

**State of New York, Office of Attorney General Eric T. Schneiderman  
Deanna R. Nelson, Assistant Attorney General In Charge (Watertown Regional)  
Before the United States Senate  
Commerce, Science & Transportation Committee  
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General Schneiderman's Watertown Regional Office sits outside the gates of the 10<sup>th</sup> Mountain Division, Fort Drum, New York. Fort Drum is one of the most deployed Army bases in the country. It is a light infantry division, home to approximately 20,000-active duty soldiers.

A large proportion of the regional work involves assisting soldiers who have fallen victim to predatory lenders and other shady business practices. These same soldiers are also frequently the target of abusive collection tactics. Many times the soldiers' financial indignities have accrued over time from both online financial predators and unscrupulous businesses that target soldiers on posts across the country. These debts follow military families with each change in duty station, and often subject soldiers to sky-high interest accumulation upon return from deployment.

We are very sensitive to the fact that soldiers are different and more vulnerable than most other consumer groups:

- Soldiers' rate of pay is ascertainable by the marks on their uniform;
- Soldiers receive regular paychecks which can be tapped directly by allotment;
- There is no administrative recourse for a soldier once an allotment has been paid out;
- Soldiers are routinely requested to provide access to their commanders for collection efforts;
- If a soldier stops an allotment or challenges a contract, they are opening themselves to the possibility of disciplinary action, loss of rank or security clearance from their employers;
- Soldiers are moving frequently which makes it difficult to commence legal action or defend legal action on questionable or fraudulent "debts."
- Very often the fraud is not obvious on the face of the transaction, and neither the soldier nor command is in a ready position to raise an effective defense.

Basically, we are dealing with a very honorable class of victims who are not likely to cry foul once victimized.

The identified thread in the predatory lending market is a prevalence of unlicensed lenders or high-cost "military specialty" lenders. These businesses regularly have undisclosed or hidden costs, deceptively characterized loan/credit products, include subtle waivers of Fair Debt Collection Practices Act protections (e.g., immediate access to chain of command), and engage in extremely aggressive collection/default activities.

These characteristics cross many markets targeting soldiers—electronics, furniture, jewelry, auto detailing/audio/upgrades, auto dealerships, “emergency” loans, leases, rent-to-own and other consumer products.

For purposes of this Committee’s work, the focus of this submission will be anecdotal information regarding the anatomy of predatory behavior in these transactions—baiting, snagging and collecting.

All of the predatory businesses take time to identify their market and single them out. Typically they are draped in the American flag, many times they employ former service members to heighten the trust of active duty soldiers, often times they hold themselves out as “specializing” in serving the needs of soldiers or federal employees. The business may have given money to a military support organization in order to receive a certificate or plaque of appreciation, which are then prominently displayed at a business location or website—again, capitalizing on common affinity marketing techniques. These are all usual bait presented to our service members, bait placed at the fingertips of our soldiers.

We have seen this in our litigation and investigations. The soldiers are targeted for the reasons cited above—they have paychecks, they will repay their debts, and they won’t complain.

In one compelling example, the staff of a predatory business was trained to only sell to soldiers. When our office sent in a non-military staff member to explore purchasing from this business, she was directed to Walmart. The business was unwilling to sell its wares to anyone other than military, and refused any payment other than by allotment. In this particular instance, the business (located in the local mall), didn’t even have a cash register or credit card reader at the store locations—only a stack of pre-filled finance agreements.

Some businesses are willing to accept non-allotment payment, but there typically is a very significant financing agreement accompanying the transaction, and usually some type of auto-payment required.

This should beg the question--what is the business selling?

This office has found time and again that the real product is not the truck, the computer, the education program, the sofa, the bedroom set, the auto detailing—it is the financing. And, as stated, the financing often comes directly out of the soldier’s pay, with a back-up payment method already in place.

“Military paper” is how this class of product is described, and it generally bears no relationship to the value of the product financed, thereby maximizing profitability in a shadow industry which profits from this type of lending. There is a low entry cost and substantial profit.

What’s an unlicensed lender? This is a class of private financing which is largely unregulated. It is not per se unauthorized, but it can be a black hole for consumers and treacherous territory for soldiers. On their face, the amounts are low. The interest rates are ostensibly capped. They are theoretically not payday loans because there is a tangible product

passing hands. Nowhere on the paperwork is there any indication that the lender is anything other than a bank or a sanctioned loan company. The devil is in the detail.

In 2010 the New York Attorney General sued SmartBuy and two unlicensed, predatory lenders. These were the same cast of characters who had just been driven out of Tennessee, now operating under slightly different names. There was the bait—electronics, and the hook—financing. On its face, these were open-ended retail installment contracts from a lender, collateralized by the electronics sold. In reality, the outrageously high (and undisclosed) interest rates (over 200%) were stuffed into the “purchase price,” making the stated interest rate appear to be within the range of predictable and authorized (10-12%). But there was underlying deceit: There were undisclosed loan costs associated with the required military allotment payment method. The full retail value of the product was never disclosed to the consumer. Sales persons soothed soldiers stating that the deals and interest rate were comparable to BestBuy. The soldier authorized the lender to contact command for a laundry list of issues, including collection. There was no way out of the contract even if a soldier wanted to return the product within the very short return period—there was a very expensive restocking fee which was required to be paid in cash. This type of contract skirts Military Lending Act protections, and also skirts lending laws.

Is overpayment a problem? Just because a soldier overpays—even dramatically—for a consumer good, does that mean there has been some sort of nefarious conduct? Likely, but not necessarily. Yet when the true price of a product has been buried in per paycheck price explanations, where the true effective interest rates are nowhere disclosed, where the contract deceptively bypasses existing state and federal regulations by artfully framing the deal, consumers—and soldiers in particular—can be seriously hurt.

Have you ever pulled your current pay statement as part of a small consumer transaction? Short of purchasing a home or seeking a bank loan, it is safe to say that most of us have not. This is not the case for our service men and women. Routinely they are walked to a computer by vendors/lenders and asked to pull their LES (leave and earnings statement). Routinely they are asked for a copy of their military identification. Routinely they are asked to produce the name and contact information of their commander. When addressing soldiers as part of financial readiness training, I point out to them that this is not acceptable. They are stunned. It is a way of life for our soldiers.

As part of our SmartBuy investigation, an employee bragged to our undercover investigator that it was apparent after reviewing an LES, the soldier did not have sufficient unencumbered room for another allotment on his pay. The employee cancelled a different allotment in order to accommodate the new one. There is competition in this dark market.

As a resident near Fort Drum, I personally went into a rental car franchise to rent a vehicle. I presented my driver's license and a credit card and was handed a set of keys. At the same time, a young Army officer came in to rent a car. He was required to produce his driver's license, military identification, credit card, commander's name and contact information, and then was walked to a computer to print out his last LES. It is not right, and it cultivates the opportunity for predatory practices and abusive collection.

Time and again we are told that these soldiers have bad credit, that these are the best and only options available to them, and also that without the pressure of a command structure, they will not honor their debts. It is simply not true. The reality of the situation is that these soldiers are being deliberately placed between a rock and a hard place. The hard place is the collections practices.

When a debt goes into collection, it is a big problem for a soldier—they face potential disciplinary action, loss of rank, and potential loss of security clearances. Vendors know this, and they capitalize on the vulnerability.

The Fair Debt Collections Practices Act makes clear that debt collectors are not to contact third parties (read: employers) regarding a debt without express permission granted by the consumer, and the debt collector is further not permitted to utilize harassment, abuse, or false and misleading representations in the collection of any debt. In the experience of our office, these protections are routinely bypassed or disregarded.

These predatory contracts contain provisions permitting the lender to directly contact a soldier's chain of command to discuss the debt. Soldiers are routinely threatened that their command will be contacted. In some extreme instances, soldiers are threatened that military police will arrest them should they not recommence payment on debts. This form of terrorism is so prevalent that we've seen soldiers harassed for debts they have never even incurred—and many times they pay because the consequences of taking a stand are so consequential.

This situation presents problems for our soldiers, and also their commanders. I received a call from an officer on post, concerned that he was asked to respond and resolve problems on the "hotline." As he put it, he regularly received calls from businesses that soldiers were not paying on various debts, and there was only one part of that equation he had control over—the soldiers. We gave him some tools to push back.

The deception and the predatory behavior are not, however, obvious to anyone other than ourselves. We receive complaints from soldiers only when they cannot understand why they have already paid over \$8,000 on a computer, but it is not paid off yet. We receive calls when a soldier is about to have security clearance terminated because of a debt they did not even know they had. We do not get complaints from soldiers that they have been paying illegal rates of interest, or were duped into a predatory transaction—they simply don't know.

The inevitable question arises: Is this a group of bad actors, or are there systemic failures, or both? In our experience, the answer is both. There are always "frequent fliers" who cultivate a degree of chaos which makes, for example, a move from Tennessee to New York nearly imperceptible, and which makes the transactions themselves appear legitimate to an uninformed reviewer. There are also abusive business and investment models which permit billions of dollars of fraud to evade regulatory oversight. These issues deserve our collective attention and redress. To this end, by letter dated June 23, 2013, Attorney General Schneiderman and several other attorneys general led by Delaware and Illinois, urged significant reform of the implementing regulations for the Military Lending Act. Large loopholes must be closed, including modifying the definitions of consumer credit to provide more comprehensive protections. The regulations

must recapture loans which are open-ended or revolving, all auto title loans, any bank loan secured by funds on deposit, and all retail sales credit loans or other similar rent-to-own transactions. Similarly, age-old traditions such as payment by allotment must be revisited to review their efficacy in our modern age. What once was efficacious may now be simply a tool of abuse. The sanitizing role of regulatory oversight must also be considered—should billions of dollars of loan work be ignored simply because the victims are many and the individual loan amounts low? Clearly the answer is no.

Thank you for your attention to these abusive practices, and your dedication to protecting the brave men and women serving in our military.