



Report: Enhancement of Protections on Consumer Credit for Members of the Armed Forces and Their Dependents

April 2014

CAPE Cost Estimate: \$111,000

EXECUTIVE SUMMARY

As requested in the House Report 112-705, page 783, accompanying H.R. 4319, the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2013, DoD was asked "...to determine if changes to rules implementing section 987 [the Military Lending Act (MLA)] are necessary to protect covered borrowers from continuing and evolving predatory lending practices." Bottom line: through DoD's research and consultation with DoD financial counselors and legal assistance attorneys, industry, advocacy groups, and Service members and families, the definitions of credit in the implementing regulation for the MLA do need to be updated and expanded to ensure that the MLA continues to provide protections to Service members and their families. However, specific definitions of problematic credit no longer appear to function well in the current marketplace. The complexity of the marketplace appears to be better accommodated with a more comprehensive approach. Accordingly, the Department is working on such a comprehensive approach in its redrafting of the implementing regulation for the MLA.

A Defense Manpower Data Center QuickCompass survey shows that 11% of enlisted Service members reported using payday loans, vehicle title loans, bank deposit advances, pawn shops and/or installment loans with interest rates over 36% APR. The results of the DMDC QuickCompass tends to indicate that most Service members report sufficient access to safe, low-cost credit, report few problems managing their finances, and report little use of or impact by high-cost credit products on their financial lives. Nevertheless, the DMDC survey results also tend to indicate that a substantial minority of Service members continue to report difficulty managing their finances, and little access to safe, low-cost credit options.

Many of the DoD financial counselors and legal assistance attorneys who responded to a DoD questionnaire said high cost of credit was often a major factor contributing to problems experienced by their clients. When asked about applying a 36% APR cap more generally, the overwhelming majority said that the loss of access to credit above that threshold would not be detrimental. Additionally, the broad consensus of respondents of the Advance Notice of Proposed Rulemaking (ANPR) is that the protections afforded to Service members and their families under the MLA are important and should be continued. Representatives of the financial industries believe the current regulation adequately defines problematic credit. The 45 consumer advocacy groups that responded to the DoD ANPR unanimously said that DoD should expand the definitions in the implementing regulation to cover high cost forms of credit currently exempt for the limitations of the Military Lending Act (MLA), and this position was also supported by all respondents from state governments and the U.S. Congress.

DoD wants Service members to be in charge of their financial matters, but as they develop financial acumen, DoD also wants them to choose behavior that will not hinder their financial future. DoD sees the limitations provided by the MLA as essential for directing Service members away from continued use of high cost products.

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REQUIREMENT

The Armed Services Committees of the 112th Congress considered several amendments to the MLA, 10 USC Section 987. The Senate Armed Services Committee had approved additional amendments to the MLA in its version of the NDAA, however, these amendments were not included in the House version. The Conference Committee determined that the Department of Defense (DoD) should conduct research to determine what credit products should be included in a revision to the regulation and how to appropriately define these products. The House Report 112-705, page 783, accompanying H.R. 4319, the NDAA for FY 2013, included the following:

Enhancement of protections on consumer credit for members of the armed forces and their dependents

The conferees are concerned that the Department must remain vigilant to eliminate continuing, evolving predatory lending practices targeting service members and their families, and believe the Department should review its regulations implementing section 987, to address changes in the industry and the evolution of lending products offered since 2007, continuing use of predatory marketing practices, and other abuses identified by consumer protection advocates, including the Consumer Financial Protection Bureau's Office of Servicemember Affairs.

The conferees direct the Secretary to conduct surveys of counselors, legal assistance attorneys, service members, and other appropriate personnel, and to consult with both consumer protection advocacy groups and representatives of the financial services industry to determine if changes to rules implementing section 987 are necessary to protect covered borrowers from continuing and evolving predatory lending practices, and to report to the Committees on Armed Services of the Senate and House of Representatives no later than 1 year after the date of enactment of this Act on the results of such review.

INTRODUCTION

In August 2006, the Department of Defense (DoD) submitted a report to Congress in response to the request for information on the impact of credit practices on the financial wellbeing of Service members and their dependents. DoD articulated the importance of financial readiness to the DoD mission, reviewed concerns raised by financial counselors and legal assistance attorneys within DoD, and provided available information on credit products, Service member use of these products, financial education programs, and availability of reasonably priced small-dollar loan products. This report will provides an update on these topics.

DOD PERSPECTIVE ON FINANCIAL STABILITY

The Department makes a significant investment in recruiting, training and progressing highly qualified Service members. The Department expects these Service members to maintain personal readiness standards, including paying their debts and maintaining their ability to attend to the financial needs of their families.¹ Losing qualified Service members due to personal issues, such as financial instability, causes loss of mission capability and drives significant replacement costs. The Department estimates that each separation costs the Department \$57,333.² Losing an experienced mid-grade noncommissioned officer (NCO), who may be in a leadership position or key technical position, may be considerably more expensive in terms of replacement costs and in terms of the degradation of mission effectiveness resulting from a loss of personal reliability for deployment and availability for duty. A study of the potential impact of the use of payday loans on enlisted members in the Air Force found “significant average declines in overall job performance and retention, and significant increases in severely poor readiness,” as a result of using payday loans.³ Additionally, financial concerns detract from mission focus and often times require attention from commanding officers and senior NCOs to resolve outstanding debts and other credit issues.

Compensation is the basis for establishing financial stability; Service members’ decisions concerning the use of their resources have a significant impact on whether they sustain their quality of life and their plans for the future. “In 2009, average [Regular Military Compensation]

¹ U.S. Dep’t of Def., Instruction 1344.09, *Indebtedness of Military Personnel* (2008) (“Members of the Military Services are expected to pay their just financial obligations in a proper and timely manner [to include alimony and child support]. A Service member’s failure to pay a just financial obligation may result in disciplinary action under the Uniform Code of Military Justice [10 U.S.C. 801-940] or a claim pursuant to Article 139 of [10 U.S.C. 801-940].”).

² U.S. Gov’t Accountability Office, GAO-11-170, [Military Personnel: Personnel and Cost Data Associated with Implementing DOD’s Homosexual Conduct Policy](#) (January 20, 2011) (estimating that each separation costs the Department \$52,800 in 2009 dollars). The cost of \$57,272 is calculated in 2013 dollars (through November 2013), using the U.S. Dep’t of Labor, Bureau of Labor Statistics, Consumer Price Index, All Urban Consumers (CPI-U), available at <ftp://ftp.bls.gov/pub/special.requests/cpi/cpi.txt>.

³ Scott Carrell and Jonathan Zinman, “In Harm’s Way? Payday Lending and Military Personnel Performance,” August 2008, Abstract

RMC for enlisted members exceeded the median wage for civilians in each relevant comparison group—those with a high school diploma, those with some college, and those with an associate’s degree. Average RMC for the enlisted force corresponded to the 90th percentile of wages for civilians from the combined comparison groups. For officers, average RMC exceeded wages for civilians with a bachelor’s or graduate-level degree. Average RMC for the officer force corresponded to the 83rd percentile of wages for the combined civilian comparison groups.”⁴

Compensation provides the basis for Service members to establish themselves, but their success is dependent upon how they choose to use this resource. Service members still represent a predominantly young group with 43% of Service members being 25 years old or less.⁵ The junior enlisted ranks (E1 – E4) comprise 44% of the military force.⁶ Thirty four percent of E1s – E4s are married⁷ and 20 percent of them have children or other legal dependents.⁸ Considering only 11.7 percent of young people of comparable age not in the military are married, Service members tend to take on more household responsibilities than their civilian counterparts.⁹ Within this context, their financial success is dependent upon their financial acumen, their ability to constrain their impulses and their ability to act as discerning consumers in the marketplace.

As young people with steady pay checks and personal responsibilities which emerge earlier than their contemporaries, they need to have a commensurate level of financial acumen and maturity to succeed. Service members are generally high school graduates who may have started college.¹⁰ Prior to entering the military they may have had limited exposure to financial literacy programs within high school, but as such, they are generally unprepared for their financial responsibilities.¹¹ The Department has established the Financial Readiness Program to assist Service members in dealing with financial concerns, by providing messaging, education, and assistance. Throughout each year, the Department provides key messages on personal finance to

⁴ For more than 40 years, Regular Military Compensation (RMC) has been recognized as a better measure than basic pay alone for comparing military and civilian compensation. RMC includes basic pay, housing and food allowances, and an adjustment due to the allowances not being subject to federal income tax. Because this measure essentially reflects the “gross pay” that service members receive in their paychecks, it provides an appropriate comparison of military and civilian wages. The Eleventh Quadrennial Review of Military Compensation, pp xvi – xvii,

[http://militarypay.defense.gov/reports/qrmc/11th_QRMC_Main_Report_\(290pp\)_Linked.pdf](http://militarypay.defense.gov/reports/qrmc/11th_QRMC_Main_Report_(290pp)_Linked.pdf)

⁵ 2012 Demographics Profile of the Military Community, page 36

http://www.militaryonesource.mil/12038/MOS/Reports/2012_Demographics_Report.pdf

⁶ Ibid, page 17

⁷ Ibid, page 44

⁸ Ibid, page 128

⁹ 11.7% of individuals age 18 – 24 who are not in the military are married (Table 57, Marital Status by Sex and Age: 2010, US Census Bureau 2012 Statistical Abstract).

¹⁰ DMDC Survey, question 20: 39% of E1-E4s have a high school diploma, 22% have less than one year of college, 24% have one or more years of college, but no degree.

¹¹ Average score for high school seniors was 48.3% and 62.2% for college students on a financial literacy test measuring (1) income; (2) money management; (3) saving and investing; and (4) spending and credit. Jump\$Start Coalition survey of high school seniors and college students, 2008, page 8.

www.jumpstart.org/assets/files/2008SurveyBook.pdf

the military community as part of a strategic communications plan that includes press releases, news articles, interviews, websites and social media. The Department has the assistance of nonprofit organizations in delivering messages and programs to promote savings and sound money management. The Department annually promotes the “Military Saves Campaign,” which occurs at the end of February each year as part of “America Saves,” sponsored by the Consumer Federation of America. The campaign asks Service members and their families to pledge towards their own savings goals, and the campaigns are supported by banks and credit unions on military installations. Initiated in 2007, the campaign has signed up 31,527 savers through 2013.¹² Additionally, the Financial Institutions National Regulatory Authority (FINRA) Foundation sponsors the “Save and Invest Program” that has provided forums at military installations (33,000 participants), fellowships for 1,200 military spouses to earn a financial counselor credential and give back to the community through 355,000 practicum hours, assistance to wounded warriors (17,000 guides distributed), 800,000 booklets on managing money during military moves and deployments, and access to no cost on-line tools to assist 150,000 military families with managing credit.¹³

The Department has established policy requiring Service members to receive financial education throughout their military careers, commencing with an initial course provided within 3 months of having arrived at their first duty station. As Service members assume supervision of others, they are also provided information on policies and practices designed to protect junior military members.¹⁴ Each of the Military Services manages its own educational program to fulfill this requirement, based on regulations from the Military Departments. For Fiscal Year 2012, the Military Services reported providing 34,867 briefings to 872,187 participants.¹⁵ In addition, the National Guard and Reserve Commands conducted 8,912 sessions, hosted at unit events lasting one-to-three days, attended by 13,480 participants.¹⁶

Department policy also requires the Military Services to provide one-on-one counseling to help a Service member determine appropriate short and long term actions to alleviate debt and achieve financial goals. The Military Services employ at least one certified financial counselor (civil service or contractor) at each military installation and have developed Military Service-specific programs to extend counseling into the military units through designated approved financial educators. For example, the Department of the Navy directs Navy and Marine Corps units to designate and train a Command Financial Specialist (E6 or above) who delivers financial education, conducts basic counseling and makes referrals to certified counselors. The Military

¹² Military Saves 2013 Report, page 2, <http://www.militarysaves.org/in-the-newsroom/military-saves-week-reports>

¹³ “Military Financial Readiness Program—Accomplishments To Date,” [SaveandInvest.org, About the Program, http://www.saveandinvest.org/MilitaryCenter/About/P124822](http://www.saveandinvest.org/MilitaryCenter/About/P124822)

¹⁴ DoD Instruction 1342.22, Family Readiness Program, July 3, 2012, page 12, <http://www.dtic.mil/whs/directives/corres/pdf/134222p.pdf>

¹⁵ ‘Fiscal Year 2012 Annual Report on Family Readiness Programs’ (internal DoD report), which reflects activities of installation-based Military and Family Support Centers/Reserve Family Program Sites.]

¹⁶ Military OneSource internal report for Fiscal Year 2012

Services reported 1,828,299 brief counseling contacts and 161,992 extended counseling contacts for Fiscal Year 2012.¹⁷ To supplement the counseling services provided by the Military Services, the Department employs contract counselors through Military One Source to conduct over-the-phone counseling (available 24/7) and 12 in-person sessions for each military client (in a 12 month period). These counselors provided 32,000 in-person sessions for 35,000 attendees in Fiscal Year 2012.¹⁸

DoD sent a 10-question survey to financial counselors and legal assistance officers who work within DoD, through the Military Service Headquarters, to determine their perspective on credit problems experienced by their clients (questionnaire and results provided at Appendix A). Two hundred and eleven financial counselors and 59 legal assistance attorneys responded to this poll. The last question¹⁹ provided respondents an opportunity to make comments on credit issues that the other questions may not have touched upon. Approximately 9 percent of the 127 responding to this question said that their clients' lack of financial knowledge contributed to over-extending themselves, and 16 percent said education could help them become more savvy consumers. Eighteen percent of 127 respondents also remarked that their clients' credit problems were the result of their desire for immediate gratification, and another 18 percent saw creditors as taking unfair advantage of their clients.

The Defense Manpower Data Center (DMDC) surveyed active duty Service members, asking them questions concerning their perspective and experiences using credit (survey at Appendix B). Respondents were asked how much they agreed or disagreed with statements about the use of credit.²⁰ Seventy-seven percent of enlisted Service members surveyed agreed/strongly agreed that overspending is the fault of the consumers, not lenders. Most Service members may understand that overspending is their own fault (as consumers), but this realization may not be sufficient to influence spending behavior for some of them.

Education may be able to inform some Service members of the pitfalls of high-cost credit products and thereby limit their exposure to the expense and risks associated with high-cost credit; however, studies on the impact of education are mixed in their results, and meta-analysis of studies does not validate education as having the desired long-term effect.²¹ DoD is not likely to persuade Service members through current financial literacy programs alone that using high cost loans is not in their long-term best interest. Behaviors more associated with habit and

¹⁷ 'Fiscal Year 2012 Annual Report on Family Readiness Programs' (internal DoD report), which reflects activities of installation-based Military and Family Support Centers/Reserve Family Program Sites.]

¹⁸ Military OneSource internal report for Fiscal Year 2012

¹⁹ Question 10 of the survey (see Appendix A): "Please provide any additional comment that may help clarify any of your choices above or provide your observations on client experiences with credit that have not been asked in the above questions."

²⁰ DMDC QuickCompass of Financial Issues, 2013, Question 12, Appendix B, "How much do you agree or disagree with the following statements?"

²¹ Daniel Fernandes, John G. Lynch, Jr. and Richard G. Netemeyer, "Financial Literacy, Financial Education and Downstream Financial Behaviors," October 8, 2013, Abstract

emotion than cognition and intention-control are less likely to be affected by education.²² The DoD continues to believe “Limiting high-cost options assists the Department in making the point clear to Service members and their families that high cost loans are not fiscally prudent and that they are to resolve their financial problems through counseling and alternatives, rather than perpetuate them through predatory high cost loans.”²³ While the Department also believes that education is both important and helpful, it is simply not as effective in steering vulnerable Service members away from high-cost loans as prohibiting those loans. As the Department stated in the preamble to the initial regulation implementing the MLA, “it is not sufficient for the Department to train Service members on how best to use their financial resources. Financial protections are an important part of fulfilling the Department’s compact with Service members and their families.”

DoD, if it were to rely solely on education, would need to overcome the promotion of high cost loans and also behavioral biases that may assuage Service members in acquiring these loans, particularly if they already have significant debt. “[M]arketing has been used profusely and effectively by for-profit firms and, at least on occasion, has contributed to making the lives of the poor even poorer. Aggressive marketing campaigns have targeted the poor on products ranging from fast foods, cigarettes, and alcohol to predatory mortgages, high-interest credit cards, payday loans, ...and various other fringe-banking schemes (see, e.g., Caskey 1996; Mendel 2005).”²⁴ Well-established concepts from social psychology (e.g., the power of the situation, construal processes, attitude change in groups, self-identity, labeling) and behavioral economics (e.g., framing, mental accounting, status quo bias) all influence the consumer’s actions and acceptance of messages.²⁵ Put another way:

“Our country’s crazed consumerism has little to do with a lack of financial literacy. Instead, two fundamental problems need to be addressed: First, we constantly soak in a bath of the mass media. Radio and television and the internet are all around us. As a result, we’re exposed to a barrage of programming in which we’re given subtle messages about what people do (or should) consume. We cannot help but be influenced by the power of marketing. Secondly, we don’t think about our spending. We spend on impulse. Or we spend — usually subconsciously — to keep up with our friends, our family, and our neighbors. We spend to make ourselves feel better when we’re down and blue. We spend to show off. We spend on

²² Ibid, pages 32 – 33

²³ Department of Defense, Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents 7 (August 9, 2006), available at http://www.defense.gov/pubs/pdfs/Report_to_Congress_final.pdf.

²⁴ Marianne Bertrand, Sendhil Mullainathan, and Eldar Shafir. “Behavioral Economics and Marketing in Aid of Decision Making Among the Poor,” <http://nrs.harvard.edu/urn-3:HUL.InstRepos:2962609>

²⁵ John G. Lynch Jr. and Wendy Wood, Special Issue Editors’ Statement: Helping Consumers Help Themselves, American Marketing Association Vol. 25 (1) Spring 2006, 1–7, ISSN: 0743-9156 (print), 1547-7207 (electronic)

things we *think* we want instead of the things we actually use and do. We spend because spending is a habit.”²⁶

We asked legal assistance attorneys about possible statements they may have heard from their clients concerning their choice to seek out high cost credit. When asked, “Based on your experience with clients, have you heard them make the following statements concerning the use of credit products with APRs over 36%?” they responded by rating “Advertising made it sound like a sure thing,” and “Only choice your client thought available,” the highest out of the six statements offered.²⁷ The behavioral terms listed above can help explain why these statements may be so commonly expressed by clients. Clients may be influenced by framing, such as the use of per-pay period pricing and statements about “no credit check needed” in advertising, which may help make costly transactions appear to be within a military consumer’s reach, regardless if they are able to repay the debt. Other advertising and business practices may make the loan process sound less imposing and the possibility of getting the loan much more certain. “[O]ne military installment lender that makes loans only to military personnel [which] advertises: ‘Quick, 90 second application process and same day approval’ for its 12 month installment loans of up to \$4,000.”²⁸ Advertising like this helps frame a favorable message to military consumers, who may be concerned they may not otherwise qualify for a loan. Lender advertising also plays upon the inherent trust the consumer has in the lender by using messages like “stop by to borrow... money from your friends.”²⁹ Also the consumer’s dependence on the default structure of loan products can easily lead them to accept offers that may not be in their own best interest.³⁰

As previously discussed, Service members and their families who use high cost loans may not be considering relief society no-interest loans, bank/credit union low interest small dollar loans, or financial counseling to resolve their financial shortfalls, even though they may be aware of the availability of these options. A meta-study of financial literacy studies reports: “Financial education is a form of information remedy. An inherent weakness of information remedies is that, for the most part, they aim to influence consumers’ evaluations of options; consumer research shows that far more variance in chosen behavior is controlled by affecting the

²⁶ J. D. Roth, “Why Financial Literacy Fails,” *Time* (Business and Money), March 11, 2013, <http://business.time.com/2013/03/11/why-financial-literacy-fails/>

²⁷ See question 5 for legal assistance officers in Appendix A. Responses were rated between “seldom” and “sometimes.” The percentage of clients with credit problems reported in question 4 corresponded to only 11 percent of the average number of clients seen in a month, which may have contributed to the low rating for responses in question 5. Legal assistance attorneys also provide assistance on family law matters, probate matters and consumer law matters outside of credit. Responses in question 4 showed that 16 percent of their clients with credit problems had high cost closed end loans and 18 percent had high cost lines of credit.

²⁸ Letter from the Consumer Federation of America, the Center for Responsible Lending, National Association of Consumer Advocates and National Consumer Law Center, August 1, 2013, page 7

²⁹ Nick Bourke, Alex Horowitz, and Tara Roche, “Payday in America: Report 2, How Borrowers Choose and Repay Loans,” Pew Charitable Trust, February 2013, page 23

³⁰ *Ibid.*, page 24

‘consideration set’ of actively considered options. Put another way, it does not matter changing consumers’ evaluation of options if consumers are not considering those options in the first place.”³¹ Thus, working through education alone would hamstring the Department’s ability to protect Service members from predatory lenders. Instead, the MLA can influence the pattern of decision-making of military consumers by changing the “consideration set” of Service member credit and emergency cash options. Thirty-one percent of enlisted Service members who used payday loans said they chose them because they felt there was “no other alternative source for borrowing cash.”³² Instead of considering more loans to accommodate chronic shortfalls in monthly resources, DoD would rather Service members obtain assistance to review their spending. Instead of committing to additional loans at high interest rates, DoD would rather Service members obtain assistance to develop plans that can reduce their overall indebtedness. Instead of considering high-cost small dollar loans to accommodate an unforeseen expenditure, DoD would rather Service members have emergency savings available for this purpose or obtain assistance through the Military Relief Societies, or low cost loans through banks and credit unions. The MLA, by limiting access to high-cost credit may, in effect, expand the “consideration set” of options for Services members in difficult financial situations. This approach may seem counter intuitive (i.e., limit options to increase their consideration set), however, certain options may not immediately come to mind for many Service members (such as reaching out to the relief societies for help, or working with a financial counselor to better balance spending with income) while others are heavily marketed or more immediately available (including high-cost credit). By limiting access to credit above a specified price threshold, the DoD intends to change the perspective of Service members in difficult financial situations, in particular by influencing them away from taking on more debt and towards considering other options to improve their personal and financial readiness.

One of the questions in the DMDC QuickCompass on Financial Issues survey asked “If high cost credit products (above 36% APR) like payday loans, vehicle title loans, installment loans, overdraft loans, and bank direct deposit advance loans weren’t available, how likely or unlikely is that you would...”³³ The responses shown below in figure 1 illustrate the potential “consideration set” of options enlisted Service members would find likely/unlikely if they could no longer access high cost credit options. The majority of enlisted Service members (88%) said that they would not be likely/very likely to be inconvenienced by not having loans over 36% APR available. This may account for the high percentage of “unlikely/very unlikely” responses for each of the other options. With this said, the options that rated the most “likely/very likely” responses were those that have the least likelihood of increasing the debt or cost of credit for the borrower. These options align with the DoD preferred approach.

³¹ Daniel Fernandes, John G. Lynch, Jr. and Richard G. Netemeyer, “Financial Literacy, Financial Education and Downstream Financial Behaviors,” October 8, 2013, page 31

³² DMDC QuickCompass of Financial Issues, 2013, Question 39, Appendix B: “What was the most important reason for choosing a payday loan rather than another source?”

³³ Ibid, Question 72.

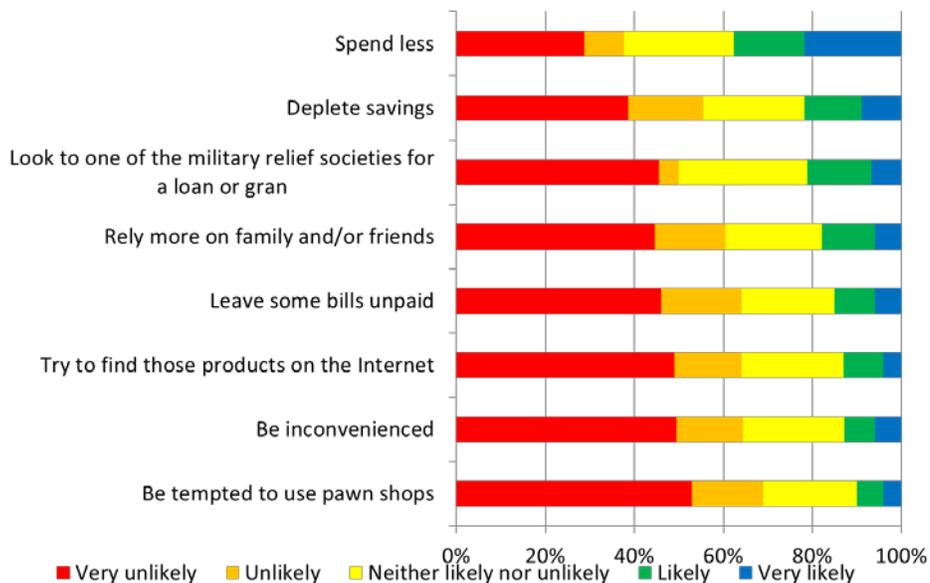


Figure 1: Actions considered if high-cost credit was no longer available.

As previously mentioned, 32% of enlisted members choosing payday loans assumed that they have no option other than to take a high-cost loan. Their assessment of financial options may have been influenced by their perception that choosing to apply for other less financially costly loans from military sources would not be approved, would require them to divulge additional information about their finances, or place themselves in a situation where their previous financial choices were going to be called into question. In responding to the DMDC survey, enlisted Service members expressed their apprehension about receiving a loan from the military relief societies. Most felt that they would be embarrassed obtaining a loan from the military relief societies and half felt that their commanders would find out (another third were uncertain). However, the majority felt it was unlikely that they would receive non-judicial punishment, lose their security clearance or be forced to return from a deployment as a result of taking a military society loan. Even so, a third or more were uncertain whether the loan would or would not adversely affect them (figure 2).³⁴

We asked financial counselors the same question about statements made during consultations as presented to legal assistance officers in the questionnaire,³⁵ but provided them different statements to evaluate that were more aligned with the conversations financial counselors would have with their clients. They rated “Client had unexpected expenses, such as car repair, PCS moving expenses, etc.” and “Client had a high debt to income ratio” as the highest, with average

³⁴ DMDC QuickCompass of Financial Issues, 2013, Question 17, Appendix B, “Assume you were having some financial trouble and you asked for assistance from a military aid society. How likely is it that each of the following would happen?”

³⁵ Question 5 in Appendix A: “Based on your experience with clients, have you heard them make the following statements concerning the use of credit products with APRs over 36%?”

responses between “sometimes” and “often.”³⁶ The DMDC QuickCompass of Financial Issues survey asked enlisted Service members who used small dollar loans why they needed the loans. In response, 70% selected “to cover one or more unexpected essential expenses.”³⁷

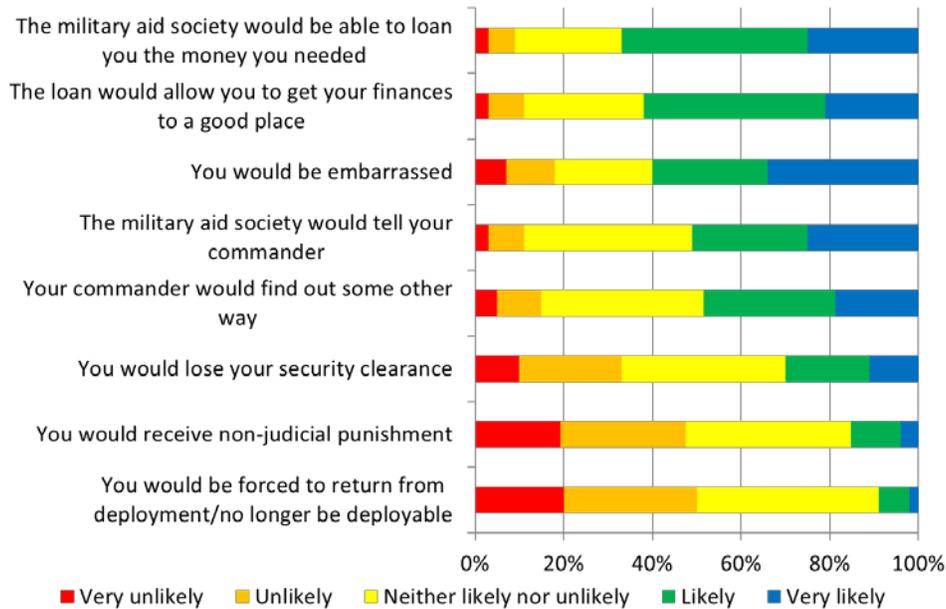


Figure 2: Enlisted Service member opinions concerning Military Aid Society loans.

Many of the financial counselors’ clients with a need for emergency cash may have been able to have received assistance from relief societies, but instead they pursued high cost loans that they potentially perceived from advertising to be within their reach. Additionally, some of these clients may have been embarrassed by accepting a relief society loan or may have been concerned that this assistance would bring them negative visibility. More so, their clients with high debt to income ratios may have felt that obtaining additional loans was preferable to seeking counseling to resolve their high level of debt, which would also have brought their financial issues to light and perhaps would require them to discuss with a counselor that they may have made some poor financial decisions in the past.

AVAILABILITY OF SMALL DOLLAR LOANS

Unlike the general public, Service members have access to very low cost, low risk, small dollar loans from military relief societies, and banks and credit unions operating on DoD installations. “Bank regulators and consumer advocates have adopted four criteria for identifying high-quality small-dollar loans: 1) an Annual Percentage Rate (APR) of no more than 36%, 2) a loan term of

³⁶ See question 5 for financial counselors in Appendix A. Respondents reported in question 4 that approximately 48 percent of their clients had credit problems. Sixteen percent of their clients with credit problems had high cost closed end loans and 14 percent had high cost lines of credit.

³⁷ Ibid, Question 31, Appendix B: “Why did [you][you and/or your spouse][you and/or your significant other] use one or more of these financial products or services in the past 12 months?”

at least 90 days, 3) repayment in installments rather than in a single lump sum, and 4) an assessment by the lender of the borrower's ability to repay the loan.”³⁸ As described above, access concerns within DoD are more likely to be associated with military consumer perceptions and behavioral bias rather than with availability of safe, inexpensive credit. As mentioned above, the Military Services have worked with private, nonprofit charitable organizations chartered to provide relief services to Service members and their families in order to provide monetary support to Service members and their families with financial hardships. The four relief societies for the Military Services (Army Emergency Relief, Navy-Marine Corps Relief Society, Air Force Aid Society and Coast Guard Mutual Assistance) provided \$142.2 million in no-interest loans and grants to 159,745 clients in 2012.³⁹

Each of the relief societies traditionally has provided no-interest loans and grants for shortfalls in household expenses (e.g., rent, mortgage, or utilities) and for unforeseen emergencies (e.g., auto repair, funeral, or family emergency). Since 2007, each of the relief societies also has offered small-dollar loans, which can be withdrawn without counseling. These loans attempt to mirror the quick approval and no hassle approach of some high cost lenders. As shown in figure 1, Service members were asked about their perceptions of borrowing from the military relief societies. The majority (64%) felt likely/very likely that the military relief society would be able to loan the money needed (25% felt neither likely nor unlikely); and 59% felt likely/very likely that the loan would allow them to get their finances in a good place (28% neither felt likely nor unlikely).⁴⁰

In addition to the support of the military relief societies, several banks and credit unions that operate on military installations offer small dollar loans designed to assist Service members who appear to need a way out of unmanageable debt. As part of their response to the Department's Advanced Notice of Proposed Rulemaking (ANPR) (Docket ID: DoD-2013-OS-0133), the Credit Union National Association (CUNA) and the Defense Credit Union Council (DCUC) provided a list of sample small dollar alternative products offered by credit unions operating on DoD installations.⁴¹ The list includes 35 examples with interest rates ranging from 0% to 24% APR. Fourteen of the listed credit unions offer the “Asset Recovery Kit (ARK)” that provides an interest free short-term advance of up to \$500 (or 80% of net income) for a \$5 fee, to be paid back within 6 months or less. Service members are limited to three ARK advances in a six month period, and are required to receive counseling as part of any loan after the first. Other

³⁸ Jim Campen, “Small Dollar Lending, Is There a Responsible Path Forward?” Center for Economic and Policy Research, August 2012, page

³⁹ From 2012 annual reports for Army Emergency Relief, Navy-Marine Corps Relief Society, Air Force Aid Society and Coast Guard Mutual Assistance

⁴⁰ DMDC QuickCompass of Financial Issues, 2013, Question 17, Appendix B, “Assume you were having some financial trouble and you asked for assistance from a military aid society. How likely is it that each of the following would happen?”

⁴¹ See list at appendix C.

examples include the Payday Alternative Loan (PAL) at 18% APR for loans \$100 - \$1,000, which includes a savings component, and lines of credit, such as the Payday Credit Line and Ready Cash, offered at 18% APR. Some of the credit unions on the list offer signature loans for small dollar amounts at interest rates ranging from 6.75% to 18% and at risk-based interest rates.

The Association of Military Banks of America (AMBA), representing banks on military installations, did not include a similar list with its response to the DoD ANPR. However, an example of a small dollar loan offered by these banks can be found in the Federal Deposit Insurance Corporation (FDIC) affordable small dollar loan pilot program: “Armed Forces Bank generally offers loans from \$250 to \$2,000. All loans are closed-end transactions for up to 24 months. The interest rate is 18 percent, and there are no fees. The borrower must open an account with the bank and maintain direct deposit. Loan payments are automatically debited from the borrower’s account.”⁴²

FINANCIAL STATUS OF ENLISTED SERVICE MEMBERS

Forty one percent of enlisted Service members (46% of E1s – E4s) said they had used one or more sources of small dollar lending in the past 12 months. These sources included payday loans, vehicle title loans, bank deposit advance loans, pawn shop loans, cash advances on credit cards, overdraft loans, overdraft lines of credit, overdraft protection from other accounts, relief society loans, and loans from friends and family.⁴³ About 62% of enlisted Service members selected responses indicating that they were able to make ends meet without difficulty. Twelve percent selected the responses “tough to make ends meet but keeping your head above water,” or “in over your head” to describe their financial condition.⁴⁴ About 26% selected the response “occasionally have some difficulty making ends meet.”

When asked about their savings habits, 14% of enlisted Service members selected the option “spend all the income received and don't save” and 4% selected the option “don't know.” Forty-four percent selected the option “regularly set aside money in savings.” The remaining 39% selected the option “save whatever is left at the end of the month.” When asked about their savings, about 57% of enlisted Service members indicated that they had at least \$500 in savings that would be available for emergencies. Eight percent indicated that they have less than \$100 and 17% indicated that they have no emergency savings.⁴⁵

⁴² http://www.fdic.gov/bank/analytical/quarterly/2008_vol2_3/2008_Quarterly_Vol2No3.html

⁴³ DMDC QuickCompass of Financial Issues, 2013, Question 30, Appendix B: Have [you][your and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?”

⁴⁴ Ibid, Question 13, Appendix B: “Which of the following best describes [your financial condition][the financial condition of you and your spouse][the financial condition of you and your partner or significant other]?”

⁴⁵ Ibid, Question 15, Appendix B: “Which of the following best describes [your saving habits][the savings habits of you and your spouse][the savings habits of you and your partner or significant other]? I[We]:”

When asked about experiencing any shortfalls in finances, 48% of enlisted Service members reported having problems in the past 12 months. Specifically, 9% said they had been more than 60 days late in paying mortgage or other debts, 17% reported that they were unable to use bank credit card(s) because the credit limit was reached, 44% reported that they were short cash between paychecks and 12% indicated that they were unable to pay monthly bills.⁴⁶ When asked about how many months in the past 12 were they short on cash, unable to use a credit card because of the credit limit was reached, or unable to pay bills or other debts, 12% said 5 to 7 months and 11% said 8 or more months. The average response was 3.4 months in a 12-month period.⁴⁷

Seventy-one percent of enlisted members said they had checked their credit score or credit report in the past twelve months. They were also asked to rate their credit history and credit score.⁴⁸ About 58% of enlisted Service members rated their own credit history as “good” or “very good,” 22% selected “neither good nor bad” and 12% selected “bad” or “very bad.” Only 4% indicated that they believed they had no credit history.⁴⁹ When asked to estimate their own credit scores, 40% selected either “between 681 and 720” or “above 720”, 27% selected as “between 581 and 640” or “between 641 and 680”, and 9% selected “500 or below” or “between 500 and 580” (equivalent to bad or very bad). Twenty-five percent didn’t know their history.⁵⁰

The survey also requested another perspective of their credit experience. Respondents were asked “In the past 5 years, has any lender or creditor turned down any request [you][you and/or your spouse][you and/or your partner or significant other] made for credit, or given you less credit than you applied for?” Thirty-four percent said they had been turned down when requesting credit, 57% said they had not and 9% said they did not know.⁵¹ Of the 34% reporting a denial of credit, 75% said they had been turned-down by banks or credit unions, 37% by finance companies, 27% by stores, 4% by payday lenders and 9% by other lenders (some had been turned-down by more than one).⁵²

The survey also asked a question about Service member awareness of problems related to credit among their fellow Service members. The results demonstrate a significant gap between how many Service members report that they have difficulties with credit and how many report seeing

⁴⁶ Ibid, Question 28, Appendix B: “During the past 12 months, did any of the following happen to [you][you and your spouse][you and your partner or significant other]? [I was][We were]...”

⁴⁷ Ibid, Question 29, Appendix B: “In how many of the past 12 months were [you][you and your spouse][you and your significant other] short on cash, unable to use a credit card because of the credit limit was reached, or unable to pay bills or other debts?”

⁴⁸ Ibid, Question 23, Appendix B: “Have you checked either your credit score or credit report in the past 12 months?”

⁴⁹ Ibid, Question 25, Appendix B: “How would you rate your credit history?”

⁵⁰ Ibid, Question 24, Appendix B: “What is your credit score?”

⁵¹ Ibid, Question 18, Appendix B

⁵² Ibid, Question 19, Appendix B: “Which of these places turned down the request or gave you less credit than you applied for?”

“other military members get in trouble using credit.” Sixty-seven percent of enlisted Service members reported seeing other military members get in trouble using credit, while, as described above across several questions, a significantly smaller percentage indicated that they personally had difficulties with credit. These responses contrast with the credit concerns respondents expressed to a question asking about whether they had seen other Service members with credit concerns over the past 5 years. By comparison 67% said that others had problems and 23% said they neither agreed nor disagreed and only 10% said they disagreed.⁵³ This may be an indication of a “social desirability bias”⁵⁴ in the results from the DMDC survey.

The Department has also found evidence of potential bias in the survey results, particularly around social desirability, related to underreporting of the use of short-term credit products. The Army Emergency Relief Society, Navy-Marine Corps Relief Society and the Air Force Aid Society reported providing 157,200 no interest loans and grants, which represent 12% of Service members. However, only 8% of those surveyed by the DMDC reported taking one of these loans or grants.⁵⁵ Service members have expressed their embarrassment when considering the use of relief society loans and grants. A similar social desirability bias likely impacted survey results relating to the use of high-cost credit products. The MLA itself, security clearance requirements, and related statements by the Department about the dangers associated with high-cost credit may have contributed to this bias by underscoring for Service members that Department opposes the use of such products.

The results of the DMDC QuickCompass on Financial Issues tends to indicate that most Service members report sufficient access to safe, low-cost credit, report few problems managing their finances, and report little use of or impact by high-cost credit products on their financial lives. Nevertheless, the DMDC survey results also tend to indicate that a substantial minority of Service members continue to report difficulty managing their finances, and little access to safe, low-cost credit options. While the relative size of these two groups varies across the different types of financial indicators surveyed, the Department estimates that between 12 and 25% of enlisted Service members may face emergency financial short-falls and indicate difficulties managing their finances and avoiding problems with credit. Finally, the Department notes that there is a substantial likelihood that the survey, due to social desirability bias on the part of the respondents, may under-state the financial readiness problems faced by Service members and Service member use of risky, high-cost credit.

⁵³ Ibid, Response d., Questions 12, Appendix B: “How much do you agree or disagree with the following statements? In the last 5 years I have seen other military members get in trouble using credit.”

⁵⁴ Sabrina M. Neeley and Maria L. Cronely, “Research Participants Don’t Tell It Like It Is: Pinpointing the Effects of Social Desirability Bias Using Direct V. Indirect Questions,” *Advances in Consumer Research*, Volume 31, page 432

⁵⁵ DMDC QuickCompass of Financial Issues, 2013, Question 30, Appendix B: “Have [you][you and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?”

In the event that Service members overwhelm their credit, or have not established cash reserves or credit for an emergency, the Department and the Military Relief Societies are prepared to assist them in order that they might resolve immediate difficulties and continue to manage their income and expenses to where they can develop a sounder financial basis. The Department wants Service members to be in charge of their financial matters, but as they develop financial acumen, the Department wants them to choose behavior that will not hinder their financial future. It may be difficult to convince Service members through education alone to choose what they perceive to be uncomfortable courses of action to resolve their financial problems when their bias may be to do otherwise, and when this bias may be supported by advertising and business practices advocating an opposite course of action. Prior to considering the use of the MLA as a way of redefining the credit “consideration set” for Service members with financial shortfalls, this report will review the status of state and federal policy governing credit that can be covered by the MLA, the reported use of these credit products by enlisted Service members, and the perspective of consumer advocates, financial industries and public officials concerning possible modifications to the definitions of credit included in the MLA.

STATE POLICY AND PRODUCTS OFFERED BY STATE REGULATED CREDITORS

The definitions included in Section 232.3 of 32 CFR Part 232, were developed to work in concert with State definitions and rules governing payday loans, vehicle title loans and tax refund anticipation loans. The supplemental information accompanying the release of 32 CFR Part 232, August 31, 2007, described some of the analysis undertaken to develop the parameters for allowable principal and repayment period. By applying both of these limitations, the combination was believed to be sufficient to cover payday and vehicle title loans without allowing loopholes for creditors to continue to offer variants of these loan products.

Significant concern has been raised about the loopholes in state policy and the subsequent changes in the marketplace that have blurred the differences between payday, vehicle title and installment loans. These systemic changes have been one of the primary reasons for the concerns expressed by consumer advocates, state officials and members of Congress about the vulnerability of Service members and their families to potentially predatory lending practices.

Current analysis of state statutes shows that there are 38 states authorizing payday lending, of which 3 (NH, OH and OR) have statutes that limit interest rates at or below 36% (though lending above 36% APR continues under alternate statutes in Ohio). Of the 35 remaining states, 24 have authority to enforce the MLA.⁵⁶ Enforcement coverage for vehicle title loans is somewhat more

⁵⁶ Sixteen (AL, AK, CO, FL, IA, ID, IN, KY, MI, MO, ND, SC, SD, TN, UT and WA) have general provisions that make violation of any law or any federal law in the course of dealings as a licensee an enforceable offense, or otherwise have sufficient authority to enforce the MLA. Seven states (CA, HI, IL, MT, NV, TX and WY) have established specific language that allows enforcement of the MLA and the regulation. One state (VA) has specific prohibitions

complicated by the structure of state statutes authorizing these loans. Of the 21 states allowing vehicle title loans,⁵⁷ 8 states authorize enforcement (IL, MO, NV, SD, TN, TX, UT and VA).

State examinations and enforcement authority have been tied to the definitions in the regulation (with the exception of Virginia which established its restrictions outside of the MLA). The Consumer Financial Protection Bureau (CFPB) noted in its April 2013 report that payday loans cannot be defined simply as closed-end loans where the principal and the interest are due the next payday (generally within two weeks to a month). Payday loans can also be of much longer duration, feature payment in installments and can be structured as open-end credit. State law, as well as other factors, has influenced providers of payday loans to consider other forms of high cost lending.⁵⁸ Consumer Federation of America (CFA) reported “a recent survey of 19 online payday lenders found that 12 offered loans in amounts over \$2,000 and 17 offered loans with terms longer than 91-days, although some loans were as short as four months;”⁵⁹ all of which are outside of the definitions included in the regulation. CFA reviewed applicable state laws and found that 11 states have laws allowing for payday loans which are outside of the definition in the regulation and 13 states have laws allowing for vehicle title loans outside of the regulation definition.⁶⁰ More importantly, they estimate based on the assigned military strength within these states that approximately 54 percent of Service members can access either a payday or vehicle title loan without violating the MLA.⁶¹

In addition to the opportunity for some Service members to continue to access payday and vehicle title loans, some providers of these loans are diversifying into offering other credit products that are not necessarily secured by a check, access to a bank account or a vehicle title and consequently not covered by the regulation. Additionally, Service members can access high cost installment loans and lines of credit from storefront and on line providers not involved with payday or vehicle title loans. Availability is again generally determined by the applicable state law. The National Consumer Law Center developed a scorecard rating state consumer protection

against lenders offering closed-end payday loans to Service members and their families. The 11 remaining states are DE, KS, LA, ME, MN, MS, NE, NM, OK, RI and WI.

⁵⁷ Twenty-one states have significant presence of high-cost vehicle title lenders. Of the 21 states, 17 (AL, AZ, DE, GA, ID, IL, LA, MO, MS, NH, NM, NV, SD, TN, UT, VA and WI) authorize lending under state statute and 4 states allow title loans as a result of other laws: KS allows title lending as open-ended lines of credit; TX allows title lenders to use a "Credit Services Organization" model; CA and SC only cap APRs up to a certain loan amount (\$2,500 and \$600 respectively). (Center for Responsible Lending, <http://www.responsiblelending.org/other-consumer-loans/car-title-loans/tools-resources/car-title-lending-by-state.html>)

⁵⁸ CFPB, Payday Loans and Deposit Advance Products, A White Paper of Initial Data Findings, April 24, 2013, http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf at p. 8.

⁵⁹ Eleven states allowing payday loans outside the MLA: AK, CO, ID, IL, IN, OH, RI, SD, TX, UT and VA ; 13 states allowing vehicle title loans outside the MLA: AZ, CA, IL, KS, LA, MO, NV, NM, OH, SC, SD, UT and WI . Tom Feltner, Laura Udis and Jean Ann Fox, “Policy Brief: Gaps in the Military Lending Act Leave Many Service Members Vulnerable to Abusive Lending Practices,” Consumer Federation of America, page 6

⁶⁰ Ibid

⁶¹ Ibid

policies for payday loans, vehicle title loans, installment loans for \$500 for six months, installment loans for \$1,000 for one year and the state criminal usury cap (if one exists). The scorecard used 36% APR as the benchmark, with APR caps above 36% failing and caps at or below 36% passing. Using the scorecard to evaluate installment products, 31 states fail to offer \$500 loans for six months and 22 states fail to offer \$1,000 loans for one year at or below 36% APR.⁶² Applying the same measure used by CFA (Service member assigned to states failing the criteria as a percentage of Service members assigned in the United States) to this evaluation of states, there are 68% of Service members who can potentially access \$500 installment loans for six months with APRs over 36% and 41% who can potentially access \$1,000 loans for one year.

As part of the Department's survey of financial counselors and legal assistance attorneys, they were asked in which states they provide their services. The questionnaire also asked about the average number of clients seen with closed-end loans over 36% APR. When considered overall as a percentage of the average number of clients they saw with credit problems, the financial counselors and legal assistance attorneys in the 31 states that failed the NCLC scorecard had 17% of their clients with loans over 36% APR, as compared to 12% of the clients of counselors and attorneys in states that passed. Similarly, counselors and attorneys had 22% of their clients with closed end loans over 36% APR in the 22 states that failed on the scorecard, versus 13% in the states that passed. It is logical to assume that Service members would more likely obtain loans with interest rates over 36% APR in states where the law allows for these loans. Perhaps equally so, counselors and attorneys in the 20 states that allow either payday or vehicle title loans not covered by the definitions in the regulation had 18% of their clients with credit problems have loans over 36% APR, versus 13% in states that do not allow for these loans. These percentages do not necessarily reflect that clients in these states had payday or vehicle title loans, but rather they were more likely to have had some kind of closed-end loan with an APR over 36%.

Availability of these lending products contrasts with the reported use by enlisted Service members. When asked about their use of various credit products in the DMDC QuickCompass on Financial Issues survey, 2% said they had used payday loans in the past 12 months and 4% said they used vehicle title loans.⁶³ Nine percent of enlisted Service members said they had

⁶² States failing to offer \$500 for six months at or under 36% APR: AL, AZ, CA, CO, DE, GA, ID, IL, KY, LA, MA, MI, MN, MS, MO, MT, NE, NV, NH, NM, NC, OH, OK, SC, SD, TN, TX, UT, WA, WV and WI; states failing to offer \$1,000 for one year at or under 36% APR: AZ, CO, DE, ID, IL, KY, LA, MN, MS, MO, MT, NV, NH, NM, NC, OH, SC, SD, TN, TX, UT and WI. Leah A. Plunkett, Emily Caplan and Nathanael Player, "Small Dollar Loan Products Scorecard – Updated," National Consumer Law Center, pages 14 – 20, <http://www.nclc.org/reports/content/cu-small-dollar-scorecard-2010.pdf>.

⁶³ DMDC QuickCompass on Financial Issues, 2013, Question 30, Appendix B: "Have [you][you and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?"

unsecured personal loans from finance companies,⁶⁴ of which 3% reported having loans with APRs over 36% and 18% with loans between 25% and 36% APRs⁶⁵ (some of these loans may have had MAPRs above 36%, depending on other fees and the sale of ancillary products). As previously discussed, social desirability bias may have influenced these percentages to under-represent the actual use of these products.

Enlisted Service members obtained roughly half of their payday loans from storefronts (42%) and half from the internet (51%).⁶⁶ Thirty-two percent reported that their loans were 91 days or less (which were covered by the current MLA regulation), 34% were more than 91 days (not covered by the current MLA regulation) and 23% said their loans were provided as revolving credit (also not covered by the current MLA regulation).⁶⁷ Seventy-three percent said that their lender asked about their military status (16% said they did not).⁶⁸ Seventy percent obtained their most recent payday loan for more than \$500 and 19% said they obtained a loan for between \$200 and \$299.⁶⁹ The majority (78%) said that they took out only 1 – 2 payday loans in the past 12 months, with 17% taking out 3 – 6 loans, and 6% taking out 7 or more loans (average number of loans was 2.8).⁷⁰

Of the 4% of enlisted Service members who said they used vehicle title loans, 47% said they obtained them from storefronts, 13% from the internet and 42% said they didn't know.⁷¹ Forty-two percent obtained loans for over \$6,000,⁷² and 69% reported that their loans had APRs of less than 36% (2% were 36% - 50%, 4% were more than 51% APR and 25% didn't know).⁷³ With one fourth of respondents not knowing their interest rates it is difficult to say with any certainty what the actual percentage of borrowers had loans that were over 36% APR. Even so, 16% of enlisted Service members who used vehicle title loans had to repay their loans in 181 days or less (covered by the MLA), with 36% having loan repayment periods of more than 181 days (not covered by the MLA). Nineteen percent had loans that were revolving credit (also not covered by the MLA).⁷⁴ Sixty-six percent of respondents said their lenders asked if they were in the military (15% said they were not asked and 19% said they didn't know).⁷⁵

⁶⁴ Ibid, Question 61, Appendix B: "Do [you][you and/or your spouse][you and/or your significant other] currently have any outstanding balances on any of the following credit products?"

⁶⁵ Ibid, Question 66, Appendix B: "What is the highest APR (interest rate) [you][you and/or your spouse][you and/or your significant other] are paying on an unsecured personal loan from a finance company?"

⁶⁶ Ibid, Question 38, Appendix B: "Where did you obtain your payday(s)?"

⁶⁷ Ibid, Question 40, Appendix B: "How much time did you have to pay off your most recent payday loan in full?"

⁶⁸ Ibid, Question 41, Appendix B: "Did the payday lender ask about active duty military status?"

⁶⁹ Ibid, Question 42, Appendix B: "What was the amount of your most recent new payday loan?"

⁷⁰ Ibid, Question 43, Appendix B: "Approximately how many payday loans did you take out in the last 12 months?"

⁷¹ Ibid, Question 45, Appendix B: "Where did you obtain your vehicle title loan(s)?"

⁷² Ibid, Question 46, Appendix B: "What was the amount of your most recent vehicle title loan?"

⁷³ Ibid, Question 47, Appendix B: "What was the APR (interest rate) on your most recent vehicle title loan?"

⁷⁴ Ibid, Question 48, Appendix B: "How much time did you have to pay off your most recent vehicle title loan in full?"

⁷⁵ Ibid, Question 49, Appendix B: "Did the vehicle title loan lender ask about active duty military status?"

Most enlisted Service members, who had installment loans from finance companies, had annual interest rates of less than 36%. Specifically, 41% had personal loans at interest rates of 18% or below, 22% had loans with APRs between 19% and 24%, 18% had loans with APRs between 25% and 36%, and 3% had loans above 36% APR. Seventeen percent said they didn't know their annual interest rate, which again calls into question the percentage describing their loans as having APRs more or less than 36%.⁷⁶ Furthermore, other costs to the consumer not included in the APR could make loans below 36% above that threshold when considered as part of that calculation. These additional costs, along with repeated refinancing have come under scrutiny:

- “Effective APR on many loans is significantly higher than the stated APR listed on the loan contract, due to the purchase of some types of credit insurance, which the lender is not legally required (under the federal Truth in Lending Act [TILA]) to include in the APR calculation.
- [Loans] can be renewed every few months, with new charging of interest, fees, and credit insurance premiums. Renewal is sometimes accompanied by a small ‘payout’ representing some of the principal already paid off in previous monthly installments. The loan amount typically resets to the original amount borrowed, or is increased.”⁷⁷

Fifteen percent of enlisted Service members who had personal loans from finance companies said that they were required to pay origination fees, 11% said they paid monthly account maintenance fees, 12% said they were required to take *mandatory* credit insurance, and 7% said they required to pay some other fee or service.⁷⁸ One of the primary purposes of the MAPR has been to consolidate costs associated with the loan, to include the sale of ancillary products and services, such as credit insurance. The value versus cost of these products has been a concern of consumer advocacy groups: “[Consumers Union and the Center for Economic Justice] review of actual credit insurance loss ratios shows that state legislatures and/or state insurance regulators, with only a very few exceptions, have failed to protect credit insurance consumers. Actual historical credit insurance loss ratios are far below even the NAIC [National Association of Insurance Commissioners] model’s modest 60% loss ratio standard.”⁷⁹

⁷⁶ Ibid, Question 66, Appendix B: “What is the highest APR (interest rate) [you][you and/or your spouse][you and/or your significant other] are paying on an unsecured personal loan from a finance company?”

⁷⁷ Mitchell Hartman, “What’s the difference between payday and installment loans?” *Marketplace*, May 13, 2013, <http://www.marketplace.org/topics/wealth-poverty/beyond-payday-loans-installment-lending-and-cycle-debt/whats-difference>

⁷⁸ DMDC QuickCompass on Financial Issues survey, Question 67, Appendix B: “Were any of the following required for this unsecured personal loan from a finance company?”

⁷⁹ Mary Griffin and Birny Birnbaum, “Credit Insurance: The \$2 Billion A Year Rip-Off Ineffective Regulation Fails to Protect Consumers,” Consumers Union and the Center for Economic Justice, March 1999, page 3, <http://www.cej-online.org/credit.php>; <http://consumersunion.org/news/credit-insurance-the-2-billion-a-year-rip-off/>

With respect to refinancing, 16% of enlisted Service members said that they had refinanced their current loan from a finance company, 78% said they had not and 6% said they did not know.⁸⁰ Refinancing an installment loan before it comes to term can allow the creditor to reset the loan with new fees and new insurance. “A delinquent borrower would be encouraged to sign up for a renewal to pay off the original loan and clean up their finances with more borrowed money. ‘If you had any money available in principal, we could renew the loan,’ [Matthew Thacker, a former assistant manager of a branch of an installment lender] says. ‘And we made more money off that because we sell the insurance on it again — more life insurance, more accidental death and dismemberment.’”⁸¹

An additional concern specifically associated with lending to members of the military has been the required use of the military pay allotment system for the payment of loans. Use of the DoD allotment system is under review by the DoD as a result of investigations conducted by the CFPB.⁸² With respect to the use of allotments for unsecured loans from finance companies, 42% of enlisted Service members said they were *required* to have a military allotment from their pay to make payment of the loan, 53% said they were not required and 6% said they did not know.⁸³

Similar questions were asked concerning unsecured personal loans obtained from banks and credit unions. Nineteen percent of enlisted Service members said they had unsecured personal loans from depositories.⁸⁴ Ten percent had refinanced their loans with their bank or credit union;⁸⁵ 38 % had been required to set up automatic withdrawals from their checking or savings accounts; 8% were required to pay origination fees; and 5% said they had monthly maintenance fees on their accounts, had purchased mandatory credit insurance, or had paid other fees or services associated with their loans.⁸⁶ Perhaps more significantly, between 9% - 11% said they did not know if they had fees or mandatory credit insurance.⁸⁷ Twenty five percent of enlisted respondents also said that they had borrowed under \$1,500⁸⁸ and 7% said their interest rates were

⁸⁰ DMDC QuickCompass on Financial Issues survey, Question 68, Appendix B: “Has this unsecured personal loan from a finance company been refinanced?”

⁸¹ Mitchell Hartman, “How World Finance makes a killing lending on the installment (loan) plan” Marketplace, May 14, 2013, <http://www.marketplace.org/topics/wealth-poverty/beyond-payday-loans-installment-lending-and-cycle-debt/lucrative-installment>

⁸² CFPB Administrative Proceeding, File No. 2013-CFPB-0003, Consent Order, in the matter of U.S. Bank National Association, Cincinnati, Ohio, http://files.consumerfinance.gov/f/201306_cfpb_enforcement-order_2012-0340-02.pdf

⁸³ DMDC QuickCompass on Financial Issues survey, Question 67, Appendix B: “Were any of the following required for this unsecured personal loan from a finance company?”

⁸⁴ *Ibid*, Question 61, Appendix B: “Do [you][you and/or your spouse][you and/or your significant other] currently have any outstanding balances on any of the following credit products?”

⁸⁵ *Ibid*, Question 65, Appendix B: “Has this unsecured personal loan at a bank or credit union been refinanced?”

⁸⁶ *Ibid*, Question 64, Appendix B: “Were any of the following required for this unsecured personal loan at a bank or credit union?”

⁸⁷ *Ibid*

⁸⁸ *Ibid*, Question 62, Appendix B: “How much did [you][you and/or your spouse][you and/or your partner or significant other] borrow on you most recent bank or credit union loan?”

above 24% APR.⁸⁹ These small loans and subprime interest rates are generally offered by finance companies instead of depositories. If the percentage enlisted Service members with finance company loans is combined with the percentage with loans from depositories, 27% of Service members had unsecured personal loans, of which 2% were above 36% APR and 10% were between 25% and 36% APR.

This report will discuss the perspective of consumer advocacy and financial industry groups, along with state officials and members of Congress, after review of financial products primarily governed by federal policies and overseen by federal regulators.

FEDERAL POLICY AND CREDIT PRODUCTS OFFERED BY FEDERALLY REGULATED CREDITORS

At the time the initial regulation was drafted in 2007, there was one product provided by financial institutions overseen by federal regulators, namely tax refund anticipation loans (RALs). The banks that had been involved with providing these loans no longer offered RALs after the 2012 tax season; however, RALs have not gone away and in some instances have been supplanted by refund anticipation checks (RACs). Payday lenders and other finance companies have continued to offer RALs and banks have gone into offering RACs. RALs offered by non-bank companies are at higher interest rates than those that had been offered by banks. Hundreds of thousands of consumers purchase RALs per year and tens of millions get RACs. Fee revenue for RALs for 2011 was \$46 million and \$550 million for RACs.⁹⁰

Twenty states currently regulate RALs: Arkansas, California, Colorado, Connecticut, Illinois, Louisiana, Maine, Maryland, Michigan, Minnesota, Nevada, New Jersey, New York, North Carolina, Oregon, Tennessee, Texas, Virginia, Washington State, and Wisconsin. Statutes primarily require disclosures to protect consumers. Additionally, Illinois statutes limit APRs to 36% and statutes for Arkansas, Connecticut, Illinois, Maine, Maryland, Minnesota, and New York prohibit tax add-on fees.⁹¹

The definition of RALs in the regulation for the MLA has no amount or term limitations, and consequently, the prohibitions and limitations in the MLA still apply to RALs. However, the MLA does not impact RACs since there is considerable question whether RACs are loans; the only instance where they may be considered loans is the advance of the cost of tax preparation.

⁸⁹ Ibid, Question 63, Appendix B: "What is the highest APR (interest rate) [you][you and/or your spouse][you and/or your partner or significant other] are paying on a bank or credit union loan?"

⁹⁰ Chi Chi Wu, Tom Feltner and Jean Ann Fox, "Something Old and Something New in Tax-Time Financial Products: Refund Anticipation Checks and the New Wave of Quickie Loans," National Consumer Law Center and the Consumer Federation of America, February 2013, page 1, <http://www.nclc.org/issues/refund-anticipation-loans.html>

⁹¹ Ibid, pages 28 -29

The California appellate court upheld a ruling in a lower court that fees advanced as part of a RAC should be considered finance charges subject to TILA disclosures.⁹²

Overdraft protection programs were not included in the initial DoD report to Congress in 2006 and not considered as part of the initial regulation implementing the MLA (fee-based protection programs are not considered credit under TILA). DoD reviewed overdraft protection programs in 2008 as a result of input from consumer advocacy groups which responded to a request for information through the Federal Register. In 2008, DOD determined that the prudential regulators were sufficiently engaged in reviewing overdraft protection programs and that they would probably make changes to policies overseeing consumer protections.

In November 2008, the FDIC released a report on overdraft programs that quantified some of the concerns that consumer advocates described in their response to the DoD information request. FDIC surveyed 1,171 member institutions concerning automated fee-based overdraft protection, line-of-credit (LOC) overdraft protection and overdraft protection linked to other accounts (linked-account programs). They found that 75% of surveyed institutions offered an automated overdraft protection program automatically as part of opening an account, with the option to opt-out. Almost all surveyed banks (94.7%) offered LOC and linked-account overdraft protection as opt-in programs. In addition to the opt-out feature of automated overdraft protection, FDIC reported that nearly half (48.8%) of the overdrafts covered by these programs were the result of automated teller machine (ATM) withdrawals and point-of-sale (POS) debit purchases, which could have been denied at the time of the transaction. FDIC also found that the batch processing of other transactions, with largest being processed first, provided opportunity for additional overdrafts. Twelve and half percent of surveyed banks received complaints on automated overdraft protection; whereas, less than 1% of banks received complaints on linked-account programs and 1.5% had complaints on LOC programs.⁹³

The prudential regulators considered additional rules to assist consumers with overdraft protection programs. The CFPB summarized regulators' efforts in their 2013 report:⁹⁴

“To further address concerns about heavy overdraft use by consumers, and with the anticipation that ‘improvements in the disclosures provided to consumers could aid them in understanding the costs associated with overdrawing their accounts and promote better account management,’ the [Federal Reserve] Board amended Regulation DD (which implements the Truth in Savings Act) in 2005 to address certain overdraft disclosures for “promoted overdraft programs” (effective July 2006.) Then again in 2009, the Board

⁹² Ibid, page 30

⁹³ FDIC Study of Bank Overdraft Programs, FDIC, November 2008, pages ii – iv, http://www.fdic.gov/bank/analytical/overdraft/FDIC138_Report_FinalTOC.pdf

⁹⁴ CFPB Study of Overdraft Programs: White Paper of Initial Data Findings, CFPB, June 2013, page 19, <http://www.consumerfinance.gov/reports/the-cfpb-study-of-overdraft-programs/>

amended Regulation DD to require new disclosures about overdraft fees and account balances (effective January 2010). Nearly concurrently with the latter amendment, the Board amended Regulation E (which implements the Electronic Fund Transfer Act) to require that consumers provide affirmative consent for overdraft coverage of ATM withdrawals and non-recurring debit card transactions (generally at the point of sale or POS) before institutions can charge overdraft fees on such transactions. This amendment was effective as of January 2010, with a mandatory compliance date of July 1, 2010 for new customers and August 15, 2010 for existing customers.

Continuing concerns about consumer protection and institutional safety and soundness stemming from overdraft programs were reflected in final guidance issued by the FDIC in 2010, proposed guidance from the OTS in 2010, and proposed guidance from the OCC in 2011 (which the OCC recently withdrew). The only extant supervisory guidance is that issued by the FDIC which applies only to institutions supervised by the FDIC.”

The CFPB report goes on to evaluate the current status and use of overdraft protection programs since the implementation of the revised rules concerning disclosures, opt-in requirements and order of batch transaction processing. During 2011, 27.8% of account holders had an occurrence of a not sufficient funds (NSF) status or use of automated overdraft protection at least once, with 20.1% having 1 – 10 NSF/overdrafts and 7.7% of account holders (28% of those with NSF/overdrafts) having more than 10.⁹⁵ Surveyed banks also had 12.8% of account holders enrolled in LOC programs and 28% in linked-account programs.⁹⁶

By comparison, the DMDC survey showed that 5% of enlisted Service members were enrolled and used automated overdraft protection, 10% LOC programs and 20% linked account programs.⁹⁷ Of those who participated in automated overdraft protection, 9% had overdrafts at least once per month, 16% twice per month and 9% every week (34% used automated overdraft protection at least 12 times per year).⁹⁸ In comparison to civilian account holders, fewer enlisted Service members are enrolled in automated overdraft protection; however, a higher percentage of enlisted members use the program than civilian account holders. Similarly, of the 10% of enlisted Service members who used LOC programs, 20% had overdrafts once per month, 18% twice per month and 3% every week (41% used LOC programs at least 12 times per year).⁹⁹

⁹⁵ Ibid, page 21

⁹⁶ Ibid, page 56

⁹⁷ DMDC QuickCompass of Financial Issues, 2013, Question 30, Appendix B: “Have [you][your and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?”

⁹⁸ Ibid, Question 50, Appendix B: “In the last 12 months about how often did you use overdraft loans?”

⁹⁹ Ibid, Question 52, Appendix B: “In the last 12 month, how often did you use an overdraft line of credit?”

Finally in comparison to these self-reported statistics of the use of automated overdraft protection, a recent article in the Wall Street Journal analyzed the amount of revenue banks obtained through automated overdraft protection, with specific focus on the revenue gained by banks on military installations. Their analysis looked at the fee revenue of 7,000 banks through their public filings and estimated the revenue of automated overdraft protection based on industry norms. “The filings don’t break out overdraft charges. But federal regulators generally estimate that overdraft fees make up the majority of bank service charges. Moebs Services Inc., a banking research and consulting firm, estimates the figure is close to 75%.”¹⁰⁰ The Wall Street Journal compared these estimated revenues against total deposits and the number of accounts held by each institution.¹⁰¹ They found that four banks on military installations were among the top ten with highest revenue per account, with revenue per account of \$234 - \$608, compared to the weighted average of \$56 per account.¹⁰² Considering that self-reported survey data shows that enrollment in overdraft programs is less than the general population and use is slightly higher (34% compared to 29%), these revenue statistics may again show that the DMDC survey data under-reports actual use.

Since the implementation of the MLA in 2007, a handful of banks developed deposit advance loans to fill a need bank members may have for emergency cash (as reported on their websites). However, prudential regulators have become increasingly concerned about these short term loans that act in a similar manner as payday loans. The Federal Reserve Board advised: “State member banks are expected to consider the risks associated with deposit advance products, including potential consumer harm and the potential for elevated compliance risk, when designing and offering such products.”¹⁰³ The FDIC articulated in their proposed guidance with request for comment: “These loans typically have high fees, are repaid in a lump sum in advance of the customer’s other bills, and often do not utilize fundamental and prudent banking practices to determine the customer’s ability to repay the loan and meet other necessary financial obligations.”¹⁰⁴

The statements from bank regulators followed shortly after the CFPB released a report on the use of deposit advance loans. This report covered 100,000 eligible accounts (about half of account

¹⁰⁰ Mark Maremont and Tom McGinty, “Hefty Bank Fees Waylay Soldiers,” *The Wall Street Journal*, January 15, 2014, <http://online.wsj.com/news/articles/SB10001424052702304887104579306770984874320>

¹⁰¹ This analysis does not appear to consider that many banks operating on military installations also operate in locations outside military installations. Additionally, it does not consider other sources of non-interest income received such as payments from organizations for in-store banking as well as compensation from the US Treasury for performing functions associated with serving as official depositories of the US government. As such, non-interest income charged per account should not be assumed to be the result of individuals using products resulting in bank service charges.

¹⁰² Ibid

¹⁰³ <http://www.federalreserve.gov/bankinforeg/caletters/caltr1307.htm>

¹⁰⁴ Proposed Guidance on Deposit Advance Products, FDIC, page 3, <http://www.fdic.gov/news/news/press/2013/pr13031a.pdf>

holders in the institution studied were eligible), of which approximately 15% used bank advance loans.¹⁰⁵ The DMDC survey results show that 3% of enlisted Service members used bank advances in the past 12 months.¹⁰⁶ The CFPB report describes account holders use of bank advances in terms of the balance during the period of an advance (may be the result of several simultaneous advances), the amount of time account holders had advances, and the total amount of these advances during a 12 month period. The average amount of an advance balance in 2011 was \$343 (as opposed to the average amount of an advance, which was \$180).¹⁰⁷ During a 12 month period, the median number of advances was 8 and the median amount of time during which account holders had these loans was 7 months.¹⁰⁸

The DMDC survey results showed that the average number of months enlisted respondents had used bank advance loans was 3.6 and 59% of them said that they borrowed more than \$300 as their most recent bank advance.¹⁰⁹ The DMDC results show the percentages of enlisted Service members within ranges of months (75% had loans for 1 – 3 months, 10% for 4 – 6 months, 3% for 7 – 9 months and 12% for 10 – 12 months).¹¹⁰ The CFPB study compares the number of months in which an account holder had bank advances compared to the total amount borrowed during a 12 month period (Figure 3).¹¹¹

¹⁰⁵ CFPB Study of Payday Loans and Bank Advance Products: White Paper of Initial Data Findings, CFPB, April 24 2013, page 27, http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

¹⁰⁶ DMDC QuickCompass of Financial Issues, 2013, Question 30, Appendix B: “Have [you][your and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?”

¹⁰⁷ CFPB Study of Payday Loans and Bank Advance Products: White Paper of Initial Data Findings, CFPB, April 24 2013, page 36, http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

¹⁰⁸ Ibid, page 39

¹⁰⁹ DMDC QuickCompass of Financial Issues, 2013, Question 35, Appendix B: “What amount did you borrow against your paycheck for your most recent bank direct deposit advance loan?”

¹¹⁰ DMDC QuickCompass of Financial Issues, 2013, Question 34, Appendix B: “In how many of the past 12 months did [you][you and/or your spouse][you and/or your partner or significant other] have bank direct deposit advance loans?”

¹¹¹ CFPB Study of Payday Loans and Bank Advance Products: White Paper of Initial Data Findings, CFPB, April 24 2013, page 39, http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

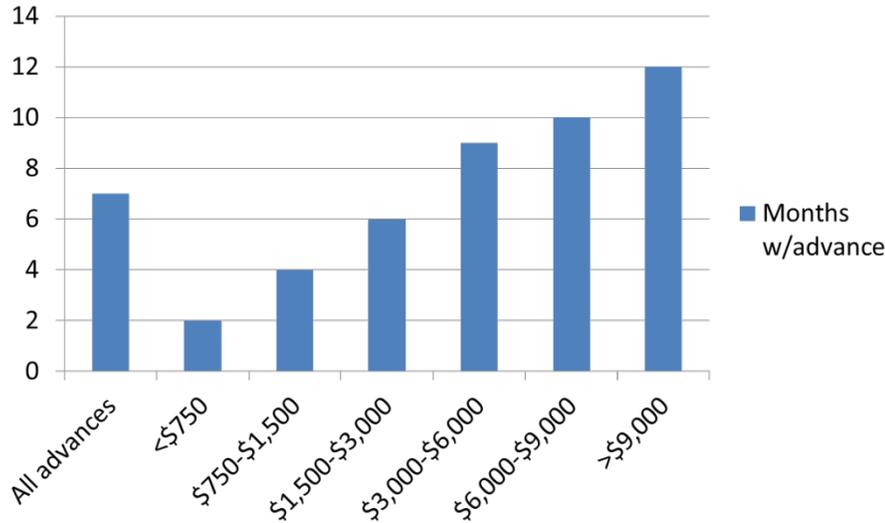


Figure3: CFPB study showing the number of months with an advance reported for account holders and the total amount borrowed during a 12 month period.

During the period of the CFPB study and the DMDC survey, there were at least seven banks offering these loans. Following the guidance from the OCC and FDIC, the large banks offering bank advances recently announced that they would no longer be providing these products in their current form. “The issue reached a climax in November [2013], when the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corp. imposed tighter restrictions on the loans. Regulators did not bar banks from offering the product, but the new rules were stringent enough to make the line of business untenable, banks say.”¹¹²

Although this probably signals that the product will no longer be available, spokespersons for some of the institutions involved made statements about follow-on actions, such as: the financial institution is “committed to finding new solutions that meet the needs of all of our customers and fit within the current regulatory expectations,”¹¹³ and “[t]he Bank has been monitoring industry developments and has proactively engaged with stakeholders as it has looked at the clear and continued need for small dollar, short-term credit solutions for its customers.”¹¹⁴ Perhaps it is to be expected that financial institutions would consider any further options in light of new regulation; however, the development of new products may promulgate new concerns not previously addressed.

Finally as part of a review of federally regulated products, this report will make comment about credit cards. In 2006 and 2007, the Department did not initially examine whether to include credit cards within the scope of the MLA implementing regulation. In 2008 as part of their

¹¹² Danielle Douglas, “Wells Fargo, U.S. Bank to end deposit advance loans, citing tougher regulation,” Washington Post, January 17, 2014, http://www.washingtonpost.com/business/economy/wells-fargo-us-bank-to-end-payday-loans-citing-tougher-regulation/2014/01/17/b65f0512-7f82-11e3-93c1-0e888170b723_story.html

¹¹³ Ibid

¹¹⁴ Ibid

response to DoD's request for information, consumer advocates included "fee-harvester" cards, which had high application fees and low credit limits to generate additional fees by producing over-limit balances. Since 2008, there have been several key changes in the regulation of credit cards, starting with the Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009. Subsequent to the Act, the Federal Reserve Board and the CFPB released regulations effective in October 2011, which addressed disclosures, solicitations, ability of card applicants to repay credit, ability of the card issuers to increase interest rates and limitations to certain fees. The CARD Act "restricts the amount of 'upfront' fees that an issuer can charge during the first year after an account is opened, and limits the instances in which issuers can charge 'back-end' penalty fees when a consumer makes a late payment or exceeds his or her credit limit."¹¹⁵

According to the requirements established in the CARD Act, the CFPB conducted a review of the Act's impact on consumers two years after implementation. The review found that the Act has resulted in some positive changes in the credit card market. Fees charged card holders for exceeding limits have largely been eliminated. The Act requires card issuers to give card holders 45 days-notice on any increases to interest rate and as a result, card issuers have largely eliminated increases resulting from late payments or other reasons defined by the issuer. As a result of these changes, interest rates increased as the back-end fees and rate changes were decreased or eliminated. These changes have helped simplify credit card agreements and disclosures, and card costs have become more aligned with the disclosed annual fees and interest rates.¹¹⁶

The CFPB review determined the CARD Act impacted access to credit in three ways: there was a substantial decrease in the number of credit card accounts held by consumers under 21 years old; there was a small decrease in the number of applicants being approved, based on their income and potential inability to repay debt; and a significant decrease in card holders receiving unsolicited increases in credit limits. The DMDC survey asked Service members about their credit card use. Respondents said they had an average of 2.4 cards,¹¹⁷ with 70% having interest rates on the card with highest interest rate below 24%, 5% between 25% and 36%, none above 36% and 15% not knowing their interest rate.¹¹⁸ They were also asked about the fees associated with the card they had with the highest interest rate. They were also asked: "Were any of the following required to get the card with the highest APR?"¹¹⁹

¹¹⁵ CARD Act Report: A review of the impact of the CARD Act on the consumer credit card market, CFPB, October 1, 2013, page 4, <http://www.consumerfinance.gov/reports/card-act-report/>

¹¹⁶ Ibid, page 5

¹¹⁷ DMDC QuickCompass of Financial Issues, 2013, Question 55, Appendix B: "How many credit cards do [you] [you and your spouse] [you and your partner or significant other] have?"

¹¹⁸ Ibid, Question 57, Appendix B: "What is the highest APR (interest rate) [you] [you and your spouse] [you and your partner or significant other] are paying on a credit card with a balance?"

¹¹⁹ Ibid, Question 58, Appendix B

	Yes	No	Don't know
Automatic payment from your bank account	12%	83%	5%
A military allotment (the military automatically takes money from your paycheck to pay your credit card bill)	6%	89%	5%
Annual membership fee	13%	81%	6%
Monthly membership fee	4%	90%	6%
Security deposit/fee or processing fee	5%	90%	5%
Fee to access account online	2%	96%	2%
Cash advance fees	13%	79%	8%

Table 1: Enlisted Service member survey responses concerning payment and fees of their credit cards with the highest interest rate.

Few respondents said that they had additional fees associated with the use of their credit card, to include cash advances, even though cash advances almost always incur a higher interest rate and/or a fee.¹²⁰ Respondents were also asked about their payment experience and use of cash advances. They were asked: “In the past 12 months, which of the following describes [your] [your and your spouse's] [your and your partner's or significant other's] experience with credit cards? [I] [We]...”¹²¹

	Yes	No	Don't know
Always paid credit cards in full	30%	66%	4%
Sometimes carried-over a balance	54%	42%	4%
Sometimes paid only the minimum payment	54%	44%	2%
Sometimes had a late fee charged	18%	79%	3%
Sometimes used the cards for a cash advance	13%	85%	2%

Table 2: Enlisted Service member survey responses concerning their experience with paying their credit cards, being charged a late fee and using the card for a cash advance.

Although only about a third said that they always paid their card balances off in full, almost half said that they did not carry over a balance. An equal number of those who said they carried over a balance also said they sometimes only made the minimum payment. Finally, the same percentage who said they had used a cash advance recognized that they had paid a fee for that advance.

There has been considerable change in Federal policy with respect to RALs, overdraft protection programs, bank draft deposits and credit cards. The need for changes in regulation may have been promulgated by innovations in financial products that were made to meet market demands and enhance profitability of institutions. Although current rule changes have curtailed the concerns raised by advocacy groups in 2008 – 2011, these changes provide little indication that

¹²⁰ <http://creditcardforum.com/blog/no-cash-advance-fee-credit-card/>

¹²¹ Ibid, Question 56, Appendix B

future industry innovation may not require additional regulatory authority to adequately protect consumers. This is the circumstance in which DoD has been presented with respect to the implementation of the MLA. The regulation for the MLA had been seen as an adequate balance between restriction and access at the time of its implementation, but changes in the marketplace have emphasized that changes to the regulation are needed at this time. As part of DoD's effort to understand the nature of these changes, DoD requested the perspective of consumer advocacy groups, industry representatives, and interested individuals.

PERSPECTIVE OF RESPONDENTS TO THE DOD ANPR

DoD posted an ANPR in the Federal Register on June 17, 2013 through August 1, 2013,¹²² requesting public comment on the report request made on pages 782 and 783 of House Report 112-329, to accompany H.R. 4310. Specifically, the ANPR requested the public respond to the following four questions:

- (1) The need to revise the implementing regulation (32 CFR Part 232), with special attention to the definition of covered consumer credit;
- (2) If there is a need for change, what should be included in any revision and why;
- (3) What should not be included in any revision and why; and
- (4) Examples of alternative programs designed to assist Service members who need small dollar loans.

Perspective provided in the responses depended primarily on the role of the respondents or the constituents the respondents represented. Eleven letters from 5 bank associations, 7 credit union associations/affiliates/councils/leagues, 2 financial services/installment lender associations, one credit union and one financial services company¹²³ expressed their satisfaction and support for the current regulation and warned against the potential for unintended consequences if the definitions are extended. Four of the responses from credit union associations and the one financial services company¹²⁴ went further to say DoD should continue to take targeted action through the regulation against problematic lenders. Three responses from rent-to-own (RTO) companies¹²⁵ expressed that RTO is not credit and therefore should not be subject to the regulation and that RTO is "an attractive marketplace choice for many, including some service

¹²² Docket ID: DoD-2013-OS-0133

¹²³ Letters from (1) the Credit Union National Association and the Defense Credit Union Council, (2) Desert Schools Federal Credit Union, (3) Georgia Credit Union Affiliates, (4) Michigan Credit Union League and Affiliates, (5) Missouri Credit Union Association, (6) National Association of Federal Credit Unions, (7) Ohio Credit Union League, (8) the American Bankers Association, Association of Military Banks of America, Consumer Bankers Association, The Financial Services Roundtable, Independent Community Bankers of America, and National Association of Federal Credit Unions, (9) American Financial Services Association, (10) National Installment Lenders Association, (11) Omni Financial Inc.

¹²⁴ Letters from (1) Desert Schools Federal Credit Union, (2) Georgia Credit Union Affiliates, (3) Michigan Credit Union League and Affiliates, (4) Ohio Credit Union League, (5) Omni Financial Inc.

¹²⁵ Letters from (1) Aaron's Inc., (2) Association of Progressive Rental Organizations, (3) Rent-A-Center,

members.”¹²⁶ The response from the online lenders defended the need for access by Service members to small dollar, short term credit.¹²⁷ Seven letters from 45 consumer advocacy groups¹²⁸ advocated extending the scope of the definitions in the regulation, and 44 consumer groups recommended extending the definitions to cover all credit subject to TILA.¹²⁹ One of the Military Relief Societies, a national veterans support organization and two individuals also provided input to extend the definitions in the regulation.¹³⁰

The perspective of agencies within state governments has been particularly insightful to the Department, since many of these organizations have oversight and enforcement responsibility over several of the credit products in question. Fourteen State Attorneys General¹³¹ recommended covering the full range of credit products and advocated including overdraft protection and RTO. Three State Departments of Veterans Affairs¹³² and the association representing 49 state credit regulators¹³³ recommended covering all credit subject to TILA. Finally, a letter signed by 54 Members of the House of Representatives recommended extending the definitions to close loopholes that allow continued access to payday and vehicle title loans, and a letter signed by 23 Senators advocated extending the definitions, along with covering installment loans.

Loan providers expressed their concern that changes in the MLA may have unintended consequences for military borrowers (such as limiting credit), add to their regulatory burdens, or

¹²⁶ Letter from the Association of Progressive Rental Organizations

¹²⁷ Letter from the Online Lenders Alliance

¹²⁸ Letters from (1) Alabama Appleseed, Alabama Arise, Americans for Financial Reform, Baltimore CASH Campaign, California Reinvestment Coalition, Chicago Consumer Coalition, Citizen Action/Illinois, Coalition on Homelessness and Housing in Ohio, Consumer Assistance Council of Cape Cod and the Islands, Consumer Federation of America, Consumer Federation of California, Consumer Federation of the Southeast, Consumers for Auto Reliability and Safety, Consumers Union, The Delaware Community Reinvestment Action Council, Inc., Economic Fairness Oregon, GRO Missouri, Heartland Alliance for Human Needs and Human Rights, Illinois Asset Building Group, Jesuit Social Research Institute – Loyola University New Orleans, Kentucky Equal Justice Center, The Leadership Conference on Civil and Human Rights, Maryland CASH Campaign, Maryland Consumer Rights Coalition, Msgr. John Egan Campaign for Payday Loan Reform, NAACP, National People’s Action, North Carolina Justice Center, Policy Matters Ohio, Reinvestment Partners, RAISE KY, Sargent Shriver National Center on Poverty Law, South Carolina Appleseed Legal Justice Center, Southwest Center for Economic Integrity, Texas Appleseed, U.S. Public Interest Research Group, Virginia Citizens Consumer Council, Virginia Partnership to Encourage Responsible Lending, Virginia Poverty Law Center, (2) Cities for Financial Empowerment Coalition, (3) Woodstock Institute (4) Texas Appleseed, (5) Sargent Shriver National Center on Poverty Law, (6) The Pew Charitable Trusts, (7) Consumer Federation of America, The Center for Responsible Lending, National Association of Consumer Advocates, National Consumer Law Center

¹²⁹ All groups listed in footnote 39, except for The Pew Charitable Trusts.

¹³⁰ Letters from The American Legion, Navy-Marine Corps Relief Society, Mr. Michael Archer, Mr. Bobby L. Allen

¹³¹ Letters from (1) Attorneys General of California, Delaware, Florida, Illinois, Indiana, Kentucky, Montana, Nevada, New York, North Carolina, Oregon, Tennessee, Washington, (2) Attorney General of Colorado

¹³² Letters from (1) Illinois Department of Veterans Affairs, (2) Tennessee Department of Veterans Affairs, (3) Washington Department of Veterans Affairs

¹³³ Letter from the National Association of Consumer Credit Administrators representing all states except Arkansas and New York

restrict their ability to offer high cost loans. Consumer advocates and state officials said that if the MLA has been designed to protect military borrowers from high cost loans (even if limited to payday and vehicle title loans), the MLA cannot fulfill its role without considering loans with longer terms (that can feature installments), open-end credit, and increased principal. These opposing viewpoints lead to the important question whether the limitations provided by the MLA since 2007 can be continued without creating undesirable consequences. This may be an appropriate point to consider these protections and the comments for and against applying them to a broader list of credit products.

The financial industry respondents found that the limitations, along with the administrative requirements of the MLA would create “unintended consequences” if the definitions in the regulation are extended beyond their current status. For example, they view the 36% cap as applied and administered by the MLA¹³⁴ will complicate existing TILA disclosures and make disclosures confusing for military borrowers. The additional requirement of providing these disclosures orally, as well as in writing, exacerbates the administration of any credit transaction according to the law, particularly if the offer is made by mail or over the internet. Other limitations also create concerns for creditors: prohibition on arbitration will require them to redraft contracts for Service members, eliminating the use of a car title will prohibit using a car as collateral as part of any loan agreement, and military borrowers would not be able to refinance a loan to lower terms. In all, the financial industry respondents view the imposed limitations and administrative requirements as potentially creating inherent unintended consequences, or potentially creating an environment where creditors will no longer want to offer credit at terms well below the 36% MAPR, which they view as perhaps the most profound consequence. Of course, each of these potential outcomes is dependent on the definitions that extend the coverage of the MLA, and upon how the limitations are implemented in the regulation with respect to the credit covered. For example, concern over the implementation of oral disclosures for mailed and internet credit offers was mitigated in the 2007 regulation by allowing creditors to provide a toll-free number. Other similar mitigations may be possible to cover unintended consequences of limitations and administrative requirements.

Consumer groups, interested individuals, state agencies and members of the House and Senate see the interest rate cap as a way of prohibiting access by military consumers to credit that characteristically has weaker underwriting standards and consequently depends on higher interest rates (to cover the cost of potential increases in default) and payment secured through access to assets (such as an allotment of pay, access to bank account, holding a check or a vehicle title). As already mentioned, all of these respondents urged the Department to close loopholes that allow creditors to offer this kind of credit and the majority of respondents advocate including all

¹³⁴ The MLA calls for all fees, charges, interest and cost of ancillary products sold with the extension of credit to be included in the annual percentage rate cap of 36%. This is referred to as the Military Annual Percentage Rate (MAPR). The MLA requires the MAPR to be disclosed to the borrower along with TILA disclosures.

credit defined in TILA (not otherwise already excluded in the MLA), which includes installment and open-end forms of credit and credit cards. As already discussed, the current ability to provide credit above 36% MAPR outside of the current definitions in the MLA is becoming more evident and of greater concern, and without revising the definitions of credit in the MLA to encompass installment and open end credit, the MLA will lose its effectiveness with respect to providing a limit on any form of credit identified in the regulation. Also as noted above, including definitions that encompass all credit defined in TILA could mean that the limitations and administrative requirements included in the MLA may apply to loans and lines of credit offered below the 36% MAPR threshold. Again, the approach taken in drafting any change will make considerable difference in the effectiveness of protections provided on credit below the threshold and many of the respondents view the extension of the MLA protections, such as the prohibition of mandatory arbitration, as a positive outcome.

SUMMARY: APPLYING LIMITS TO CREDIT THROUGH THE MLA

In the final analysis, the question comes to whether the current MLA regulation is sufficient to address the concerns of the Department regarding the use of credit by Service members? Financial counselors and legal assistance attorneys rated the high cost of credit as the most often seen negative characteristic of credit that contributed to the problems experienced by their clients.¹³⁵ They see availability of high cost credit as a hazard to military borrowers; however, others believe it is a necessary component to their financial viability. The Online Lenders Alliance (OLA) stated in their response to the ANPR: “OLA believes that it is vital that these [military] families retain broad access to credit products, especially short-term, small-dollar loans, to bridge the gap of unexpected shortfalls.” As previously discussed, the Military Relief Societies are chartered to address these shortfalls and provide grants and no interest loans to assist Service members and their families. Additionally, the Department allows Service members to obtain an advance on pay to accommodate out-of-pocket expenses as a result of permanent change of station moves. Advances are approved within parameters designed to protect the Service member’s ability to repay the advance without negative impact on their ability to manage their finances. The amount of the advance can be increased and the time required to repay the advance can be extended, depending on the extenuating circumstances of the Service member.¹³⁶ OLA did not list these alternatives in its discussion of resources available to military consumers to bridge the gap of unexpected shortfalls.

DoD also asked financial counselors and legal assistance attorneys: “Do you think a limit of 36% APR on all available credit would create problems for Service members and their families? [and] What will happen to Service members with bad credit?” Two hundred and fifty-two

¹³⁵ Question 8, Appendix A; average rating was 3.6 – between “sometimes and often”

¹³⁶ DoD Instruction 1340.18, “Advance Pay Incident to a Permanent Change of Station (PCS) for Members of the Uniformed Services,” September 11, 2012

respondents provided narrative answers. Respondents understood the questions differently; however, their responses lead to a conclusion on whether a restriction of credit to a limit of 36% APR would be detrimental. Forty-three percent of respondents said they did not believe a limit of 36% APR would create problems for Service members and their families. An additional 44% said that such a limit would be detrimental, but because the limit was set too high. Both groups (87% of respondents) validated the perspective that an APR of 36% would not disenfranchise Service members and their families by being too restrictive. Approximately four percent were concerned that the limit could cause harm by being too restrictive and another five percent were not clear in their response whether they were concerned because the limit was too high or too restrictive. Finally, there were another four percent who provided general comments about credit not related to the 36% APR limit.¹³⁷

The current usage level of each product with an APR of over 36% might signal that further regulation would not be proportional to the adjustments the credit market might need to undertake to accommodate the restrictions imposed by the MLA. However, this report has already stated that respondents may have under-reported their use of these products or may have been uncertain about various terms of their loans. Eleven percent of enlisted Service members reported using payday loans, vehicle title loans, bank deposit advances, pawn shop loans and/or installment loans with interest rates over 36% APR.¹³⁸ This represents a significant percentage of the enlisted force. Reviewing the financial status of this subgroup, as compared to all enlisted Service members, shows that on average, there were twice as many of them having negative characteristics:

¹³⁷ Question 7, Appendix A

¹³⁸ DMDC QuickCompass of Financial Issues, 2013, Question 30, Appendix B: "Have [you][your and/or your spouse][you and/or your significant other] used any of the following financial products or services to cover expenses in the past 12 months?" The percentage reflects only respondents who had used one or more of the products listed.

Characteristic	Subgroup	All
Had one or more financial difficulties in the past 12 months: more than 60 days late on mortgage or other debts, unable use to credit card (maxed limit), short on cash between paychecks, unable to pay monthly bills. ¹³⁹	81%	48%
Had problems 5 or more months in the past year with financial difficulties. ¹⁴⁰	37%	23%
Rated their credit history as bad or very bad. ¹⁴¹	29%	12%
Described their financial condition as “tough to make ends meet, but keeping your head above water,” or “in over your head.” ¹⁴²	33%	12%
Described their financial situation as “somewhat worse,” or “much worse” compared to twelve months ago. ¹⁴³	36%	20%

Table 3: Comparison of enlisted Service members who reported using payday loans, vehicle title loans, bank deposit advances, pawn shop loans and/or installment loans with interest rates over 36% APR with all enlisted Service members who responded to the DMDC survey questions concerning the personal finances and credit.

DoD sees the limitations provided by the MLA as essential for directing individuals away from continued use of high cost products. Additionally, the broad consensus of respondents of the ANPR, DoD financial counselors and DoD legal assistance attorneys all believe the protections afforded to Service members and their families under the MLA are important and should be continued. Representatives of the financial industries believe the current regulation adequately defines problematic credit. However, some lenders who had specialized in traditional closed-end payday or vehicle title loans are now offering installment products or hybrid products with characteristics of payday/vehicle title and installment loans. In addition, some lenders are offering open-end variations of payday and vehicle title loans. Since these optional approaches are not in violation of the state laws where these lenders operate, there is no reason to believe these approaches will cease, and they may expand if viewed as being profitable. To adjust to this new environment, the 45 consumer advocacy groups that responded to the DoD ANPR unanimously said that DoD should expand the definitions in the implementing regulation, and this position was also supported by all respondents from state governments and the U.S. Congress.

For DoD, the question has been how best to modify the definitions in the regulation to provide consistent and comprehensive coverage of the credit market and provide for the potential that

¹³⁹ Ibid, Question 28, Appendix B: “During the past 12 months, did any of the following happen to [you][you and your spouse][you and your partner or significant other]? [I was][We were]...”

¹⁴⁰ Ibid, Question 29, Appendix B: “In how many of the past 12 months were [you][you and your spouse][you and your significant other] short on cash, unable to use a credit card because of the credit limit was reached, or unable to pay bills or other debts?”

¹⁴¹ Ibid, Question 25, Appendix B: “How would you rate your credit history?”

¹⁴² Ibid, Question 13, Appendix B: “Which of the following best describes [your financial condition][the financial condition of you and your spouse][the financial condition of you and your partner or significant other]?”

¹⁴³ Ibid, Question 14, Appendix B: “Compared to 12 months ago, is [your financial situation][the financial situation of you and your spouse][the financial situation of you and your partner or significant other] better, worse, or has it stayed the same?”

lenders may not be satisfied with the status quo and may continue to find other ways of offering credit, some of which may have detrimental terms. Conceptually, there are two approaches to modifying the definitions: (1) as has been done in the past, cover each product individually, being sufficiently broad in scope for each, as well as succinct in defining terms to preclude unintended coverage; or (2) cover all products and create exceptions where there are important caveats that should be recognized.

Defining individual products may be a sensible approach if the Department's objective is to selectively target specific products in the marketplace that are projected to be problematic. This is the approach taken to define the scope of the initial regulation; however, the credit marketplace has changed in the past seven years and is likely to continue to change as state laws, consumer attitudes, market opportunities and regulatory focus evolve. Revising the definitions of the existing products in the regulation to overcome current concerns and criticisms would require writing definitions that either would impinge on other forms of credit, or would continue to be inadequate. For example, defining payday loans in order to cover loans with terms longer than 91 days could become complicated. Eliminating the term limit of the loan is simple enough; however, would longer loans continue to be paid in one lump-sum or in installments? To define the loans as having lump-sum payments would leave a significant loophole for payday loans paid in installment. If the definition included payday loans paid for in installments, how would these loans be differentiated from other installment loans? There may be other factors that could be used to discern installment payday loans from other installment loans, but each of these factors could then be used as a loophole to evade the protections of the MLA.

If the Department could craft a definition that covered payday loans without covering installment loans, because some lenders offer both products, a Service member could be directed toward the product not covered by the MLA. The same concerns could be raised about definitions covering open-end forms of payday and vehicle title loans and the availability of other high cost open-end loans offered by the same lender. Specific definitions of problematic credit no longer function well in the current marketplace. The complexity of the marketplace appears to be better accommodated with a more comprehensive approach. Accordingly, the Department is working on such a comprehensive approach in its redrafting of the implementing regulation for the MLA.

APPENDIX A: POLL OF DOD FINANCIAL COUNSELORS AND LEGAL ASSISTANCE ATTORNEYS

- A. DoD requested the Military Services distribute a questionnaire to financial counselors and legal assistance attorneys to obtain their feedback. The questionnaire included only 10 questions, which mostly requested narrative responses. The questionnaire had the following opening paragraphs to explain the reason for our inquiry:

The Conference Report for the National Defense Authorization Act for Fiscal Year 2013 requires the Secretary of Defense to survey Service members, poll DoD legal assistance attorneys and DoD financial counselors, and request input from consumer advocates and industry to evaluate changes in credit markets that may be harmful to Service members and their families and to report back to the Congress by the end of calendar year 2013.

This “quick poll” has been designed to obtain feedback from DoD financial counselors [legal assistance attorneys] on lending products in general that are above 36% APR. Additionally, we ask a question on negative characteristics of lending products that tend to get your clients into trouble.

DoD financial counselors [legal assistance attorneys] can provide a valuable perspective since they see Service members who have either found themselves needing assistance or have been directed to obtain assistance because of financial difficulties, sometimes from accumulation of too much debt and/or the use of credit products that create a debt spiral. Previous studies have shown that Service members and their families will sometimes attempt to extend their credit using products that someone with a good credit rating would not consider.

The MLA was enacted to limit opportunities for active duty Service members and their families to become involved with high cost products, which they often times continue to refinance. We need feedback on your recollection of how often you have clients that have high cost loans and if possible, why they took these loans. Specifically did they get the high cost loan because they had no option, or because they thought this was the best option they had available? This quick poll has a limited scope on requesting feedback on credit products: the MLA doesn't cover mortgages and auto financing, so our information request does not consider these credit products.

We will be separately surveying active duty Service members through the Defense Manpower Data Center on the credit products they use (outside of mortgages and auto financing), and we will also ask consumer advocates, financial industries and other concerned individuals for feedback through the Federal Register about credit that may be

harmful to Service members and their families. We appreciate the important role you play in the lives of Service members and their families, and we appreciate your input to help us determine what may require additional restrictions.

B. Overall, there were 270 responses received to the questionnaire. The questions are provided below, with the aggregate or summarized responses to each question provided in italics:

1. Which of the following best describes your employment category?
 - a. Member of the military (active, guard or reserve): *89*
 - b. DoD civilians: *181*

2. Where do you work? (In which organization and location have you been working for the past six months)
 - a. Organization: *52 Army; 81 Navy; 34 Marine Corps; 104 Air Force*
 - b. Location: *224 in various states; 46 in locations overseas*

3. What do you do? (What role did you perform the majority of your time over the past six months?)
 - a. Administrator overseeing financial counseling program: *31*
 - b. Financial counselor seeing clients: *149*
 - c. Unit financial specialist assisting Service members: *29*
 - d. Administrator overseeing legal assistance program: *15*
 - e. Legal assistance attorney seeing clients: *46*

4. On a monthly basis, what is the average number of clients who: (total, overall average, and applicable percentage shown)
 - a. You see for legal assistance/financial counseling? *7048; average 26*
 - b. Have some problem with loans or credit? *2443; average 9; 34.7% of all clients*
 - c. Have loans with over 36% APR (payday, vehicle title and/or installment): *383; average 1; 15.7% of clients with loan/credit problems*
 - d. Have lines of credit with over 36% APR (payday, vehicle title, bank deposit advance, credit cards, etc.): *350; average 1; 14.3% of clients with loan/credit problems*
 - e. Have voluntary allotments to financial institutions for products/services other than investments and insurance?: *2158; average 8; 88.3% of clients with loan/credit problems*

5. Based on your experience with clients, have you heard them make the following statements concerning the use of credit products with APRs over 36%? (response provided to the following statements using a Likert Scale: Not at all = 1; Seldom = 2; Sometimes = 3; Often = 4; Very often = 5)

- a. For Financial Counselors:
 - i. Client has expenses that are consistently greater than income: *205 responses; 3.6 average*
 - ii. Client has a high debt to income ratio: *205 responses; 3.8 average*
 - iii. Client has had a sudden loss of income, either second job or spouse's income: *205 responses; 2.9 average*
 - iv. Client had unexpected expenses, such as car repair, PCS moving expenses, etc.: *204 responses; 3.8 average*
 - v. Client has maxed-out existing credit or has been turned down for additional credit: *204 responses; 3.4 average*
 - vi. Other (please specify below): *86 responses; 3.6 average*
 - b. For Legal Assistance Attorneys:
 - i. Only choice available because other sources turned your client down: *56 responses; 2.1 average*
 - ii. Only choice your client thought available: *56 responses; 2.2 average*
 - iii. A friend told your client about the loan being easy to obtain: *55 responses; 1.8 average*
 - iv. Advertising made it sound like a sure thing: *56 responses; 2.2 average*
 - v. It was where your client got his or her previous loan: *56 responses; 2.0 average*
 - vi. Other (please specify below): *49 responses; 1.8 average*
6. Please describe notable credit products you have seen clients use to extend their credit beyond what their FICO score or established credit limits on other products would afford them. Also, please describe notable credit products that were the primary cause for clients seeking assistance.

Two hundred and twenty-eight respondents answered in narrative. Some of the products mentioned more often were purchases of cars, appliances and furnishings (59 times); credit cards (54 times); Pioneer Lending (45 times); Omni Loans (33 times); payday loans (31 times); vehicle title loans (29 times); overdraft protection (17 times); and student loans (17 times).

7. Do you think a limit of 36% APR on all available credit would create problems for Service members and their families? What will happen to Service members with bad credit?

Two hundred and fifty-two respondents answered in narrative. Respondents understood the question differently; however, we can still draw a conclusion on whether a restriction of credit to a limit of 36% APR would be detrimental. Forty-three percent of respondents said they did not believe a limit of 36% APR would

create problems for Service members and their families. An additional 44 percent said that such a limit would be detrimental because the limit was set too high. In the context we have been considering this question, these respondents validated that the limit would not disenfranchise Service members and their families by being too restrictive. Consequently, 87 percent did not see a limit of 36% as adversely restricting credit. Approximately four percent were concerned that the limit could cause harm by being too restrictive and another five percent were not clear in their response whether they were concerned because the limit was too high or too restrictive (we have asked these respondents to provide clarification). Finally, there were another four percent who provided general comments about credit not related to the 36% APR limit.

8. We are also interested in evaluating the extent to which negative characteristics of credit contribute to the problems experienced by your clients. Please rate how often you have seen the following negative characteristics have impacted your clients. (response provided to the following statements using a Likert Scale: Not at all = 1; Seldom = 2; Sometimes = 3; Often = 4; Very often = 5)

- a. Loans secured on considerations other than the borrower's ability to repay the loan: *241 response; 2.8 average*
- b. Mandatory arbitration: *221 responses; 2.0 average*
- c. Mandatory use of allotments to secure the loan: *251 responses; 2.9 average*
- d. High interest rates and/or large additional fees: *262 responses; 3.6 average*
- e. Unclear or deceptive information provided to the borrower prior to signing: *247 responses; 3.1 average*
- f. Too little time provided to repay the loan: *250 responses; 2.4 average*
- g. Unnecessary additional services and other charges included with the loan: *247 responses; 3.0 average*
- h. Rolling-over, flipping or refinancing of loans without significant reduction in the principal: *254 responses; 2.9 average*
- i. Other (specify below): *57 responses; 2.8 average*

9. Please provide any additional comments you may have concerning negative characteristics of credit:

One hundred and sixty-three respondents answered in narrative. Their insights covered concerns about credit, military consumers and the impact credit has on their lives. Approximately 49 respondents commented on creditors misleading military borrowers and offering them more credit than they can productively repay. Twenty-six respondents discussed the lack of understanding on the part of military consumers, and 11 added that more education is needed.

10. Please provide any additional comment that may help clarify any of your choices above or provide your observations on client experiences with credit that have not been asked in the above questions.

One hundred and twenty-seven respondents answered in narrative. Narratives varied, reiterating the role creditors play in exacerbating debt, amplifying the need for education, and elaborating on problems associated with client spending behavior.

APPENDIX B: DEFENSE MANPOWER DATA CENTER (DMDC) QUICKCOMPASS OF FINANCIAL ISSUES



Human Resources Strategic Assessment Program (HRSAP)
Information and Technology for Better Decision Making

- You have reached the redirect page for Department of Defense Human Resources Strategic Assessment Program (HRSAP) surveys. You will be redirected to our contractor's web site (a secure .com site run by Data Recognition Corporation) to participate in the survey.
- DMDC has set up a telephone line for anyone who wishes to verify the survey's legitimacy. Call DSN 372-1034 from any DoD or other government telephone with DSN for a list of current DMDC surveys. If you do not have access to a DSN telephone line, call 1-571-372-1034. The prerecorded list does not include surveys conducted by agencies other than DMDC.
- Please enter your Ticket Number below, then click the Continue button to access your survey.

- If you are not automatically transferred, click on the link below:
<http://www.dodsurvey.net/>



2013 QuickCompass of Financial Issues

Welcome

[Security Protection Advisory](#) [RCS# DD-P&R\(AR\)2145](#)
[Exp. 04/30/2014](#)

You have been selected to take a survey about the financial well being of active duty members. When you click the *Continue* button below, you will be asked to:

- Read the Privacy Act Statement
- Review your contact information
- Provide your e-mail address(es) so we can communicate

Thank you for your time and participation.

Section 508 Compliance
The U.S. Department of Defense is committed to making electronic and information technologies accessible to individuals with disabilities in accordance with [Section 508 of the Rehabilitation Act \(29 U.S.C. §794d\), as amended in 1999](#). Send feedback or concerns related to the accessibility of this Web site to: DoDSection508@osd.mil. For more information about Section 508, please visit the [DoD Section 508 Web site](#). Last Updated: 08/13/2013

PRIVACY ACT STATEMENT & INFORMED CONSENT INFORMATION

In accordance with the Privacy Act, this notice informs you of the purpose of the survey and how the findings of these surveys will be used. It also provides information about the Privacy Act and informed consent. Please read it carefully.

AUTHORITY: United States Code Sections 10 USC 1782 and 10 USC 136.

PRINCIPAL PURPOSE: Information collected in this survey will be used to research personal financial issues of active duty personnel. This information may be used to assist in the formulation of policies and programs for Service members. Findings will be used in reports provided to Congress. Some findings may be published by the Defense Manpower Data Center (DMDC) or in professional journals, or presented at conferences, symposia, and scientific meetings. Data could be used in future research. Datasets without any identifying information may be analyzed by researchers outside of DMDC. Briefings and reports on results from these surveys will be posted on the Web: <http://www.dmdc.osd.mil/surveys/>

ROUTINE USES: None.

DISCLOSURE: Providing information on this survey is voluntary. Most people can complete the survey in 20 minutes. There is no penalty or loss of benefits to which you are entitled if you choose not to respond. However, maximum participation is encouraged so that the data will be complete and representative. Your survey responses will be treated as confidential. Identifying information will be used only by government and contractor staff engaged in, and for purposes of, survey research. For example, the research oversight office of the Office of the Under Secretary of Defense (Personnel and Readiness) and representatives of the U.S. Army Medical Research and Materiel Command are eligible to review research records as a part of their responsibility to protect human subjects in research. This survey is being conducted for research purposes. In no case will individual identifiable survey responses be reported. If you answer any items and indicate distress or being upset, etc., you will not be contacted for follow-up purposes. However, if you indicate a direct threat to harm yourself or others within responses or communications about the survey, because of concern for your welfare, DMDC may notify an office in your area for appropriate action.

SURVEY ELIGIBILITY AND POTENTIAL BENEFITS: DMDC uses well-established, scientific procedures to randomly select a sample that represents the Defense community based on combinations of demographic characteristics (for example, paygrade, gender, etc.). This is your chance to be heard on issues that directly affect you. While there is no direct benefit for your individual participation, your responses on this survey **make a difference**.

STATEMENT OF RISK: The data collection procedures are not expected to involve any risk or discomfort to you. The only risk to you is accidental or unintentional disclosure of the data you provide. However, the government and its contractors have a number of policies and procedures to ensure that survey data are safe and protected. For example, no identifying information (name, address, Social Security Number) is ever stored in the same file as survey responses. Survey data may be shared with organizations doing research on DoD personnel but only after minimizing detailed demographic data (for example, paygrade and detailed location information) that could possibly be used to identify an individual. A confidentiality analysis is performed to reduce the risk of there being a combination of demographic variables that can single out an individual. Government and contractor staff members have been trained to protect client identity and are subject to civil penalties for violating your confidentiality.

If you experience any difficulties taking the survey, please contact the Survey Processing Center by sending an e-mail to DMDC.QCSurvey@mail.mil or call, toll-free, 1-800-881-5307. If you have concerns about your rights as a research participant, please contact: OUSD(P&R) Regulatory Oversight Office, R2o2@tma.osd.mil, 703-575-2677 or 703-575-3536.

Once you start answering the survey, if you desire to withdraw your answers, please notify the Survey Processing Center prior to October 22, 2013. Please include in the e-mail or phone message your name, Ticket Number, and the PIN that you selected when you started this survey. Unless withdrawn, partially completed survey data may be used after that date.

Click *Continue* if you agree to do the survey.

BACKGROUND INFORMATION

1. Were you on active duty on September 5, 2013?

- Yes
 No, I separated or retired on or before September 5, 2013

2. What is your current paygrade? *Mark one.*

- E-1 E-6 W-1 O-1/O-1E
 E-2 E-7 W-2 O-2/O-2E
 E-3 E-8 W-3 O-3/O-3E
 E-4 E-9 W-4 O-4
 E-5 W-5 O-5
 O-6 or above

3. Do you live with someone with whom you share finances to include using credit? *Mark "Yes" if this is the case, even if you are temporarily living apart (e.g., due to deployment, temporary duty, or permanent change of station).*

- Yes
 No

4. What is your marital status?

- Married
 Separated
 Divorced
 Widowed
 Never married

5. Which of the following best describes your current living arrangements? *Mark one.*

- I am the only adult in the household.
 I live with my spouse/partner/significant other.
 I live with my spouse/partner/significant other and one or more other adults.
 I live with other adult family, friends, or roommates.

For this question, the definition of "child, children, or other legal dependents" includes anyone in your family, except your spouse, who has, or is eligible to have, a Uniformed Services Identification and Privilege card (also called a military ID card) or is eligible for military health care benefits, and is enrolled in the Defense Enrollment Eligibility Reporting System (DEERS).

6. Do you have a child, children, or other legal dependents based on the definition above?

- Yes
 No

7. What is the highest degree or level of school that you have completed? *Mark the one answer that describes the highest grade or degree that you have completed.*

- 12 years or less of school (no diploma)
 High school graduate—traditional diploma
 High school graduate—alternative diploma (home school, GED, etc.)
 Some college credit, but less than 1 year
 1 or more years of college, no degree
 Associate's degree (e.g., AA, AS)
 Bachelor's degree (e.g., BA, AB, BS)
 Master's, doctoral, or professional school degree (e.g., MA, MS, MEd, MEng, MBA, MSW, PhD, MD, JD, DVM, EdD)

8. Are you Spanish/Hispanic/Latino?

- No, not Spanish/Hispanic/Latino
 Yes, Mexican, Mexican-American, Chicano, Puerto Rican, Cuban, or other Spanish/Hispanic/Latino

9. What is your race? *Mark one or more races to indicate what race you consider yourself to be.*

- White
 Black or African American
 American Indian or Alaska Native
 Asian (e.g., Asian Indian, Chinese, Filipino, Japanese, Korean, Vietnamese)
 Native Hawaiian or other Pacific Islander (e.g., Samoan, Guamanian or Chamorro)

10. Where is your permanent duty station (homeport) located?

- In one of the 50 states, D.C., Puerto Rico, or a U.S. territory or possession
 Overseas

11. In the past 24 months, have you been deployed longer than 30 consecutive days?

- Yes
 No

GENERAL OPINIONS ON CREDIT

12. How much do you agree or disagree with the following statements? *Mark one answer for each item.*

	Strongly disagree	Disagree	Neither agree nor disagree	Agree	Strongly agree
a. Most people benefit from the use of credit.....	<input checked="" type="checkbox"/>				
b. Overspending is the fault of consumers, not lenders.....	<input checked="" type="checkbox"/>				
c. There is too much credit available today.....	<input checked="" type="checkbox"/>				
d. In the last 5 years I have seen other military members get in trouble using credit.....	<input checked="" type="checkbox"/>				
e. Use of credit is a problem for a lot of military members.....	<input checked="" type="checkbox"/>				

FINANCIAL HEALTH

13. Which of the following best describes [your financial condition] [the financial condition of you and your spouse] [the financial condition of you and your partner or significant other]?

- Very comfortable and secure
- Able to make ends meet without much difficulty
- Occasionally have some difficulty making ends meet
- Tough to make ends meet but keeping your head above water
- In over your head

14. Compared to 12 months ago, is [your financial situation] [the financial situation of you and your spouse] [the financial situation of you and your partner or significant other] better, worse, or has it stayed the same?

- Much better
- Somewhat better
- Stayed the same
- Somewhat worse
- Much worse

15. Which of the following best describes [your saving habits] [the saving habits of you and your spouse] [the saving habits of you and your partner or significant other]? [I] [We]:

- Spend all the income received and don't save.
- Save whatever is left at the end of the month.
- Regularly set aside money in savings.
- Don't know.

16. How much do [you] [you and your spouse] [you and your partner or significant other] have in an emergency savings fund?

- Don't have an emergency savings fund
- Less than \$100
- Between \$100 and \$499
- Between \$500 and \$999
- \$1,000 or more

17. Assume you were having some financial trouble and you asked for assistance from a military aid society. How likely is it that each of the following would happen? *Mark one answer for each item.*

	Very unlikely	Unlikely	Neither likely nor unlikely	Likely	Very likely
a. The military aid society would be able to loan you the money you needed.....	<input checked="" type="checkbox"/>				
b. The loan would allow you to get your finances to a good place.....	<input checked="" type="checkbox"/>				
c. The military aid society would tell your commander.....	<input checked="" type="checkbox"/>				
d. Your commander would find out some other way.....	<input checked="" type="checkbox"/>				
e. You would be embarrassed.....	<input checked="" type="checkbox"/>				
f. You would lose your security clearance.....	<input checked="" type="checkbox"/>				
g. You would be forced to return from deployment/no longer be deployable.....	<input checked="" type="checkbox"/>				
h. You would receive a non-judicial punishment.....	<input checked="" type="checkbox"/>				
i. It would hurt your ability to get promoted.....	<input checked="" type="checkbox"/>				

18. In the past 5 years, has any lender or creditor turned down any request [you] [you and/or your spouse] [you and/or your partner or significant other] made for credit, or given you less credit than you applied for?

- Yes
 No
 Don't know

19. [Ask if Q18 = "Yes"] Which of these places turned down the request or gave you less credit than you applied for? *Mark all that apply.*

- Bank, savings and loan, or credit union
 Finance company
 Store
 Payday lender
 Other

[Ask if Q19 = "Other"] Please specify the type of place that turned down the request for credit or gave you less credit than you applied for.

20. [Ask if Q18 = "Yes"] Were you later able to obtain the full amount by reapplying to the same place or by applying elsewhere?

- Did not reapply
 Yes
 No

21. Was there any time in the past 5 years that [you] [you and/or your spouse] [you and/or your partner or significant other] thought of applying for credit at a particular place, but changed your mind because you thought you might be turned down?

- Yes
 No
 Don't know

22. [Ask if Q21 = "Yes"] At which of these places did [you] [you and/or your spouse] [you and/or your partner or significant other] change your mind and not apply for credit because you thought you might be turned down? *Mark all that apply.*

- Bank, savings and loan, or credit union
 Finance company
 Store
 Payday lender
 Other

[Ask if Q21 = "Yes" AND Q22 = "Other"] Please specify the type of place that [you] [you and/or your spouse] [you and/or your partner or significant other] did not apply for credit because you thought you might be turned down.

23. Have you checked either your credit score or your credit report in the past 12 months?

- Yes
 No
 Don't know

24. What is your current credit score?

- Above 720
 Between 681 and 720
 Between 641 and 680
 Between 581 and 640
 Between 531 and 580
 Between 501 and 530
 500 or below
 Don't know

25. How would you rate your credit history?

- Very good
 Good
 Neither good nor bad
 Bad
 Very bad
 I have no credit history
 Don't know

26. [Ask if (Q4 = "Married" OR (Q4 <> "Married" AND Q5 = "I live with my spouse/partner/significant other." OR Q5 = "I live with my spouse/partner/significant other and one or more other adults."))] **What is your [spouse's] [partner's or significant other's] current credit score?**

- Above 720
- Between 681 and 720
- Between 641 and 680
- Between 581 and 640
- Between 531 and 580
- Between 501 and 530
- 500 or below
- Don't know

27. [Ask if (Q4 = "Married" OR (Q4 <> "Married" AND Q5 = "I live with my spouse/partner/significant other." OR Q5 = "I live with my spouse/partner/significant other and one or more other adults."))] **How would you rate the credit history of your [spouse] [partner or significant other]?**

- Very good
- Good
- Neither good nor bad
- Bad
- Very bad
- No credit history
- Don't know

28. **During the past 12 months, did any of the following happen to [you] [you and your spouse] [you and your partner or significant other] ? [I was] [We were]... Mark "Yes" or "No" for each item.**

	Yes	No
a. More than 60 days late in paying mortgage or other debts.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
b. Unable to use bank credit card(s) because the credit limit was reached.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
c. Short on cash between paychecks.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
d. Unable to pay monthly bills.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>

29. [Ask if Q28 a = "Yes" OR Q28 b = "Yes" OR Q28 c = "Yes" OR Q28 d = "Yes"] **In how many of the past 12 months were [you] [you and your spouse] [you and your partner or significant other] short on cash, unable to use a credit card because the credit limit was reached, or unable to pay bills or other debts?**

- 1 month
- 2 to 4 months
- 5 to 7 months
- 8 or more months

CREDIT PRODUCTS

30. **Have [you] [you and/or your spouse] [you and/or your partner or significant other] used any of the following financial products or services to cover expenses in the past 12 months? Mark "Yes" or "No" for each item.**

	Yes	No
a. Overdraft loan.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
b. Overdraft line of credit.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
c. Overdraft protection from savings, credit card, or another account.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
d. Bank direct deposit advance loan.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
e. Payday loan.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
f. Vehicle title loan.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
g. Cash advance on a credit card.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
h. Pawn shop.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
i. Loan from Army Emergency Relief, Navy-Marine Corps Relief Society or Air Force Aid Society.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
j. Loan/borrow from friends or family.....	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>

31. [Ask if Q30 a = "Yes" OR Q30 b = "Yes" OR Q30 c = "Yes" OR Q30 d = "Yes" OR Q30 e = "Yes" OR Q30 f = "Yes" OR Q30 g = "Yes" OR Q30 h = "Yes" OR Q30 i = "Yes" OR Q30 j = "Yes"] **Why did [you] [you and/or your spouse] [you and/or your partner or significant other] use one or more of these financial products or services in the past 12 months? Mark all that apply.**

- Needed to cover regular monthly expenses
- Needed to cover one or more unexpected essential expenses
- Needed to cover one or more unexpected unessential expenses

BANK DIRECT DEPOSIT ADVANCE LOANS

You indicated in a previous question that in the last 12 months [you] [you and/or your spouse] [you and/or your partner or significant other] took a bank direct deposit advance loan to cover expenses. The next set of questions asks for more information about direct deposit advance loans taken. [For this set of questions, where you see the word "you" or "your", answer for you and/or your spouse / partner or significant other.]

32. [Ask if Q30 d = "Yes"] For what purpose(s) have you taken a bank direct deposit advance loan? *Mark all that apply.*

- PCS moving expenses
- Monthly bills were more than income
- Help a family member or friend
- Cover expenses for unsold former home
- Spouse/partner/significant other unemployed after PCS move
- Unexpected car or home repair
- Other

[Ask if Q30 d = "Yes" AND Q32 = "Other"]
Please specify the purpose(s) for taking a bank direct deposit advance loan.

33. [Ask if Q30 d = "Yes"] What was the most important reason for choosing a bank direct deposit advance loan rather than another source? *Mark one.*

- Convenient location
- Greater privacy
- Less paperwork
- Faster approval
- More respectful employees
- Quick and easy process
- Less harm to my credit
- Less expensive than other sources for borrowing cash
- No other alternative source for borrowing cash
- Other

[Ask if Q30 d = "Yes" AND Q33 = "Other"]
Please specify the most important reason for choosing a bank direct deposit advance loan rather than another source.

34. [Ask if Q30 d = "Yes"] In how many of the past 12 months did [you] [you and/or your spouse] [you and/or your partner or significant other] have bank direct deposit advance loans?

- 1-3 months
- 4-6 months
- 7-9 months
- 10-12 months

35. [Ask if Q30 d = "Yes"] What amount did you borrow against your paycheck for your most recent bank direct deposit advance loan? *If you borrowed several amounts in the days before your most recent paycheck, add those together.*

- Less than \$100
- Between \$100 and \$199
- Between \$200 and \$299
- Between \$300 and \$399
- Between \$400 and \$499
- \$500 or more
- Don't know

36. [Ask if Q30 d = "Yes" AND (Q34 = "4-6 months" OR Q34 = "7-9 months" OR Q34 = "10-12 months")] Were you contacted by the bank to help you find an alternative source of credit to meet your needs?

- Yes
- No
- Don't know

PAYDAY LOANS

You indicated in a previous question that in the last 12 months [you] [you and/or your spouse] [you and/or your partner or significant other] took a payday loan to cover expenses. The next set of questions asks for more information about payday loans taken. [For this set of questions, where you see the word "you" or "your", answer for you and/or your spouse / partner or significant other.]

37. [Ask if Q30 e = "Yes"] For what purpose(s) have you taken a payday loan? Mark all that apply.

- PCS moving expenses
- Monthly bills were more than income
- Help a family member or friend
- Cover expenses for unsold former home
- Spouse/partner/significant other unemployed after PCS move
- Unexpected car or home repair
- Other

[Ask if Q30 e = "Yes" AND Q37 = "Other"] Please specify the purpose(s) for taking a payday loan.

38. [Ask if Q30 e = "Yes"] Where did you obtain your payday loan(s)? Mark all that apply.

- From a store
- From the Internet
- Don't know

39. [Ask if Q30 e = "Yes"] What was the most important reason for choosing a payday loan rather than another source? Mark one.

- Convenient location
- Greater privacy
- Less paperwork
- Faster approval
- More respectful employees
- Quick and easy process
- Less harm to my credit
- Less expensive than other sources for borrowing cash
- No other alternative source for borrowing cash
- Other

[Ask if Q30 e = "Yes" AND Q39 = "Other"] Please specify the most important reason for choosing a payday loan rather than another source.

40. [Ask if Q30 e = "Yes"] How much time did you have to pay off your most recent payday loan in full? If you have a current loan, that is your most recent loan.

- 91 days or less
- More than 91 days
- Provided as revolving credit (no set date for full payment as long as payments are made on time)
- Don't know

[Ask if Q30 e = "Yes" AND Q40 = "Provided as revolving credit (no set date for full payment as long as payments are made on time)"] You indicated that your most recent payday loan was provided as revolving credit. How often were/are payments due? Payments were/are due:

 days

41. [Ask if Q30 e = "Yes"] Did the payday lender ask about active duty military status?

- Yes
- No
- Don't know

42. [Ask if Q30 e = "Yes"] What was the amount of your most recent new payday loan?

- Less than \$100
- Between \$100 and \$199
- Between \$200 and \$299
- Between \$300 and \$399
- Between \$400 and \$499
- \$500 or more
- Don't know

43. [Ask if Q30 e = "Yes"] Approximately how many payday loans did you take out in the last 12 months? *Include rollover loans as a separate loan in your calculations.*

- 1-2
 3-6
 7-10
 11-19
 20 or more

VEHICLE TITLE LOANS

You indicated in a previous question that in the last 12 months [you] [you and/or your spouse] [you and/or your partner or significant other] took a vehicle title loan to cover expenses. The next set of questions asks for more information about vehicle title loans taken. [For this set of questions, where you see the word "you" or "your", answer for you and/or your spouse / partner or significant other.]

44. [Ask if Q30 f = "Yes"] For what purpose(s) have you taken a vehicle title loan? *Mark all that apply.*

- PCS moving expenses
 Monthly bills were more than income
 Help a family member or friend
 Cover expenses for unsold former home
 Spouse/partner/significant other unemployed after PCS move
 Unexpected car or home repair
 Other

[Ask if Q30 f = "Yes" AND Q44 = "Other"]
 Please specify the purpose(s) for taking a vehicle title loan.

45. [Ask if Q30 f = "Yes"] Where did you obtain your vehicle title loan(s)? *Mark all that apply.*

- From a store
 From the Internet
 Don't know

46. [Ask if Q30 f = "Yes"] What was the amount of your most recent vehicle title loan?

- Less than \$500
 Between \$500 and \$999
 Between \$1,000 and \$1,999
 Between \$2,000 and \$3,999
 Between \$4,000 and \$5,999
 \$6,000 or more
 Don't know

47. [Ask if Q30 f = "Yes"] What was the APR (interest rate) on your most recent vehicle title loan?

- Less than 36%
 36-50%
 51% or more
 Don't know

48. [Ask if Q30 f = "Yes"] How much time did you have to pay off your most recent vehicle title loan in full? *If you have a current vehicle title loan, that is your most recent vehicle title loan.*

- 181 days or less
 More than 181 days
 Provided as revolving credit (no set date for full payment as long as made payments on time)
 Don't know

[Ask if Q30 f = "Yes" AND Q48 = "Provided as revolving credit (no set date for full payment as long as payments made on time)"] You indicated that your most recent vehicle title loan was provided as revolving credit. How often were/are payments due? Payments were/are due:

 days

49. [Ask if Q30 f = "Yes"] Did the vehicle title loan lender ask about active duty military status?

- Yes
 No
 Don't know