA Database
    - The MLA database is a new database created to facilitate MLA compliance
  - Use of statement, code, or similar indicator describing military status contained in a consumer report obtained from a national credit bureau

# MLA Safe Harbor (cont'd)

- Creditors must retain records
- Creditors may not use the MLA database to conduct a “look back” to establish whether a borrower in a previous transaction was a covered borrower

# MLA Penalties

- Knowing violations up to \$200,000 and a year in prison
- Other violations give rise to:
  - Actual damages not less than \$500 per violation
  - Appropriate punitive damages and equitable or declaratory relief
  - Court costs and attorney's fees
  - Inability to recover principal or interest



# MLA Take Away

- Work with your credit bureaus to ensure the proper use of credit reports to ascertain borrower status with respect to the MLA
- Ensure that credit documents comply with the MLA substantive restrictions and disclosure requirements
- Make sure that the MAPR calculations are incorporated into product pricing