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1160 Defense Pentagon
Washington DC 20301-1160

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Re: RIN 0790-A120
Limitations on Terms of Consumer Credit to Service Members and Dependents
72 *Federal Register* 18157, April 11, 2007

Dear Sir or Madam,

The undersigned trade associations representing insured depository institutions appreciate the opportunity to comment on the Department of Defense's ("The Department") proposal to implement the consumer protections in Public Law 109-364, the John Warner National Defense Authorization Act for Fiscal Year 2007,) section 670, "Limitations on Terms of Consumer Credit Extended to Service Members and Dependents" ("Payday Loan Law"). The proposed rule is intended to regulate the terms of certain consumer credit to service members and their spouses and dependents.

We applaud the Department's efforts to develop a rational and manageable regulation to implement the Payday Loan Law that balances the statute's goal of curtailing certain abusive practices associated with payday loans and the need to avoid unintended consequences that may harm service members and their spouses and dependents. By focusing the rule on the abusive practices that initially raised Congressional concerns and limiting application of the statute to certain loans, the Department has taken a significant step towards ensuring service members and their spouses and dependents – like other consumers -- continue to have access to beneficial and necessary financial products and services. It is critical that the final rule retain that careful focus so as not to deprive service members and their spouses and dependents of access to mainstream credit products nor to increase their credit costs.

Depository institutions already are subject to an extensive array of consumer protection laws and are examined frequently and, in some cases, continually. Moreover, they are not the source of the problems that gave rise to the Payday Loan Law. We believe, therefore, that the best way to ensure a proper balance and protect service members and their spouses and dependents is to rely on the existing system of bank supervision and regulation. We also believe that relying on the existing bank regulatory system will allow depository institutions to explore offering innovative, small-dollar, short-term credit products that the Department and policy makers have recognized as beneficial. For these reasons, we respectfully recommend that the Department focus its efforts on filling the gap in existing regulations by applying the protections of the Payday Loan Law to lenders outside the heavily regulated environment in which banks and savings associations operate.

Whether the Department focuses on types of products or on types of lenders, it is critical that the final rule retain a specific and focused application. Otherwise, service members and their spouses and dependents are likely to be denied access to mainstream credit products or be able to enjoy them only at increased costs. A focused application of the final rule will also avoid the unintended consequences that initially concerned the undersigned trade associations. While we believe the Department has thoughtfully interpreted many of the substantive provisions in a practical fashion, if the rule were applied more generally or to a broader array of loans, those provisions would present significant challenges and burdens that would discourage offering many financial products and services beneficial to service members and their spouses and dependents. The result could be harmful to service members and their spouses and dependents who would find their financial options limited.

These points, along with suggestions for certain technical changes, are discussed below.

Treatment of insured depository institutions.

The Department has invited comment on:

> [W]hether the final regulation should exclude regulated banks, credit unions and savings associations and their subsidiaries from coverage by the regulation generally, or in limited circumstances such as in the following circumstances: (1) the depository institutions are subject to supervision and regulation by a federal regulatory agency; (2) the institution extends covered "consumer credit"; (3) the extension of consumer credit by the institution is subject to supervisory guidance by the federal bank regulatory agency that addresses consumer protection, disclosure, and safety and soundness criteria applicable to such lending; and (4) the federal bank regulatory agency agrees to act on matters referred to it by the Department concerning complaints that such lending to a covered member may be inconsistent with the supervisory guidance, applicable law, or is having an adverse effect on military readiness.

It is helpful to approach this issue from two perspectives: first, whether it is reasonable for the Department to rely on the existing system of regulation and supervision for insured depository institutions and their subsidiaries, and second, what likely would happen if the Department did not rely on the bank regulatory system.

We encourage the Department to rely on the existing supervisory framework for depository institutions. The existing system ensures that banks operate safely and soundly and that consumers are protected. The first criterion set out in the Department's solicitation of comment on this issue is a simple, binary determination. Either an institution is subject to the primary jurisdiction of a federal banking agency[1] or it is not, and thus the first criterion proposed by the Department is satisfied.

Depending on how the Department defines "consumer credit" in the final rule, an institution either would be extending covered credit or it would not be. However, it is safe to assume that within the universe of federally regulated and supervised depository institutions there will be some that extend "consumer credit." Accordingly, the second criterion proposed by the Department is easily satisfied.

With respect to the third element, there can be no doubt that insured depository institutions and their subsidiaries are subject to an extensive body of consumer protection laws. 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 Section 5 (prohibiting unfair and deceptive acts and practices)
11. Homeowners Equity Protection Act of 1994 (HOEPA)
12. Electronic Funds Transfer Act
13. Credit Practices Rule
14. Expedited Funds Availability Act
15. Fair Credit and Charge Card Disclosure Act
16. Fair Credit Billing Act

In addition to regulations, depository institutions are subject to official "guidance" and "guidelines" issued by the agencies regulating depository

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[1] The Federal Deposit Insurance Act defines "Federal banking agency" as "the Comptroller of the Currency, the Director of the Office of Thrift Supervision, the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation." 12 U.S.C. 1813(z). A comparable bright line exists for credit unions and their regulator.

institutions 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)
- OCC: Gift Card Disclosures (http://www.occ.treas.gov/ftp/bulletin/2006-34.doc) – the OTS has issued parallel guidelines
- Interagency Guidelines on Nontraditional Mortgages, see, e.g., http://www.fdic.gov/news/news/financial/2006/fil06089.html

These are just a small sample of the rules and guidelines that apply when a federally supervised depository institution offers consumer credit.

Even when other lenders are subject to one of these consumer protection laws, they are rarely examined for compliance. In any case, unlike insured depository institutions, other lenders are certainly not subject to the regular audits and review that apply to depository institutions. The supervisory regime for non-depository lenders stands in sharp contrast to the current system of bank supervision, which has ample resources to detect, and respond to, problems arising in a regulated institution.

In fact, the largest depository institutions have “resident examiners” who conduct 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. In all cases, the examiners have access to all records of a depository institution, including any complaints filed by customers or members of the public at large. Problems are detected early and dealt with quickly.

The federal banking agencies take consumer complaints very seriously and include a review of consumer complaints as a regular part of the examination process. There is no reason to doubt that they would give a referral from the Department anything less than full and careful consideration. We can also point out that the federal banking agencies have ample resources, including a broad range of enforcement tools, at their disposal to ensure compliance with consumer protection laws. Very often problems are addressed informally during the course of an examination, but if a bank is found to have violated a law or otherwise engaged in an inappropriate practice and fails to correct the situation, the regulator may take an increasingly severe series of enforcement steps, beginning with informal agreements and extending to removal orders or civil money penalties. It is in no one's interest – not the customer's, not the bank's, and not the regulator's – to allow a problem to fester. Furthermore, federal banking agencies are usually able to take corrective action with little or no impairment of a bank's ability to offer other, valuable services to customers.

For these reasons, we believe the Department can and should rely on the supervisory programs of the federal banking agencies to address abuses. Failing to do so could lead to many of the unintended consequences noted in our prior comment letters that only serve to disadvantage servicemembers and their dependents.

For example, the Payday Loan Law carries with it draconian penalties, and loans violating the statute's provisions are void as of the day they are made. Lenders can go to jail. And the class action lawyers are always circling. Faced with the potential consequences of being found acting in conflict with the statute, some bankers will be overly cautious in determining which products are subject to the regulation. Others may conclude that the risks are simply too great to continue offering the products and services currently available to service members and their spouses and dependents. As a result, the cost of credit goes up or availability of credit goes down. Neither option helps service members; both are entirely avoidable. Recognizing that the purposes of the statute are met for depository institutions through their existing regulatory system is the most logical approach to avoid this problem.

Some have expressed concern about creating an unlevel playing field if the Department were to rely on the system of bank regulation and supervision. The irony of such a concern is that an unlevel playing already exists today; however, it favors the payday lenders. By focusing on payday lenders and other creditors who are outside the highly regulated and supervised environment in which banks operate, the Department would be filling a gap that exists *outside* of the world of bank regulation. And, it would focus resources on the abuses that the Department identified in its August 2006 report to Congress.

Thus, the undersigned trade associations respectfully submit that the best way to protect service members and their spouses and dependents while preserving access to beneficial and affordable credit products is for the Department to build on the existing system of banking regulation and keep its regulation focused on the lenders who operate outside the regulatory and supervisory system that protects bank customers.

If the Department moves forward and adopts the rule substantially as proposed, though, we recommend the following steps.

232.3 Definitions.

Consumer credit.

The proposal defines "consumer credit" for the purpose of the new law as "credit offered or extended to a covered borrower primarily for personal, family or household purposes" and then lists and defines specific types of loans: payday loans, vehicle title loans, and tax refund anticipation loans. Each of the specified types of loans is defined as "closed-end credit." To enhance the regulation's readability and minimize any ambiguity, we strongly recommend that the Department include the "closed-end credit" qualifier in the definition of "consumer credit" itself, rather than repeat it in each of subdefinition contained in the definition. We believe that including the qualifier "closed-end credit" in the general description of "consumer credit will make the regulation a clearer and more straightforward expression of the Department's intent.

Overall, we agree with the approach elected by the Department. The final regulation should apply only to closed-end credit. As discussed in greater detail in our joint 5 January 2007 comment letter, applying the statute to open-end credit such as credit cards may deprive service members and their spouses and dependents of many of these products. For example, under the proposed regulation, loans to service members and their spouses and dependents may not exceed a 36 military annual percentage rate ("MAPR"). The proposed MAPR includes not just interest, but also fees such as cash advance fees. An MAPR that includes cash advance fees, for example, or other fees for a small dollar advance, which are common with open-end loan programs like credit cards, could easily exceed the 36% limit. By focusing on the type of closed-end products that initially raised concerns, the Department's proposal avoids these problems.

Moreover, the ambiguity and subjectivity of other provisions in the proposed regulation raise significant potential liability possibilities if open-end credit were covered. The vagueness of the proposed provisions prohibiting “onerous legal notices” and “unreasonable notices from the covered borrower as a condition for legal action” coupled with the severe consequences for violations – including voidance of the loan and criminal sanctions – provide strong incentives to avoid any loan covered by the regulation. Other provisions such as the requirement to calculate an MAPR and provide oral disclosures are additional reasons lenders would avoid making any covered loan. As a result, if the final definition of consumer credit were to include open-end loans, their availability would be severely limited for service members and their spouses and dependents.

We also suggest that the Department revise the definition to make clear that “consumer credit” only covers credit subject to Regulation Z, the regulation which implements the Truth in Lending Act. As with the proposed regulation, Regulation Z only applies to credit offered or extended for personal, family or household purposes. However, to avoid confusion, ensure consistency, and avoid litigation, we recommend a specific reference to Regulation Z.

For the reasons discussed above, we recommend that the final regulation define “consumer credit” as, “closed-end credit that is covered by Regulation Z that is offered or extended to a covered borrower and that is described in paragraph (b)(1) of this section.“

***Payday loans*.** The first subset of loans covered in the proposed definition of consumer credit is payday loans, defined as closed-end credit with a term of 91 days or less in which the amount financed does not exceed $2,000 and the covered borrower:

1. Receives funds from and incurs interest and/or is charged a fee by a creditor, and contemporaneously provides a check or other payment instrument to the creditor who agrees with the covered borrower not to deposit or present the check or payment instrument for more than one day; or

2. Receives funds from and incurs interest and/or is charged a fee by a creditor, and contemporaneously authorizes the creditor to initiate a debit or debits to the covered borrower's deposit account (by electronic fund transfer or remotely created check) after one or more days. This provision does not apply to any right of a depository institution under statute or common law to offset indebtedness against funds on deposit in the event of the covered borrower's delinquency or default.

We agree with this focused definition. The target of the statute was predatory loans, particularly payday loans. Payday loans are typically short term, that is, one month or less, and usually under $1,000. Thus, we believe that the Department is capturing the intended target. Therefore, we concur with the Department’s approach.

We believe that the parameters set by the Department in the proposal are appropriate. Expanding the definition to include larger or longer-term loans could potentially bring in other loans such as student loans, personal unsecured loans, and work-out loans that should not be subject to the regulation's restrictions. Those loans, in effect, would become unavailable to service members and their spouses and dependents. For example, the restrictions against refinancing loans with the same creditors could deprive service members and their spouses and dependents of choices for refinancing for improved terms and conditions.

In addition, while the Department has attempted to make manageable the requirements and restrictions for covered credit, the requirements to calculate a separate and additional cost of credit term, the MAPR, and to provide oral disclosures, as well as the highly ambiguous prohibitions against "onerous legal notices" and "unreasonable notices from a borrower as a condition of legal action" will mean that depository institutions will have strong reasons to avoid making any covered credit available to service members and their spouses and dependents. Thus, if the regulation is expanded to cover other types of loans, service members and their spouses and dependents will have fewer loan products from which to choose.

We also agree that payday loans should be limited to instances where the borrower receives funds and contemporaneously provides a check or authorizes a debit to a deposit account. This condition captures a key trait of payday loans and will help avoid unintended inclusion of other loans that are not a target.

We suggest that the final rule make clear that the adverb ***"***contemporaneously" modifies "receives funds from." Otherwise, this provision could be interpreted to mean that the loan is only covered if the borrower receives funds and incurs interest/and or is charged a fee at the time the borrower receives funds; unscrupulous lenders could escape coverage by delaying charging interest or fees until after funds are disbursed.

Vehicle title loans. The next subset of loans covered by the proposed definition of consumer credit are "vehicle title loans" which are defined as "closed-end credit with a term of 181 days or less that is secured by the title to a motor vehicle owned by a covered borrower, other than a purchase money transaction." While we have questions (as discussed below) about how the regulation would impact title loans, we generally support this proposed definition, including the 181 days or less term qualification.

By limiting application to loans with terms less than 182 days, the regulation will not cover most popular conventional non-purchase car refinancing loans, which usually have terms more than 182 days. Covering all loans secured by vehicle titles would limit the choices of service members and their spouses and dependents. For example, such loans would then be subject to the restrictions against refinancing with the same creditor. While the Department permits such refinancings when the new loan results in "more favorable terms," as discussed later, lenders will tend to avoid such loans to escape the consequences of subjective interpretations of this phrase. The proposed definition will facilitate refinancing vehicle loans.

Some depository institutions tell us, however, that they currently make non-purchase loans with terms under 182 days secured by a vehicle such as a car or snowmobile. Such loans are sometimes made to customers with low credit scores who do not qualify for alternative sources of credit and need a small loan. The collateral makes the loan less risky – the borrower has greater incentive to repay, and the lender has collateral to help offset any default. In addition, some lenders make loans secured by a car simply because the car is a more manageable collateral than the item being purchased with the loan. For example, perfecting a loan secured by a car may be simpler than perfecting a loan secured by livestock. Similarly, in the event of a default on the loan, managing a car repossession and sale may be simpler than handling other types of collateral. If such loans are covered, depository institutions will have to adjust their lending practices and possibly eliminate some loans in order to comply, though we would note that the result may be a reduction in financial services beneficial to customers.

We do recommend, however, that the final regulation clarify that "motor vehicle" means only motorized vehicles which must be registered pursuant to state law. This will provide clarity and avoid inadvertent violations or confusion on what vehicles are covered.

Exclusions. The proposed regulation lists loans specifically not covered by the regulation. We suggest that the list of loans excluded from the definition of "consumer credit" be identified as illustrative. While it is appropriate to set forth a comprehensive list of covered transactions, it is impossible to do so for those not covered. To avoid any ambiguity over whether the list of loans not covered contains the entire universe of excluded transactions, and to ensure a certain level of flexibility in the final rule, we suggest that the introductory language in proposed 32 C.F.R. § 232.3(b)(2) read, "For purposes of this part, consumer credit does not include the following transactions, among others:" Since consumer finance can be a rapidly changing and evolving area, this approach will incorporate appropriate flexibility in the final rule.

Specifically excluded from coverage is "any other credit transaction that is not consumer credit extended by a creditor, is an exempt transaction, or is otherwise subject to disclosure requirements for purposes of Regulation Z." The undersigned associations strongly support the exclusion of loans not otherwise subject to the disclosure provisions of Regulation Z. The reference to Regulation Z provides consistency, enhances lenders' ability to understand and interpret the regulation, and minimizes subjectivity. Since Regulation Z disclosures apply to most consumer loans, this provision will also ensure uniformity. For additional clarity and simplicity, though, we suggest that the final regulation omit "is not consumer credit extended by a creditor, is an exempt transaction, or" so that it reads, "Any credit transaction that is not subject to disclosure requirements for purposes of Regulation Z." We believe that these changes will make the provision clearer and remove redundancies that could be misinterpreted.

Covered borrower.

Under the proposal, "covered borrower" includes a person who is a "regular or reserve member of the Army, Navy, Marine Corps, Air Force, or Coast Guard, serving on active duty under a call or order that does not specify a period of 30 days or less, or such a member serving on Active Guard and Reserve duty as that term is defined in 10 U.S. C. 101 (d)(6)." Also covered are the member's spouse, the member's child defined in 38 U.S.C. 101(4), or an individual for whom the member provided more than one-half of the individual's support for 180 days immediately preceding an extension of consumer credit covered by this part.

We agree with the proposed definition so long as all covered borrowers are entitled to an identification card or other documents showing their status as described in the definition and so long as their eligibility may be verified through a database. However, absent a reliable and practical means to determine and verify status, lenders are unfairly vulnerable to inadvertent and unavoidable violations of the regulation and subject to potential significant liability. Any definition of covered borrower should be built around the ability to demonstrate and verify eligibility.

Military annual percentage rate.

Under the proposal, the MAPR is the cost of a consumer credit transaction expressed as an annual rate. The MAPR includes the following cost elements associated with the extension of consumer credit to a covered borrower if they are financed, deducted from the proceeds of the consumer credit, or otherwise required to be paid as a condition of the credit:

1. Interest;
2. Fees;
3. Credit service charges;
4. Credit renewal charges;
5. Credit insurance premiums including charges for single premium credit insurance, fees for debt cancellation or debt suspension agreements; and
6. Fees for credit-related ancillary products sold in connection with and either at or before consummation of the credit transactions.

The MAPR does not include a fee imposed for actual unanticipated:

1. Late payments;
2. Default;
3. Delinquency; or
4. Similar occurrence.

The MAPR also does not include tax return preparation fees associated with a refund anticipation loan, whether or not the fees are deducted from the loan proceeds.

We appreciate the Department's flexibility in trying to design a workable military interest rate disclosure, but we reiterate our concerns about creating a competing term to describe the cost of credit. We strongly recommend using the annual percentage rate ("APR") definition from the Federal Reserve Board's Regulation Z since that is the standard used by lenders across the country and is a term with which most consumers are familiar.

Conceptually, we believe that an MAPR that is inconsistent with Regulation Z's APR will not help service members and their spouses and dependents to shop for and compare credit costs. The notion of the MAPR conflicts with several decades of development of a term consumers understand and are able to use to compare credit prices. We believe that creation of a conflicting cost-of-credit term undercuts efforts to provide a meaningful term with which to compare credit costs and will only serve to confuse service members and their spouses and dependents. Such confusion may cause them simply to ignore all interest rate disclosures. This problem is aggravated since servicemembers and their spouses and dependents will be forced to deal with a parallel but different term that will engender confusion and make it difficult to compare and contrast differing loan products or understand the terms of a loan.

The impact of the reduced efficacy of the APR will be magnified if the coverage of the regulation is broadened to include other loans beyond the closed-end products described in the proposed definition. Moreover, if the regulation is broadened to cover other loans, the MAPR calculation itself would inhibit lenders from offering service members and their spouses and dependents covered products because it would necessitate calculating, disclosing, and explaining a confusing term. In other words, since the MAPR and APR are not equivalent, the MAPR becomes a barrier to lending.

If the Department chooses to institute a new cost of credit term different from the APR, we suggest that it adopt and refer specifically to the APR in Regulation Z and then specify any fees excluded from the APR that it believes should be included in the MAPR, such as certain credit insurance premiums. Using the existing APR structure will help to avoid unintended consequences and ease compliance by providing predictability and clarity. And, fundamentally, the closer the MAPR is to the existing APR, the easier it will be for creditors and consumers to understand.

232.5 Identification of covered borrower.

The proposal would provide lenders a safe harbor against violations of the regulation for failure to recognize a covered borrower if the applicant signs a statement declaring whether he or she is a covered borrower. Having the covered borrower volunteer eligibility addresses many of the concerns raised in our 5 January 2007 letter and presents a rational and practical solution. Absent voluntary identification of eligibility, lenders would have to manually access the Department's database for each and every loan to determine eligibility, an unworkable solution for even a modest number of loans.

We believe it critical that the regulation require borrowers to advise lenders of their eligibility. However, we are concerned about the proposed "covered borrower identification statement" that references the borrower's marital status. Specifically, the proposed statement asks borrowers to verify whether they are:

> A dependent of a member of the Armed Forces on active duty because I am the member's spouse, the member's child under the age of eighteen years old, or I am an individual for whom the member provided more than one-half of my financial support 180 days immediately preceding today's date.

It could be very clear from this statement and by process of elimination, that an applicant is indeed the spouse. As discussed in our 5 January 2007 letter, inquiring about marital status raises the potential for violations of the Equal Credit Opportunity Act.[2] Specifically, the implementing regulation of that law, Regulation B[3] generally prohibits lenders from inquiring about the marital status of a person applying for individual, unsecured credit. Lenders that violate this regulation are subject to actual and punitive damages, in addition to regulatory sanctions.

Unless the Federal Reserve Board amends Regulation B or its Official Staff Commentary to indicate that such inquiries do not violate the regulation, lenders will be very reluctant to use this form and risk violating Regulation B. Given the narrow application of the proposal, the impact is minimal, but it will be relevant for certain loans offered by depository institutions such as tax refund anticipation loans. We encourage the Department to work with the Federal Reserve Board to resolve this issue.

[2] 15 U.S.C. 1601 et seq.
[3] 12 CFR 202.5(d)(1)

As noted earlier, we generally support the proposed safe harbor related to determining eligibility of loan applicants. However, we have concerns about the caveat to this "safe harbor" discussed in the preamble to the proposal, especially if the regulation were expanded to cover additional loans. The preamble explains:

> If the loan applicant signs a declaration that denies being a covered borrower, but the creditor obtains documentation as part of the credit transaction reflecting that the applicant is a covered borrower (such as, a current military leave and earning statement as proof of employment, or a tax filing that takes advantage of a specific tax provision designed to benefit the military), the applicant's declaration would not create a safe harbor for the creditor. In such cases creditors should seek to resolve the inconsistency, but if they are unable to do so, they may avoid any risk of noncompliance by treating the applicant as a covered borrower based on the documentation or by declining to extend credit due to the inability to verify information provided in the borrower's signed declaration.

We appreciate that the Department wishes to prevent “willful blindness” and agree with that goal. However, we are concerned that lenders might be held accountable for information available or provided, but not reviewed as a routine matter or in the normal course of business. For example, a lender may obtain documentation such as an earning statement but not review the name of the employer. For tax refund anticipation loans, lenders typically do not review the tax return, which is prepared by a professional tax preparer. Accordingly, if not alerted by the borrower, these lenders would probably not be aware of evidence of a borrower’s eligibility contained in the documentation absent a new procedure to review carefully all tax returns, adding new costs to providing these loans. Moreover, it is not clear what would trigger additional review. Would a military address, which is not typically reviewed or necessarily recognized as “military address,” be a red flag? Lenders would have to alter policies and processes and complicate and lengthen the loan approval process for the sake of a very small number of loans.

Fundamentally, we believe that the approach of the Servicemembers Civil Relief Act, which places responsibility on the servicemember to demonstrate eligibility, is the most workable approach. The goal is to develop a method for easily identifying and confirming eligibility without creating onerous burdens for creditors or relieving them from willful blindness. Therefore, we suggest that if the final regulation contains such a caveat to the safe harbor, it limit responsibility for further inquiry to those cases when eligibility is “readily apparent.” While such language is also subjective, it poses less risk.

As with other elements in the entire proposal, if coverage of the regulation remains limited as proposed, the caveat will be workable.

The proposal also permits lenders to verify the status of an applicant by requesting that the applicant provide a current (previous month) military leave and earning statement or a military identification card. In addition, lenders may request that activated members of the National Guard or Reserves also provide a copy of the military orders calling the covered member to military service and any orders further extending military service. We agree with this provision. It would be consistent with existing requirements under the Servicemembers Civil Relief Act and would be useful for confirming eligibility. This should be optional for creditors; it should not be mandatory.

Finally, the Department notes in the preamble that it believes that it would be unnecessarily burdensome to require creditors to make a new determination about eligibility in each transaction, given that it is unlikely the borrower's status will change in the course of short-term transactions. Accordingly, the proposed rule would not apply when the same creditor extends consumer credit to a covered borrower to refinance or renew an extension of credit that was not covered by Part 232 because the consumer was not a covered borrower at the time of the original transaction. We agree and urge the Department to retain this provision in the final rule.

232.6 Mandatory loan disclosures.

MAPR and Regulation Z disclosures. Under the proposal, lenders must provide to covered borrowers the MAPR and the total dollar amount of all charges included in the MAPR as well as the disclosures required under Regulation Z, which includes the APR. The Department specifically asks for suggestions on alternative approaches.

As discussed in our comments to the definition of MAPR above, we believe that disclosing the well-established APR along with a non-comparable MAPR will confuse rather than enlighten or help service members and their spouses and dependents. If the MAPR is defined differently from the APR, the Department should, at the very least, consider including a statement explaining the differences between the two terms. However, we believe that it will be challenging to design a statement that will adequately inform borrowers and be presented in a manner that borrowers are likely to notice and understand. For this reason, we strongly encourage the Department to develop an MAPR that is as close as possible to the Federal Reserve Board's APR, especially since the Federal Reserve Board has developed and refined the APR over nearly 40 years of experience.

Oral disclosures. Under the proposal, the MAPR, description of payment obligation, and statement about protections for service members must be provided orally. The Regulation Z disclosures are not required to be provided orally. In mail and internet transactions, lenders may provide a toll-free telephone number on or with the written disclosures that consumers may use to obtain oral disclosures and the creditor provides oral disclosures when the covered borrower contacts the creditor for this purpose.

We commend the Department for offering a practical, rational approach to the oral disclosure requirement. Trying to provide disclosures orally will be difficult in many instances, and without the approach taken by the Department in the proposal, will present a barrier for many transactions with service members and their spouses and dependents. We also agree that the Regulation Z disclosures should not be provided orally. As discussed in our 5 January 2007 letter, the Regulation Z disclosures simply are not designed to be provided orally and would provide little benefit to borrowers, if indeed borrowers would even have the patience or will to listen.

Though the Department has demonstrated flexibility with regard to the proposed oral disclosure requirements, challenges and burdens remain, relating to setting up, maintaining, and monitoring systems to provide the required disclosures for a small percentage of borrowers. Accordingly, the oral disclosures requirements would pose an impediment to providing any covered loan to service members and their spouses and dependents. So long as the regulation is applied narrowly as proposed, we believe that the impact will be minimal. Indeed, the oral disclosures requirement is another reason we applaud the focused approach taken by the Department in defining consumer credit.

232.8 Limitations

(1) Restrictions against refinancing with the same lender. Under this section, a lender may not extend consumer credit to a covered borrower if the lender is rolling over, renewing, repaying, refinancing, or consolidating consumer credit provided by the lender unless the new transaction "results in more favorable terms to the covered borrowers, such as a lower MAPR."

We commend the Department's effort to make more workable the statute's prohibition against a lender refinancing a loan originally made by that same lender. However, as discussed in our 5 January 2007 letter, depository institutions would still be reluctant to refinance such a loan except as specifically permitted by the regulation. Under the proposal, this would mean that they would only refinance if the MAPR of the new loan were lower.

There may be other terms that are arguably more favorable to the borrower. For example, in a work-out loan, smaller payments or extended payment terms that permit the borrower to continue to afford to pay the loan may be more favorable. Similarly, reducing multiple payments to a single payment, such as a student loan consolidation, may be more convenient and simpler for the borrower even if the APR is not lower. However, it is not clear under the proposal whether such loans would be deemed under the regulation as being "more favorable." Depository institutions are very likely to err on the side of caution and simply not offer those options to covered borrowers because the cost of being second-guessed is too great. To illustrate lenders' reluctance to interpret subjective regulations, under Regulation Z, borrowers may waive their right to rescission to "meet a bona fide personal financial emergency."[4] However, depository institutions report that they never permit a borrower to waive that right, not even the bank president, as one bank reported, because the consequences of later reinstituting the right of rescission are too great. The same absolute ban approach likely would apply in this case.

To the degree that the regulation is limited in scope to only certain loans, the impact of the restrictions of this provision is minimal to depository institutions. However, if the regulation were expanded to cover additional types of loans, depository institutions would avoid refinancing loans of their customers who are service members and spouses and dependents of service members. Perhaps the greatest negative impact would be the restricted ability for borrowers to work-out loans in arrears or default.

(2) Prohibition against waivers of the right to legal recourse. Under the proposal, it would be unlawful for the lender to require the borrower to waive the covered borrower's right to legal recourse under any otherwise applicable provision of state or federal law, including any provision of the Servicemembers Civil Relief Act.

We have no additional comments to this provision beyond what was already discussed in our 5 January 2007 letter. Our concern is that the provision could create the potentially impossible task of having to comply with the laws of all 50 states and the District of Columbia for every covered loan – even assuming the applicable state law could be identified. The regulation's proposed focused application will minimize this problem for consumers and depository institutions. However, if the regulation were applied more broadly, service members and their spouses and dependents could lose access to financial products offered by depository institutions as this provision would be another barrier to providing services.

(3) Prohibition against onerous legal notice provisions. Under the proposal, lenders may not impose onerous legal notice provisions on covered borrowers in the case of a dispute. The proposed regulation does not offer guidance on what would be "onerous legal notice." Without such guidance, the ambiguity and subjectivity of the provision impart strong motivation for depository institutions to avoid any loan potentially subject to the regulation. To the degree that the regulation remains narrowly applied, it raises fewer concerns. However, we encourage the Department to provide an exclusive list of what is considered "onerous legal notice."

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[4] 12 CFR 226.15(e)

(***4) Prohibition against unreasonable notice from the covered borrower as a condition for legal action***. Pursuant to the statute, the proposal prohibits lenders from imposing unreasonable notices from covered borrowers as a condition for legal action. This appears to overlap with the prohibition in paragraph (3), above. As with that prohibition, the subjectivity and ambiguity of the provision present significant arguments against offering any loan potentially covered by the regulation. To the degree that the regulation remains narrowly applied, it raises fewer concerns. However, as with the previous prohibition, we encourage the Department to provide an exclusive list of what is considered "unreasonable notice." Moreover, if this prohibition applies to notices that are different from the notices referred to in paragraph (3), we request that the Department make this clear.

(***5) Prohibition against lenders using a check or other method of access to a financial account or title to a vehicle as security for the obligation.*** Under the proposal, lenders may not use a check or other method of access to a deposit, savings, or other financial account maintained by the covered borrower or use the title of a vehicle as security for the obligation, except that, in connection with a consumer credit transaction with an MAPR consistent with 232.4(b), the creditor may:

1. Require an electronic fund transfer to repay a consumer credit transaction, unless otherwise prohibited by Regulation E;

2. Require direct deposit of the consumer's salary as a condition of eligibility for consumer credit unless otherwise prohibited by law; or

3. If not otherwise prohibited by applicable law, take a security interest in funds deposited after the extension of credit in an account established in connection with the consumer credit transaction.

We generally agree with these elements of the proposal, especially the step to link the statute's restrictions related to account access to Regulation E. The Department explains in the preamble that the exemptions are intended to "to facilitate creditors to make alternative loans designed to assist covered borrowers with financial recovery." We appreciate the Department's attempt to be flexible and sensitive to the ability of depository institutions to provide affordable loan products to service members and their spouses and dependents.

As the Department appreciates, direct debit can be a crucial component to alternative loans, including small dollar affordable loans. The automatic payment assists borrowers by helping to ensure that they make on-time payments. It also makes the loan more feasible for a lender to offer because there is less risk that the borrower will pay late or miss payments, and it can reduce transaction processing costs. Depository institutions offering alternative loans confirm the importance of the direct debit component. By continuing to allow direct debit of payments, consistent with Regulation E, the proposal will ensure that direct debit will remain an option for an alternative product. Moreover, any concern about the nexus to the automatic payment arrangements and payday loans is adequately addressed in the definition of payday loan.

The proposal limits the exception to consumer credit transactions "with an MAPR consistent with Section 232.4(b)." That section relates to the prohibition against charging an MAPR greater than 36 percent on covered loans. However, the meaning of or need for the qualification, "consistent with section 232.4(b)", is unclear. Under the proposal, the MAPR of any covered loan cannot exceed 36 percent. Accordingly, it is not clear how a covered loan would not qualify for the exception since, by regulation, it cannot charge an MAPR that exceeds 36 percent. To avoid confusion, we suggest that this phrase "with an MAPR consistent with 232.4(b)," be deleted.

We also suggest that the final regulation omit restating the prohibition against using the title of a vehicle as security for the obligation as this redundancy is confusing and unnecessary. The proposed regulation is providing that lenders may not "use the title of a vehicle as a security for the obligation" for a vehicle title loan, which is defined as a loan "secured by the title to a motor vehicle. . ." In effect, the proposal is prohibiting a feature which is a critical defining feature of one type of covered loan. If the loan does not use a title to the vehicle as security, as prohibited by the regulation, it is by definition, not a "vehicle title loan" and therefore not covered. Moreover, we do not believe that it is necessary to include the prohibition in this section. The regulation already covers vehicle title loans and applies all the restrictions of the regulation to those loans. In any case, the Department should be consistent in terminology when describing title loans. For example, the regulation should be clear that it is referring to "motor vehicles" not just "vehicles."

Under the proposal, notwithstanding the general prohibition against using access to an account as security, "The creditor may require direct deposit of the consumer's salary as a condition of eligibility for consumer credit, unless otherwise prohibited by law." It is unclear to us how direct deposit of salary amounts to a "method of access to a deposit. . . account . . . as security for the obligation." We suggest that the Department delete this confusing provision and make clear in the preamble that such arrangements continue to be permitted.

Direct deposit does not give a lender "access" to an account. The check, direct debit, or other payment instrument gives the lender access to the account. And the employer, not the lender, has access to the account to make the salary payment, but has no security interest in the funds. Thus, the reference to direct deposit of salary seems unrelated and incongruent with the general provision related to access to the account as security. Moreover, it is our understanding that service members are required to have direct deposit of their salary, so it will have no impact on service members. We believe that this provision will create confusion without adding any benefits to service members. Therefore, we suggest it be deleted and any question about direct deposit be addressed in the preamble.

The proposal will help to promote alternative loan products by allowing lenders to take a security interest in funds deposited after the extension of credit. An important component of many affordable small dollar, short term loan programs is a feature which automatically deposits a portion of the borrower's payment into a savings account. The savings feature helps borrowers to accumulate funds that are available for emergencies and unexpected expenses so that they are less likely to seek and use payday lenders. However, lenders are less likely to offer such a feature if they are unable to use these funds to repay the loan in event of a loan default. The proposal allows lenders to continue to offer this important option.[5]

Not included in this exception are deposits made prior to the loan. This means that service members and their spouses and dependents may not use their existing savings accounts as a security for a loan. We do not see this as having a significant impact at this time because of the narrow definition of covered credit. However, if the regulation were applied to a broader array of loans, service members and their spouses and dependents would face additional restrictions and higher credit costs if they are unable to use existing savings accounts, including certificates of deposits, as security for a loan.

232.11 Effective date and transition.

Under the proposal, the regulation only applies to credit extended and consummated on or after October 2007. We strongly agree that the regulation should only apply to covered loans made after the effective date of the regulation. Otherwise, loans made in good faith could automatically be considered illegal and voidable, a severe and unfair penalty for loans that were legal when made. Moreover, retroactive application is unworkable. Lenders would have to review all outstanding loans to determine whether they are subject to the regulation. They would then have to determine which of those were made to borrowers covered under the regulation, a daunting task given that it is expected that the system for verifying eligibility will be a manual one, as it is today. Even if it were feasible to identify existing loans and eligible borrowers, it is not clear what action should be taken. Must the loan be redesigned by the effective date? What if the lender cannot redesign the loan so that it is compliant? How would customer notice requirements be handled retroactively? For these reasons, we support the Department's approach.

[5] It is worth noting that the savings component was stressed by panelists at an FDIC forum in December 2006 on affordable small dollar loans. The FDIC Advisory Committee on Economic Inclusion also confirmed that a savings component is important to encourage financial responsibility.

The Department requests comment on the ability of creditors to comply with the proposed rules by 1 October 2007 if the final regulation is published on or before 1 September 2007. It will be difficult for banks and savings associations that provide short-term credit to evaluate their loan products and make any necessary revisions to their loan programs in order to be in compliance by 1 October. If the final regulation does not rely on the exiting bank regulatory scheme to enforce lending and consumer protection laws, it is critical that the Department keep the scope of the regulation narrow and that the final rule not be expanded to apply to a broader group of credit products. Applying the regulation to limited loan products will help depository institutions to comply with the final regulation in such a short period.

Conclusion.

The undersigned banking trade associations appreciate the Department's efforts in crafting a proposed regulation that helps address the abusive practices that caused Congress to adopt the Payday Loan Law. However, we continue to believe that the final rule should rely on the well-established banking regulatory system and that the final regulation should focus on those lenders that are not regulated by a federal banking agency.

Absent this approach, concentrating on closed-end short-term loans that raised concerns about their impact on military morale and readiness, will alleviate those concerns without creating a situation that is likely to make men and women in uniform—and their families—second-class citizens in the financial marketplace. We encourage the Department not to retreat from the focused approach in the draft rule, and we look forward to continuing to work with the Department and other interested parties to ensure that servicemembers and their dependents continue to have access to appropriate and beneficial financial products and services.

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American Bankers Association on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership--which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks--makes ABA the largest banking trade association in the country.

America's Community Bankers is a national trade association representing the nation's community banks of all charter types and sizes, including state and federally chartered savings institutions and commercial banks. ACB members pursue progressive, entrepreneurial and service-oriented strategies in providing financial services to benefit their customers and communities. Our members represent $1.7 trillion in assets across the nation and are both stock and mutually owned. To learn more about ACB, visit www.ACB.us.

Founded in 1959, the **Association of Military Banks of America** (AMBA) is a not for profit association of banks operating on military installations, banks not located on military installations but serving military customers, and military banking facilities designated by the U.S. Treasury. The association's membership includes both community banks and large multinational financial institutions, all of which are insured by the Federal Deposit Insurance Corporation.

The **Consumer Bankers Association** is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments and deposits. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation / regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

The **Independent Community Bankers of America** represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to representing the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than $908 billion in assets, $726 billion in deposits, and more than $619 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

The **Financial Services Roundtable** represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine accounting directly for $12.4 trillion in managed assets, $561 billion in revenue, and 1.8 million jobs.