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January 23, 2007

The Honorable Dr. David S.C. Chu
Under Secretary of Defense
for Personnel and Readiness
2000 Defense
Pentagon
Washington, D.C. 20301-4000

Dear Secretary Chu:

The American Bankers Association (ABA) submits this letter pursuant to the Federal Register notice published by the Department of Defense (DOD) on December 5, 2006.¹ We would note that this letter is in addition to the views that we expressed in our letter filed by the ABA and four other bank trade associations on January 5, 2007. We appreciate very much the opportunity to present to DOD our additional views as we work towards the shared objective of combating abusive payday lending products offered to service men and women, while ensuring that the protections included in section 670 of the John Warner National Defense Authorization Act for Fiscal Year 2007, Pub. L. 109-364 (the Payday Law) do not create unintended limitations on the ability of servicemembers and their families to obtain valuable, popular, and helpful credit products available to the general public.

We would like to present the following two points in this supplemental letter:

- DOD may wish to consider the use of payroll cards as an element in the overall solution to the problem of payday lending. While military personnel and their spouses and dependents should have every opportunity to use full-service checking accounts with direct deposit features, a payroll card may be a worthwhile, appropriate, and simpler alternative for those military customers who find it a better fit for their personal financial preferences and practices.
- Perhaps the most effective way to avoid the unintended consequences outlined in our January 5 letter is to exempt insured depository institutions that are subject to an effective regulatory program that prohibits abusive payday lending practices. An implementing regulation focusing on payday lenders and other lenders who operate outside the highly regulated and supervised environment could ensure that those avenues for abusive payday loans are closed off as well.

¹ 71 Fed. Reg. 70512 (Dec. 5, 2006).

These points are developed further, below.

I. Use of payroll cards. The Secretary may wish to investigate the role payroll cards could play in the effort to address payday lending. Today, payroll cards are an increasingly popular and convenient banking alternative for those who do not wish to use or have difficulty managing checking accounts. Under such programs, the only deposits permitted are direct deposit of wages, and account funds can only be accessed through the use of the card given to the employee (e.g., a Visa or MasterCard card). Thus, for example, the account holder cannot write checks or arrange for a direct debit. Accordingly, payday lenders would not have the ability to access payroll card funds through a post-dated check or direct debit avenue. In addition, these limitations essentially eliminate the risk of the account holder overdrawing the account.

There are a number of potential payroll card models. Under one typical model, the DOD could have a specific arrangement with a particular depository institution to open accounts and issue cards. Under an alternative model, servicemembers on their own initiative could open payroll card accounts offered by any of a variety of participating depository institutions. In the latter case, DOD would not be involved directly or indirectly, except as the source of the direct deposit. In both examples, the account could only be funded by direct deposit and accessed only through a debit card and use of a personal identification number.

We would emphasize that as a normal rule, military personnel and their spouses and dependents should be given full opportunity to use full-service checking accounts and direct deposits, as they offer the most flexible way to manage finances and payments. If given a choice between a full-service checking account and a payroll card, we believe the overwhelming majority of servicemembers would elect to use checking accounts. However, for those few who would prefer otherwise or who find managing a checking account challenging, a payroll card may be an appropriate alternative, providing convenience as well as security.

II. Definition of “creditor.” The Payday Law vests broad discretion in DOD to define creditor in a way that meets the purpose of the statute. The only parameter set in the statute is that a creditor be “a person who is engaged in the business of extending consumer credit and meets such additional criteria as are specified for such purpose in regulations prescribed under [the Payday Law].”²

We believe it is instructive to look at the DOD’s Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents, dated August 9, 2006, (the DOD Report) for guidance on how “creditor” should be defined. That report provided the impetus for the bill that became the Payday Law, and thus, in the absence of any legislative history of the Payday Law, could serve as an indication of Congress’ intent.

The DOD Report repeatedly focuses on the abuses by payday lenders and other types of lenders that are not subject to the extensive consumer protection laws and supervisory regime within which insured depository institutions operate. Of the case studies provided in the DOD Report of the impact of predatory loans on servicemembers, 13 of the 17 examples involved people who had become trapped by spiraling debt resulting from multiple payday loans.³ The remaining examples involved servicemembers who had run into trouble with car title loans, military installment loans,

² The Payday Law also applies to assignees of creditors.

³ DOD Report, at 39-42.

and loans to rent-to-own companies. None of the examples cited appear to have involved a bank or savings association.

In fact, by way of illustrative contrast, the DOD Report singled out several insured depository institutions for their efforts at meeting servicemembers' need for small-denomination, short-term loans at a reasonable cost. Banks also were featured at a recent symposium sponsored by the Federal Deposit Insurance Corporation (FDIC) on Affordable, Responsible Loans for the Military as sources of desirable, helpful credit. Our members are eager to work with the military to continue meeting the servicemembers' credit needs by offering products that servicemembers find helpful, and we are engaged in discussions with the FDIC on how to facilitate and promote further small-denomination, short term loan products.

However, the burdens and limitations imposed by the Payday Law that are designed to stamp out abusive practices could, if applied directly to insured depository institutions, make it difficult or impossible for insured depository institutions to offer many of the credit products that servicemembers need and that borrowers in the general public find valuable. We offered illustrative examples in our January 5 letter of the types of useful, desirable, and uncontroversial products that could become prohibited for military families.

Implicit in our January 5 letter is the point that we wish make explicit here: DOD will be in the best position to protect servicemembers and avoid unintended adverse consequences if it exempts insured depository institutions from the scope of its regulation implementing the Payday Law. Other approaches would be far more complicated to develop and to administer without limiting choices for military families, if they could be developed at all.

This approach recognizes the extensive consumer protections that already apply when a servicemember walks into an insured depository institution. Unlike payday lenders and the lenders engaging in the unscrupulous conduct cited in the DOD report, insured depository institutions are heavily regulated and closely examined. Depository institutions are examined for compliance with a myriad of consumer finance protection laws, including, for example—

1. Truth In Lending Act
2. Equal Credit Opportunity Act
3. Real Estate Settlement Procedures Act
4. Fair Housing Act
5. Home Mortgage Disclosure Act
6. Fair Credit Reporting Act
7. Truth in Savings Act
8. Consumer Leasing Act
9. Fair Debt Collection Practices Act
10. Federal Trade Commission Act prohibiting unfair and deceptive acts and practices
11. OCC anti-predatory lending regulations
12. Homeowners Equity Protection Act of 1994 (HOEPA)
13. Guidance on Nontraditional Mortgage Loans
14. Electronic Funds Transfer Act
15. Credit Practices Rule
16. Expedited Funds Availability Act
17. Fair Credit and Charge Card Disclosure Act
18. Fair Credit Billing Act

In addition to regulations, the agencies regulating depository institutions have issued official “guidance” and “guidelines” to the institutions they regulate, helping ensure that abusive lending practices are kept out of the banking system. A small sampling of this information includes the following:

- FDIC: Supervisory Policy on Predatory Lending, FIL-6-2007 (<http://www.fdic.gov/news/news/financial/2007/fil07006.html>)
- OCC: Advisory on Payday Lending: OCC AL 2000-10 (<http://www.occ.treas.gov/ftp/advisory/2000-10.doc>)
- OCC: Advisory on Predatory Lending: OCC AL 2003-2 (<http://www.occ.treas.gov/ftp/advisory/2003-2.pdf>)
- OTS: Memorandum for Chief Executive Officers on Payday Lending (<http://www.ots.treas.gov/docs/2/25132.pdf>)
- Joint Guidance on Overdraft Protection Programs. (<http://www.federalreserve.gov/boarddocs/srletters/2005/SR0503a1.pdf>)
- OTS: Memorandum for Chief Executive Officers on Title Loan Programs (<http://www.ots.treas.gov/docs/2/25131.pdf>)
- Joint release of the 4 banking agencies, FTC, DOJ, HUD, FHFB, OFHEO, and NCUA: Predatory lending brochure (<http://www.occ.treas.gov/ftp/release/2003-79.htm>)

Insured depository institutions are examined frequently. The largest banks and savings associations have “resident examiners” who literally report to work every day at those institutions and engage in ongoing examination of the institutions’ activities. Many other institutions are examined annually. The longest any bank or savings association goes without being examined is 18 months. The examiners have access to all records of a bank or savings association, including any complaints filed by customers or members of the public at large. Problems are detected early and dealt with quickly. This extensive system of regulation is a crucial distinction between insured depository institutions and payday lenders. In short, our point is that for insured depository institutions, there exists in place today a well-staffed and experienced program of supervision, with ample legal authority, that can be drawn upon to ensure that these institutions are prohibited from abusive lending practices. The chief contribution of the Payday Law can be in making sure that an adequate program is in place to stop these abusive practices by lenders outside of the regulatory environment of the insured depository firms and their affiliates.

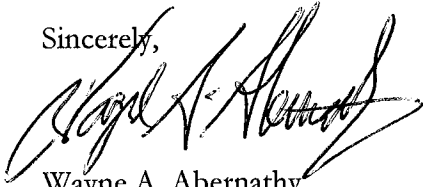
Moreover, insured depository institutions are not fly-by-night operations. They depend on their reputation and goodwill to preserve the trust of the public. Any bank or savings association that loses that trust would be severely disadvantaged in the marketplace. Thus, it is very much in the best interest of every insured depository institution not to engage in practices that will present a reputation risk and potentially erode the public’s trust.

For these reasons, the ABA respectfully requests that the DOD exempt insured depository institutions from the definition of “creditor” in its regulation implementing the Payday Law, relying upon the supervisory programs of their regulators to prohibit abuses. This would keep the focus of

the new legislation where it belongs—on payday lenders—and in so doing would address the problems Congress intended to address while avoiding the potential unintentional consequences that could hurt servicemembers and their families.

We appreciate very much the opportunity to share our views with you and would be happy to provide you any additional information you would find helpful.

Sincerely,

A handwritten signature in black ink, appearing to read "Wayne A. Abernathy". The signature is fluid and cursive, with a large initial "W" and "A".

Wayne A. Abernathy
Executive Director
Financial Institutions Policy
and Regulatory Affairs