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**Before the  
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Chairman Rockefeller, Ranking Member Thune, and distinguished Members of the Committee, I'd like to thank you for the opportunity to speak with you today concerning consumer protection for the military, particularly in the area of predatory lending to servicemembers and their families.

Many of you already know me as I've testified before you on other committees, and I've also had the opportunity to visit with some of you in your home States. But for those of you who are not familiar with my office, the Office of Servicemember Affairs at the Consumer Financial Protection Bureau (Bureau or CFPB), I'd like to take a few moments to tell you what we do.

As laid out in the Dodd-Frank Act, the Office of Servicemember Affairs at the Bureau is responsible for:

- Developing and implementing initiatives to educate and empower servicemembers and their families to make better-informed decisions regarding consumer financial products and services;
- Monitoring complaints submitted by servicemembers and their families about consumer financial products and services, and the responses to those complaints; and
- Coordinating the efforts of Federal and State agencies, as appropriate, regarding consumer protection measures relating to consumer financial products and services offered to, or used by, servicemembers and their families.

Obviously my mission ties in very directly to the issues that you'd like to address today. Before I go into what we're doing at the Bureau when it comes to predatory lending, however, I'd like to add a little historical perspective. Before I came to the Bureau, I was at the Council of Better Business Bureaus from 2004 to 2010, running their BBB Military Line program. In that role, I had a ringside seat for the fight to create and pass the original Military Lending Act (MLA), which was designed to protect servicemembers from the predatory lenders that were springing up around military bases in ever-increasing numbers.

I've lived on or near military installations my entire life, and it's a fact that a great many of them have a "strip" of businesses outside the gates, offering military families everything from furniture to used cars to electronics to jewelry – and the high-cost credit to pay for them, as well. But in the early 2000s there was an alarming increase in the number of businesses offering the new phenomenon of "payday loans," and a corresponding increase in the number of

servicemembers taking advantage of that easy money, often without the ability to repay what they borrowed. To cite evidence from one of the military relief societies: “In 2001, Navy-Marine Corps Relief Society provided only \$5,000 to 9 service members falling victim to the predatory lending industry. In 2006, Navy-Marine Corps Relief Society provided over 1.37 million dollars to military members and/or families who were victimized by predatory lenders.”<sup>1</sup>

The Pentagon took notice of the fact that indebtedness was beginning to take a serious toll on military readiness. On May 3, 2006, Adm. Mike Mullen, [then] Chief of Naval Operations wrote in an administrative memo to Navy personnel: “A sailor’s financial readiness directly impacts unit readiness and the Navy’s ability to accomplish its mission.... I am concerned with the number of sailors who are taken advantage of by predatory lending practices, the most common of which is the payday loan.”<sup>2</sup> The national news media also took note: “Thousands of U.S. troops are being barred from overseas duty because they are so deep in debt they are considered security risks, according to an Associated Press review of military records.”<sup>3</sup>

And two academics undertook a major study of the problem in 2005, looking at the geographic distribution of payday lenders across the U.S. to see if there was, in fact, a disproportionate number of payday lenders targeting military personnel.<sup>4</sup> Professors Chris Peterson and Steven Graves examined the density of payday lenders in 20 states. Their work described “an environment where servicemembers are literally surrounded by lenders clamoring to charge annual rates averaging around 450 percent.”<sup>5</sup> They showed that even considering other variables such as income and ethnicity, the counties and zip codes that had the greatest overrepresentation of payday lenders tended to have one thing in common: proximity to large military populations. For example, in California, Texas, Virginia, and Washington (states with large servicemember populations), the study showed at least 60 percent of the 20 highest payday lending zip codes were associated with military installations. To quote Peterson and Graves: “payday lenders crowd around the gates of military bases like bears on a trout stream.”<sup>6</sup>

By 2005, the use of high-cost credit targeting servicemembers was being discussed in the halls of Congress, and Senator Elizabeth Dole requested that the Department of Defense (Department or DoD) report on predatory lending practices. On August 9, 2006 the Department did just that, publishing a report entitled “Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents.” The report found that: “predatory lending undermines military readiness, harms the morale of troops and their families, and adds to the cost of fielding an all-volunteer fighting force. Education, counseling, assistance from Aid Societies, and sound alternatives are necessary but not sufficient to protect Service members from predatory lending

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<sup>1</sup>[http://www.cnic.navy.mil/regions/ndw/installations/nsa\\_annapolis/ffr/support\\_services/counseling\\_and\\_assistance/personal\\_finance\\_management/danger\\_of\\_payday\\_loans.html](http://www.cnic.navy.mil/regions/ndw/installations/nsa_annapolis/ffr/support_services/counseling_and_assistance/personal_finance_management/danger_of_payday_loans.html)

<sup>2</sup> Navy League, Sea Power Magazine, June 2006

<sup>3</sup> [http://www.nbcnews.com/id/15337932/ns/us\\_news-military/t/debt-holds-us-troops-back-overseas-duty/#.UILD3tKkrYc](http://www.nbcnews.com/id/15337932/ns/us_news-military/t/debt-holds-us-troops-back-overseas-duty/#.UILD3tKkrYc)

<sup>4</sup> Steven M. Graves & Christopher L. Peterson, Predatory Lending and the Military: The Law and Geography of “Payday” Loans in Military Towns, 66 OHIO ST. L.J. 653, 672 (2005)  
<http://www.law.fsu.edu/faculty/2005workshops/peterson.pdf>

<sup>5</sup> Graves & Peterson, p. 153.

<sup>6</sup> Graves & Peterson, p. 145.

practices or products that are aggressively marketed to consumers in general and to military personnel directly.”<sup>7</sup>

Senator Dole stated at a Senate Banking hearing to discuss the report: “Predatory lenders are blatantly targeting our military personnel, undermining their financial stability and tarnishing their service records. This practice not only creates financial problems for individual soldiers and their families, but also weakens our military’s operational readiness....”<sup>8</sup>

Then-Undersecretary of Defense for Personnel and Readiness David Chu at that same hearing stated: “We need legislative action, to get to the bottom line because without it, we cannot curtail the migration of this set of predatory practice to other products.”<sup>9</sup>

Congress passed the bipartisan Talent-Nelson Amendment (also known as the Military Lending Act) in 2006 and it was signed into law on October 17, 2006 (P.L. 109-364) (10 U.S.C. 987) – and I should note, with appreciation, that one of the authors, Senator Bill Nelson, is on this Committee. Senator Talent said of the amendment, “The fact is, predatory payday lenders are targeting American troops and are trying to make a buck off of their service to our country. We rely on the military to protect us, and we have just taken a significant step to protect them from predatory lenders.”<sup>10</sup>

The Talent-Nelson Amendment does two important things for military consumers: (1) it expressly caps the rate at which a creditor extends consumer credit to a covered member of the armed forces or a dependent of a covered member, prohibiting annual percentage rates, including fees, greater than thirty-six percent; and (2) it creates a series of consumer protections for covered members and dependents (for example, a prohibition on the mandatory use of an allotment to repay the debt and a prohibition on requiring a covered member or dependent to submit to arbitration to resolve disputes related to the credit contract).

DoD was given the task of drafting implementing regulations (32 C.F.R. Part 232) for the Military Lending Act, and they were published on August 31, 2007. DoD opted to define consumer credit covered by the Act to include only three types of consumer loans, and to define those fairly narrowly. In general, the three types of loans are:

- Payday loans: closed-end loans with terms of 91 days or fewer, for \$2,000 or less;
- Auto title loans: closed-end loans with terms of 181 days or fewer; and
- Refund anticipation loans: closed-end credit.

I think it is widely accepted that for those products that fall within the Department’s definition of “consumer credit” the law has had a positive impact. When the Consumer Federation of America took a look at the Military Lending Act five years after implementation, they concluded: “To the extent products met these definitions, the law has been largely effective in

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<sup>7</sup> [http://www.defense.gov/pubs/pdfs/Report\\_to\\_Congress\\_final.pdf](http://www.defense.gov/pubs/pdfs/Report_to_Congress_final.pdf)

<sup>8</sup> <http://www.gpo.gov/fdsys/pkg/CHRG-109shrg50303/html/CHRG-109shrg50303.htm>

<sup>9</sup> Ibid.

<sup>10</sup> <http://www.gpo.gov/fdsys/pkg/CREC-2006-06-22/pdf/CREC-2006-06-22-pt1-PgS6406.pdf>

curbing predatory payday, car title, and tax refund lending to covered borrowers.”<sup>11</sup> However, the MLA’s protections only apply if the credit product falls within the DoD’s limited definition of consumer credit. For example, even if a servicemember or their spouse takes out a payday loan with a military annual percentage rate (MAPR) in excess of 36 percent, agencies with administrative enforcement authority under the law are unable to enforce the protections of the MLA if that loan is for a term greater than 91 days, over \$2,000, or structured as open-end credit.

The increasing concern now is that lenders have easily found ways to get outside of the definitions in the current DoD rule implementing the MLA. As I testified before the Senate Banking Committee in June 2012: “I hear from financial counselors on the installations about the prevalence of payday-like products that are specifically marketed to military families – often with patriotic-sounding names and the American flags on the website to match, but with a sky-high interest rate for the servicemember who takes out the loan. And the internet is full of ‘military loans,’ some outright scams and others with very high interest rates. Although the Military Lending Act put a 36 percent cap on the annual percentage rate of certain types of loans to the active-duty military, some lenders have found ways to get outside of the definitions in the Department of Defense (DoD) rule implementing the Military Lending Act.”<sup>12</sup>

In some states, state law allows a broad range of high-cost credit products that fall outside of the narrow band of products covered by the current rule. For example, California, Texas, and Virginia – together home to more than a third of our active-duty servicemembers – all permit auto title loans of longer than 181 days as well as high-cost installment loans. And in many states across the country, banks offer deposit-advance loans – lines of credit offered in connection with a borrower’s deposit account. As discussed in more detail in the Bureau’s recent white paper on payday loans and deposit advance products, when the Bureau used a special fee-based APR calculation in order to help compare deposit advance products to payday loans for purposes of the paper, it found that that APR could exceed 300 percent.

In my almost three years at the Bureau I have had the opportunity to visit more than 70 bases and National Guard Units. And at nearly every stop issues related to high-cost lending come up. Here are just a few of the stories I’ve heard on the road:

- The spouse of a wounded warrior in the Illinois National Guard took out an auto title loan of \$2,575 at an APR of 300 percent. The finance charges on the loan were \$5,720.24 for a total amount of \$8,295.24. The loan was not subject to the Act’s protections under the current rule because it had a term longer than 181 days.
- At the Airman and Family Readiness Center at Travis Air Force Base, California I heard about a servicemember who borrowed \$6,000. He financed this amount for 36 months at 102.47 percent APR. The loan cost the servicemember \$13,463.04 and was secured by the title of his car. The loan was not subject to the MLA’s protections under the current rule because it was for a term longer than 181 days.

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<sup>11</sup> <http://www.consumerfed.org/pdfs/Studies.MilitaryLendingAct.5.29.12.pdf>

<sup>12</sup> <http://www.consumerfinance.gov/newsroom/written-testimony-of-holly-petraeus-before-the-senate-committee-on-banking-housing-and-urban-affairs/>

- From one of the military aid societies I heard about servicemembers from North Carolina and Delaware who each took out loans at an APR of 584.68 percent. The loans were not subject to the Act’s protections under the current rule because they were structured as open-end lines of credit.
- A JAG at Marine Corps Recruit Depot-San Diego had a client who took out an auto title loan of \$10,000. The terms of the loan were 36 months with an APR of 101.9 percent. The Marine used his military ID to get the loan, so they were aware of his military status, but because the amount and duration of the loan exceeded the parameters of loans covered by the current rule the protections of the Act did not apply.
- A community readiness consultant at Joint Base McGuire-Dix-Lakehurst in New Jersey told me about a sailor with severe debt problems. He had one loan from a military-specific lender with an APR at 499 percent. This loan was not subject to the protections of the Military Lending Act because it was structured as an open-end line of credit. The sailor had a second loan at an APR of 197 percent with a balance of over \$1,500. This loan was not subject to the Act’s protections under the current rule because it was for a term longer than 91 days. The sailor was paying over 66 percent of his take-home pay trying to pay off these two loans.

There are also studies that have been done about the continued prevalence of high-cost lenders targeting military families. As part of its latest research on payday lending, The Pew Charitable Trusts found that: “5.9 percent of payday and auto title loan borrowers live in a household that includes current members of the Armed Services. Comparatively, 2.5 percent of U.S. households overall are active duty, in the National Guard, or in training. This difference is statistically significant.”<sup>13</sup>

And DoD has also reported that: “(U)nscrupulous lenders have sought, and are seeking, to create products and services which fall outside of the MLA and the enforcement actions mentioned above. Several years removed from its enactment, however, our financial counselors and legal assistance attorneys still see clients who have payday or vehicle title loans. They also report that internet and overseas opportunities exist to evade the law, and that some unscrupulous lenders – and even borrowers – still attempt to skirt or evade the law, by entering into loans that charge interest greater than 36 percent and contain terms that have been modified to avoid falling under the MLA. Creditors and lenders still attempt to avoid the MLA by utilizing procedures or modifying products to fall outside of the regulation.”<sup>14</sup>

Concerns about the effectiveness of the current rule have led to renewed interest from Congress. Recently, thanks in large part to the efforts of Senators Reed, Blumenthal, and others, we have seen updates to the Act through amendments signed into law in January of this year. Based on those amendments, DoD is taking another look at the effectiveness of the MLA, which may include rewriting the rule as appropriate. And they provided enforcement authority for the Act to federal regulators, including the Bureau. As a result, in September the Bureau announced amendments to our Supervision and Examination Manual incorporating the requirements of the

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<sup>13</sup> Letter from Nick Bourke, Project Director, the Pew Charitable Trusts to Holly Petraeus, February 26, 2013.

<sup>14</sup> [http://www.veterans.senate.gov/hearings.cfm?action=release.display&release\\_id=f3ab7d1a-7bbe-48ee-a476-9b812241ea8c](http://www.veterans.senate.gov/hearings.cfm?action=release.display&release_id=f3ab7d1a-7bbe-48ee-a476-9b812241ea8c)

Military Lending Act so our Supervision teams can be actively checking for compliance with the Act. We also released guidelines to our examiners on how to identify consumer harm and risks related to Military Lending Act violations when supervising payday lenders.<sup>15</sup>

DoD has now begun exploring potential revisions to its existing regulation. It put an Advance Notice of Proposed Rulemaking (ANPR) in the *Federal Register* on June 17, 2013, requesting input from counselors, legal assistance attorneys, servicemembers, consumer protection advocacy groups, representatives of the financial services industry, and other interested parties.

The comments submitted in response detailed many of the concerns about evasion of the provisions of the MLA:

- The Colorado Attorney General wrote: “Given the narrow definitions, lenders have easily circumvented the purpose and protections intended by [the] MLA by simply offering 92 day loans, loans for \$2001, or by structuring the loans as open-end credit.”<sup>16</sup>
- Separately, a bipartisan group of 13 Attorneys General wrote: “While the MLA has been largely successful in curbing abusive lending in those categories covered by the Department’s current rules, the narrow categories and definitions create large loopholes that permit lenders to fashion abusive or predatory transactions that avoid the MLA’s protections.”<sup>17</sup>
- Consumer advocates in Texas wrote: “Store visits conducted by Texas Appleseed in Killeen, Texas reveal that some storefronts surrounding military bases have pivoted to offering high-cost multiple-payment products to service members. For example, at least one national payday lender with two locations in Killeen, both within three miles of Fort Hood, offers six-month multiple-payment payday loans up to \$3000 with a fee of \$22 for every \$100 borrowed. Combined with \$36.26 in interest and fees, a \$1500 multiple-payment loan therefore costs the borrower \$386.26 if the loan is paid back on schedule for an annual percentage rate of 581.72 percent. The MLA does not include these multiple-payment payday loans, even though they contribute to the cycle of debt.”<sup>18</sup>
- Comments from the head of the Illinois Department of Veteran Affairs extended beyond the active-duty population: “Approximately one out of every ten veterans reported having more than \$40,000 in unsecured debt. For many veterans, some of this debt is acquired while on active -duty, often from high-cost lenders that frequently target military bases.” She also noted that in Illinois, “the current Department of Defense rule does not apply to all forms of payday lending permitted by state law....”<sup>19</sup>
- 23 of your Senate colleagues also weighed in: “Due to the narrow definition of consumer credit, certain lenders are offering predatory loan products to service members at exorbitant triple-digit effective interest rates and loan products that do not include the additional protections envisioned by the law. As such, a wide range of credit that is

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<sup>15</sup> <http://www.consumerfinance.gov/newsroom/cfpb-lays-out-guidelines-for-protecting-servicemembers-in-the-payday-lending-market/>

<sup>16</sup> <http://www.regulations.gov/#!documentDetail:D=DOD-2013-OS-0133-0034>

<sup>17</sup> <http://www.regulations.gov/#!documentDetail:D=DOD-2013-OS-0133-0002>

<sup>18</sup> <http://www.regulations.gov/#!documentDetail:D=DOD-2013-OS-0133-0016> (accessed July 31, 2013)

<sup>19</sup> <http://www.regulations.gov/#!documentDetail:D=DOD-2013-OS-0133-0006> (internal citation omitted)

structured as open-ended versus closed-ended or that otherwise is structured to evade the limitations set forth in the current regulations fall completely outside the law's intended prohibitions.”<sup>20</sup>

The Department has since asked a group of Federal agencies, including the Bureau, the Department of the Treasury, the Federal Deposit Insurance Corporation, the Federal Reserve Board of Governors, the Office of the Comptroller of the Currency, the National Credit Union Administration, and the Federal Trade Commission, to assist it as it takes a fresh look at the MLA rule. In July of this year, Col. Paul Kantwill, Director of Legal Policy, Office of the Undersecretary for Personnel and Readiness, Department of Defense, testified before the Senate Veteran Affairs Committee: “the Department has assembled the Prudential Regulatory Agencies and the CFPB to explore revisions to the regulation. We have established a team of skilled economists and analysts to assist us in this initial rulemaking, in addition to a similarly-skilled team of drafters.”<sup>21</sup> We are pleased to be helping the Department as they undertake this effort, and fully support the efforts of the Department and the working group.

Some parties have raised concerns about changes to the MLA regulations severely limiting access to credit for servicemembers. In fact, servicemembers do have lower-cost, less risky alternatives that are available to them, and that DoD encourages them to utilize.

For one thing, each branch of the service is supported by what is called a military relief society<sup>22</sup>, which offers small no-interest loans and grants to servicemembers in need of emergency funds. In 2012, the relief societies provided \$142.2 million in no-cost loans and grants to 159,745 clients.

As the Department noted however back in 2006: “We are continuing to improve the already substantial system of support available to them, but we need your assistance in limiting the availability of loans that fail to consider the ability of the borrower to repay so that service members can and will consider other alternatives.”<sup>23</sup>

In December of 2011, my office held a full-day Financial Fitness forum where one of the panels specifically discussed alternatives to high-cost, high-risk loan products.<sup>24</sup> Many of the programs that were highlighted at that forum were discussed as part of the Department’s original report to Congress in 2006 – where the DoD listed 24 different alternatives to high-cost loans.<sup>25</sup>

The bottom line, from my perspective based on what I have seen and heard in recent years, is that I have real concerns about the ability of lenders to easily evade the current MLA regulations. The original rule was effective for those products that it covered, but over the past 6 years we

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<sup>20</sup> <http://www.regulations.gov/#!documentDetail;D=DOD-2013-OS-0133-0036>

<sup>21</sup> [http://www.veterans.senate.gov/hearings.cfm?action=release\\_display&release\\_id=f3ab7d1a-7bbe-48ee-a476-9b812241ea8c](http://www.veterans.senate.gov/hearings.cfm?action=release_display&release_id=f3ab7d1a-7bbe-48ee-a476-9b812241ea8c)

<sup>22</sup> Army Emergency Relief, Navy-Marine Corps Relief Society, Air Force Aid Society, Coast Guard Mutual Assistance

<sup>23</sup> <http://www.gpo.gov/fdsys/pkg/CHRG-109shrg50303/html/CHRG-109shrg50303.htm>

<sup>24</sup> [http://files.consumerfinance.gov/f/201209\\_cfpb\\_Financial-Fitness-Whitepaper.pdf](http://files.consumerfinance.gov/f/201209_cfpb_Financial-Fitness-Whitepaper.pdf)

<sup>25</sup> [http://www.defense.gov/pubs/pdfs/Report\\_to\\_Congress\\_final.pdf](http://www.defense.gov/pubs/pdfs/Report_to_Congress_final.pdf)

have seen significant changes in the type of products offered and the contours of state law, and I think it's critically important to ensure that the MLA protections keep up. I believe that any approach that has strict definitions that define individual products will fall victim to the same evasive tactics that are plaguing the current rule. And I know this is a shared concern with the Department.

I also believe that from a military financial readiness point of view it makes no difference whether the loan is made by a depository institution or a non-depository institution, nor does it matter whether the loan is structured as open- or closed-end. A loan with a sky-high interest rate, onerous arbitration requirements, and burdensome fees has the same adverse impact on military financial readiness no matter who offers it.

Also, as Senator Talent said back in 2006: "Our troops deserve uniform, national protection against abusive financial practices that target them." I do not see the logic in a soldier at Fort Drum, New York having different protections from one at Fort Hood, Texas.

I've heard quite frequently that DoD should fall back on financial education or command influence to deal with these issues. In fact, that was in some of the responses to the ANPR. On that subject I agree with what the Department wrote in the original preamble to the regulation: "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."<sup>26</sup>

In sum, the underlying goals of protecting military and financial readiness that led to passage of the MLA in 2006 are as important today as they were when the Act was originally passed. I think we should all be indignant when we hear of servicemembers trapped in outrageous loans and realize that there is little we can do under the current regulations because they are just longer than 91 days or structured as open-end credit. We owe it to our servicemembers and their families to do the best possible job of crafting rules that properly implement the intent of the Military Lending Act.

I'll close with a quote from Senator Elizabeth Dole who was a leader in getting the original Act passed: "Supporting our service members means more than providing the equipment and training necessary for fighting .... We should also support their livelihood and their families, and predatory lending can seriously harm both."<sup>27</sup> I look forward to working with you, the Department and all stakeholders who have an interest in accomplishing these goals.

Thank you.

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<sup>26</sup> <http://www.gpo.gov/fdsys/pkg/FR-2007-08-31/pdf/07-4264.pdf>

<sup>27</sup> <http://www.gpo.gov/fdsys/pkg/CHRG-109shrg50303/html/CHRG-109shrg50303.htm>