



National Association
of Federal Credit Unions
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NAFCU | Your Direct Connection to Advocacy, Education & Compliance

May 31, 2016

Marcus Beauregard

Chief, Department of Defense-State Liaison Office; Office of the Deputy Assistant Secretary of Defense for Military Community & Family Policy

Paul Kantwill

Director, Office of Legal Policy; Office of the Under Secretary of Defense for Personnel and Readiness

RE: Extension of Exemption for Consumer Credit Cards from MLA Rule Requirements

Dear Mr. Beauregard & Mr. Kantwill,

On behalf of the National Association of Federal Credit Unions (NAFCU), the only national trade association focusing exclusively on federal issues affecting the nation's federally insured credit unions, I am writing to you regarding the Military Lending Act (MLA) Final Rule's current credit card compliance deadline of October 3, 2017. Given the substantial compliance challenges of the MLA Rule, NAFCU and our members urge the Department of Defense (DoD) to proactively exercise its authority extend the exemption for credit card accounts from the requirements of the MLA Rule until at least October 3, 2018.

General Comments

Credit unions are different than most other types of financial institutions. As member-owned not-for-profit cooperatives, credit unions strive to provide their members with products and services designed to help each member achieve their individual financial goals. The relationship between a credit union and its member is based on fairness and responsible practices. As such, credit unions have a strong track record of working with active duty members of the armed forces and their families to escape the kinds of debt traps that prompted the passage of the MLA. While NAFCU and our members support the Department's goal of protecting active duty members of the armed forces and their families from financial exploitation, implementing the requirements of the MLA Rule for credit cards imposes time-consuming regulatory compliance burdens that are especially challenging for smaller, community-oriented financial institutions.

Unlike other consumer credit products, credit cards have multi-dimensional pricing structures including various fees and periodic rates, as well as other features such as rewards and benefits that must be taken into consideration when updating core systems and policies to bring them into compliance with the MLA Rule. This is particular important since the rule will require our

members to calculate an effective military annual percentage rate (MAPR) each billing cycle and re-credit fees or premiums charged in excess of the 36 percent MAPR cap set forth in the MLA and the MLA Rule. Given the unique and highly complex challenges that are specific to credit card accounts, NAFCU requests the Department grant additional time to allow our members to bring their credit card accounts into compliance with the requirements of the MLA Rule.

Background

Section 670 of the *John Warner National Defense Authorization Act* for Fiscal Year 2007,¹ also known as the MLA, establishes limits on the terms of consumer credit extended to active duty service members and their dependents (covered borrowers) and directs the Secretary of the Defense to issue regulations implementing the requirements of the MLA.

On August 31, 2007, the Department finalized a regulation placing substantive limitations on the terms of payday loans, vehicle title loans, and tax refund anticipation loans offered to covered borrower pursuant to its authority under the Act. *See*, 72 Fed. Reg. 50580 (Aug. 31, 2007). The Department made significant revisions to the MLA Rule on July 22, 2015, that expanded its scope to include most consumer credit products (covered loans) with exceptions for residential mortgages and loans expressly intended to secure the purchase of motor vehicles or personal property that are also secured by the property or vehicle being purchased. *See*, 80 Fed. Reg. 43560 (July 22, 2015). These requirements are set to be implemented on October 3, 2016.

As part of this rule, the Department established a conditional exemption for credit cards to account for potentially “dramatic changes to the terms, conditions, and availability of those products to Service members and their families.” 80 Fed. Reg. at 43572. This exemption recognized that under the MLA Rule “the typical creditor that issues a credit card would be required to revamp the fee, terms, and other conditions for that credit product when offering it to a covered borrower or, more drastically, disqualify the covered borrower from opening that credit card account.” *Id.* Therefore, the Department determined that credit cards warranted “special consideration” under the MLA and extended the expiration of the exemption for these products until October 3, 2017, leaving open the possibility of extending the expiration of the exemption up to an additional year. *Id.*

Discussion

As the implementation deadline for all other covered loans draws near, our members continue to grapple with the challenges of the rule as it applies to products that have pricing structures far less complicated than traditional, mainstream credit card accounts. Credit unions expect the process for credit cards to be even more unwieldy. Therefore, NAFCU believes that the Department should exercise its authority under 10 U.S.C. § 987(h) and 32 C.F.R. § 232.13(c)(2) to exempt credit cards from the MLA Rule for at least an additional year to allow our members to opportunity to complete the process of updating core systems and developing policies and

¹ Pub. L. No. 109-364, Tit.VI, § 670, 120 Stat. 2083, 2266-69 (Oct. 17, 2006) (codified at 10 U.S.C. § 987).

procedures for the prompt re-crediting of any premiums or fees that may exceed the 36 percent MAPR cap set forth in the MLA and the MLA Rule.

The MLA Rule requires credit unions to utilize a different calculation method for the MAPR than is used to calculate the APR which is a major undertaking that will require significant coordination with systems providers. For the first time under the MLA Rule, credit unions will be required to calculate an effective annual rate each billing cycle that includes premiums and fees that are typically excluded from the definition of “finance charge” under Regulation Z. For example, Regulation Z excludes application fees, late fees, over the limit fees, participation fees, and premiums related to insurance and debt cancellation or suspension products. *See*, 12 C.F.R. § 1026.4(c)-(d). On the other hand, the MLA Rule incorporates many of these fees back into the MAPR including credit insurance premiums, application fees, and participation fees. *See*, 32 C.F.R. § 232.4(c)(1). Even though the rule makes exceptions for certain bona fide and reasonable fees in paragraph (d) of Section 232.4, our members must still work with systems providers to account for these fees in case it is later determined that particular fees or premiums are not “bona fide” or “reasonable.”

Contrary to the explanations provided by the Department in the preamble, credit unions will not simply be able to “calculate the total charges included in the MAPR and waive an amount necessary to comply with the 36-percent limit of [Section 232.4(b)].” 80 Fed. Reg. at 43583. The Department’s chosen methodology for calculating the MAPR for open-end consumer credit plans requires credit unions to use an effective APR calculation method originally intended as an optional disclosure for home-equity lines of credit that first requires credit unions to break fees and premiums into three separate categories and apply three different formulas to arrive at an effective MAPR. The simple fact is that making such calculations is complex, involves a considerable amount of work on behalf of credit unions and their vendors and will require substantial changes to existing systems or the adoption of new systems that track not only the typical pricing features of credit cards but compare those to the outstanding monthly balance and then calculate an effective monthly MAPR.

For example, the calculation methodology for an effective monthly MAPR adopted by the Department, and imported from Section 1026.14 of Regulation Z, contemplates credit unions sorting premiums and fees into periodic rates, minimum or fixed charges, and transaction charges. This alone requires credit unions to, for the first time, develop procedures to sort fees into separate categories and program systems to apply the different calculation methodologies outlined in paragraphs (c)(1) through (3) of Section 1026.14 of Regulation Z. While this may seem simple enough when done on an individual account basis, as the Department did in the example it provided in the preamble to the final rule, developing systems and procedures to accomplish this on an aggregate basis across all consumer credit accounts held by covered borrowers is a significant and time-consuming regulatory compliance burden.

Due to the difficulty of calculating a MAPR for each billing cycle combined with the Department’s “all-inclusive” approach to the MAPR, credit unions could unintentionally hit the 36-percent MAPR cap and be required to re-credit fees or premiums under the MLA rule. NAFCU is concerned that extensive and complex credit card MAPR calculations and the

requirement to re-credit premiums or fees charged in excess of the 36 percent MAPR cap may impact the flexibility of credit unions to charge similar fees in subsequent billing cycles. While neither the Credit CARD Act nor Regulation Z prohibit credit unions from decreasing or rebating premiums or fees charged to covered borrowers, both the Act and Regulation Z have restrictions on credit unions resuming rates or fees following a temporary reduction of those charges. As a general rule, Section 1026.55 of Regulation Z prohibits creditors for increasing an annual percentage rate or a fee or charge on a consumer credit card account unless an exception applies. The Official Interpretations to Regulation Z issued by the Consumer Financial Protection Bureau (CFPB) clarify that the resumption of original rates or fees following a temporary reduction of those charges is considered a rate or fee increase and is subject to the restrictions in Section 1026.55. *See* Official Interpretations, §§ 1026.9(c)(2)(v)-2.ii, 1026.55(b)-3. This means that the MLA Rule may inadvertently foreclose the ability of credit unions to resume fees in subsequent billing cycles without first complying with the requirements in Regulation Z. Delaying the ability of credit unions to resume the original fee structure of a consumer credit card account could impose additional costs on credit unions with little offsetting benefit to covered borrowers.

Given the potential unintended consequences of the MLA Rule, NAFCU also believes that extending the deadline for credit card accounts to comply with the MLA Rule is warranted to allow the Department additional time to consider the consequences of the MLA Rule for consumer credit card accounts and to consider possible regulatory solutions to this issue. At present, the MLA Rule could potentially lead to dramatic changes to the terms, conditions, and availability of consumer credit cards offered to covered borrowers since credit unions will be required to reconsider fees, terms, and other conditions not only in light of the requirements of the MLA Rule, but also in light of the restrictions on fee increases in Regulation Z.

Conclusion

While NAFCU and our members recognize the important protections in the MLA and the MLA Rule, we request that the Department extend the exemption for credit card accounts until at least October 3, 2018 to allow additional time to address the unique complexities associated with consumer credit card accounts. Many of the changes required to bring credit cards into compliance with the rule require major undertakings on the part of credit unions and their vendors to overhaul systems to account for new and complicated monitoring requirements.

Should you have any questions or if you would like to discuss these issues further, please feel free to contact me by telephone at (703) 842-2244 or amonterrubio@nafcu.org, or Benjamin Litchfield, Regulatory Compliance Counsel at (703) 842-2241 or blitchfield@nafcu.org.

Sincerely,



Alexander Monterrubio
Director of Regulatory Affairs