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Pentagon rules will leave military families unprotected

Put muscle in predatory lending regulations, consumer groups urge

Washington, D.C. - June 12, 2007 - Consumer advocates strongly urged the Department of Defense Monday to make significant changes to proposed federal regulations to ensure that predatory lenders can no longer strip earnings from U.S. soldiers and their families. As written, the regulations will leave loopholes large enough for payday, auto title and other predatory lenders to glide through, letting them gouge military borrowers without regard for a pending 36 percent interest rate cap, said the groups in a written response to the Pentagon's request for public comments.

Congress passed the 36 percent cap on consumer loans to military borrowers last fall after the Pentagon documented the devastating impact predatory lending is having on troop morale and combat readiness. The law exempts only residential mortgages and loans to purchase personal property. Congress charged the Department of Defense with writing rules that would implement the cap and other financial protections for military borrowers included in the Military Lending Act, also known as the Talent/Nelson Amendment. But the consumer groups say the proposed rules leave many predatory products untouched.

"The Pentagon has worked hard to get protections in place before the date the law takes effect, and we appreciate their commitment. But these rules end up giving predatory lenders leave to raid the personal funds of the troops," said Jean Ann Fox, director of consumer protection for the Consumer Federation of America (CFA). "This industry knows how to get around even the tightest of regulations. They will have no problem with the narrow definitions in the Pentagon's proposed rules."

In a statement introducing the proposed rules, the Pentagon acknowledged that payday loans and similar products have two problems: exorbitant interest rates of 400 percent and higher, and a built-in structure that compels borrowers to renew an expensive short-term loan many times because they cannot afford to pay it off. The typical payday borrower pays back nearly $800 for a $325 loan.

Banks and other financial institutions argued strongly for an exemption for their products. The Pentagon's rules limit the law to payday, auto title and refund anticipation loans, and defined those so narrowly that many similarly structured high-cost products already on the market will not be subject to the 36 percent cap. For example, the proposed rules would not stop any predatory car title lending in Virginia, and would not stop payday-like products by banks.

The proposed rules would not apply at all to military installment lenders who refinance loans at high fees with little benefit to the borrower. In the Pentagon's own predatory lending report to Congress last year, they raised specific concerns about military installment lenders' high interest rates and unfair terms.

In public comments on the proposed rules, CFA, the Center for Responsible Lending, the National Consumer Law Center, Consumers Union, and the National Association of Consumer Advocates called on the Pentagon to rewrite the rules to make the 36 percent cap meaningful by the October 1 implementation date if possible, and if not by that date, to take advantage of the extension Congress provided for in the Military Lending Act. Congress gave the Pentagon nine months after the October 1 implementation to refine the rules.

"As it is, big payday companies can target military borrowers with bad loans, like the one Advance America uses in Pennsylvania – a $500 revolving loan with a fee of $149.50 every month—*in addition* to the interest they say the loan carries," said Kathleen Keest, senior policy counsel for the Center for Responsible Lending. "This is one example among many that we have documented—what turns out to be a 370 percent interest loan that would not be subject to the Military Lending Act."

The 36 percent cap enacted by Congress will stop predatory lending if the Pentagon plugs loopholes that predatory lenders have used to get around similar state laws. The consumer groups lay out a solution in their comments that will exempt certain loans that can benefit borrowers, but only when the interest rate is reasonable.

"The only safe loophole is a low-cost loophole. We just can't allow predatory lenders to ignore these borrower protections, especially the interest rate cap," said Lauren Saunders, managing attorney with the National Consumer Law Center. "A 36 percent cap not only stops price gouging on the order of loan sharks, it stops loan flipping too. Predatory lenders just don't find it worth their while to target military families at 36 percent, though legitimate businesses have no problem operating under that limit."

The groups pledged to work closely with the Pentagon and other stakeholders in crafting revised regulations that will carry out Congress' intention.

"We're offering the Department of Defense a way to do this that will carry out the intent of the law and will not leave military borrowers exposed to many of the worst practices in the industry," said Saunders. "We want the same thing the Pentagon wants, and there is plenty of common ground with the banking industry too. We will continue to offer our experience in crafting laws that offer real protections until those protections are firmly in place."

To read the consumer groups' comments in their entirety, click here.

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Contacts:

Consumer Federation of America, Jean Ann Fox or Travis Plunkett, 202-387-6121
Center for Responsible Lending, Kathleen Keest or Carol Hammerstein, 919-313-8518
National Consumer Law Center, Lauren Saunders, 202-452-6252