

CERTIFICATION NEWS



Regulatory Compliance

Military Lending Act—What You Need to Know

By *Ania Scanlan*

Did you know that the Department of Defense regulates a portion of your community bank's lending activities and that changes were recently made to the rule? The rule impacts all financial institutions and important compliance dates are coming up quickly. Compliance with the final rule implementing the Military Lending Act (MLA) is required by Oct. 3, 2016, for the majority of credit products. For credit cards, compliance is

required by Oct. 3, 2017. The regulations implementing the amended MLA can be found in 32 CFR Part 232.

Overview

In essence, the Department of Defense amended its MLA regulation to define consumer credit consistently with the Truth in Lending Act and its implementing Regulation Z. This amendment allows the MLA requirements to apply to a wider range of credit products that currently fall outside of the law's scope. The rule requirements apply to covered borrowers who are also covered members of the military.

There are a few significant provisions of this new rule that community bankers must take note of. First, the MLA caps the amount of interest that a lender may charge on consumer credit at 36 percent. This military annual percentage rate (MAPR) cap will now apply to a wider range of closed-end and open-end credit products due to the new definition of credit

See [MLA](#), page 2



PROFESSIONAL PROFILE

Get to Know Charles W. Trump Jr., an ICBA Certified Banker in Pennsylvania

By *Runay Olson*

Charles Trump is the vice president at First Federal Savings and Loan Association of Greene County in Waynesburg, Pa. He became a Certified Community Bank Security Officer in 2009 and a BSA/AML Professional in 2010 through ICBA's certification programs.

What makes a community bank different from the largest banks?

Trump: Often, community, hometown banks provide more personalized service experiences, as

Fact Check

First Federal Savings and Loan Association of Greene County

Headquarters: Waynesburg, Pa.

Retail offices: Nine

Bank asset size: \$900 million

Number of bank employees: 130

Number of staff in auditing and BSA/AML: Five

Website: www.firstfederalofgreene.com

Taglines/Motto: The people you know, the people you trust

See [Profile](#), page 3

Audit Institute (Week 1)

- Sept. 12-16; Minneapolis

Audit Institute (Week 2)

- Sept. 19-23; Minneapolis

Annual Current Issues/ Certification Conference

- Oct. 4-7; Minneapolis
- Oct. 17-20; Orlando, Fla.

Bank Security Institute

- Sept. 11-14; Minneapolis

BSA/AML Institute

- Aug. 1-3; Denver
- Nov. 7-9; Dallas

Community Bank IT Institute

- Aug. 8-12; Minneapolis

Compliance Institute

- Sept. 25-30; Denver

Consumer Lending Institute

- Sept. 18-21; Minneapolis

Commercial Lending Institute

- Oct. 23-28; Phoenix

Credit Analyst Institute (NEW)

- Aug. 14-17; Minneapolis

MLA, continued from page 1

the MLA adopted. Second, the lender must provide detailed disclosures, including all disclosures applicable to a specific credit product under Regulation Z, a statement of MAPR, and a description of the borrower's payment obligations. Finally, the safe harbor provisions were amended to allow a creditor to use their own method of determining coverage (see Safe Harbor section below).

Determination of Coverage

Banks must determine whether a credit applicant is a covered borrower at the time the consumer becomes obligated on a consumer credit transaction or establishes an account for consumer credit. Consumer credit under the MLA now has the same definition as under Regulation Z, meaning primarily for personal, family, or household purposes, that is (i) subject to a finance charge, or (ii) is payable by a written agreement in more than four installments.

Covered Credit Products

On Oct. 3, 2016, all forms of vehicle title loans, installment loans, unsecured open-end lines of credit, payday loans, refund anticipation loans, and deposit advance loans become subject to the requirements under MLA. Your bank has until Oct. 3, 2017, to comply with these requirements for credit cards.

Exempted Credit Products

The MLA exempts certain credit products from its requirements including:

- residential mortgages;
- any credit transaction that is secured by and expressly intended to finance the purchase of a motor vehicle and personal property;
- any credit transaction that is an exempt transaction for the purposes of Regulation Z (other than a state exempted transaction under 12 CFT 1026.29); and
- any credit transaction when it is determined that a consumer is not a covered borrower by using a safe-harbor method.

Who is a Covered Borrower?

A covered borrower is always a consumer. If that consumer, at the time he or she becomes obligated on a consumer credit transaction or establishes an account for consumer credit, is a "covered member" or a dependent of a covered member, then he or she is deemed to be a covered borrower.

This definition requires banks to also understand the concept of a "covered member." A covered member is a member of the U. S. Armed Forces who is serving on active duty or who is serving on active Guard or Reserve duty.

The new MLA requirements also apply to dependents of covered borrowers. Dependents include:

- spouses,
- dependent children (under 21 years of age or who meet other conditions),
- parents and in-laws dependent on the servicemember for more than half of their support,
- un-remarried widows and widowers of covered borrowers, and
- any person over whom the servicemember has custody ordered by a court.

Some of these dependents may need to meet other conditions in order to qualify as a dependent for the purposes of the MLA (see 10 U.S.C. 1072(2) for details).

Safe Harbor

The MLA rule prescribes two methods for conducting a covered-borrower check. The first method is to use information obtained from the Department of Defense's Defense Manpower Data Center's (DMDC) database. The second method is to use information obtained from a qualified nationwide consumer reporting agency record (e.g. included on a credit report). The MLA rule does not require a specific method to be used to determine a covered borrower, thus lenders are permitted to use other methods. However, the safe harbor applies only if a lender uses one of the two determination methods specified in the MLA.

Under the rule, lenders must also timely create and maintain a record of the information obtained from the DMDC database or from a consumer reporting agency. Generally, the determination must be made no more than 30 days prior to the date a consumer applies for credit. This provision provides for changes to a consumer's status of serving in the U.S. Armed Forces and ensures that banks will make a determination based on current information available to them.

Military Annual Percentage Rate

The MAPR is capped at 36 percent for covered transactions. This calculation is

different from the finance charge calculation that Regulation Z requires be disclosed for all consumer loan transactions. In simple terms, the MAPR is more inclusive than the finance charge calculation and includes several loan fees and charges that would not be considered part of the finance charge calculation under Regulation Z.

Charges Included in MAPR

The MAPR includes the following charges when they are applicable to an extension of consumer credit:

- any premium or fee for credit insurance;
- any fee for a debt cancellation contract;
- any fee for a debt suspension agreement;
- any fee for a credit-related ancillary product sold in connection with the credit transaction for closed-end credit or an account for open-end credit; and
- except for a bona fide fee (other than a periodic rate) which may be excluded under special rules for credit card accounts, the following:
 - finance charges, as defined in Regulation Z, associated with the consumer credit;
 - any application fee charged to the covered borrower (except when the application fee is charged in connection with a short-term, small amount loan); and
 - any participation fee (except as provided in special rules for open-end credit).

Charges Excluded from MAPR

For credit card accounts, creditors who offer consumer credit card accounts may exclude from the MAPR any "bona fide" and reasonable fees, other than a periodic rate. For example, the application fee, participation fee, annual fees and balance transfer fees may be excluded. Credit insurance and debt protection premiums and fees, and credit-related ancillary product fees must be included in the MAPR calculation for credit cards regardless of whether they are bona fide and reasonable.

Required Disclosures

In addition to providing a covered borrower with the traditionally-required Regulation Z disclosures, banks must also provide "a statement of the MAPR" and a clear description of the payment obligation.

A "statement of the MAPR" applicable to the extension of credit must be provided

MLA, continued from page 2

both, in writing and orally. The statement must describe the charges a lender may impose, but it does not need to include a numerical value or dollar amount of the charges included in the MAPR. A model statement is outlined in the regulation.

Civil Liability

The MLA also prohibits requiring a borrower to waive his or her right to legal recourse, to submit to arbitration, or to waive rights available to the borrower under the Servicemembers Civil Relief Act.

Under the rule, civil liability can be imposed for a violation of the requirements of the implementing regulation. A person who violates the MLA and its implementing regulation will be civilly liable to a covered borrower, as follows:

- any actual damage sustained as a result of a violation, but not less than \$500 for each violation;
- appropriate punitive damages;
- appropriate equitable or declaratory relief; and
- any other relief provided by law.

In addition, a person found to have violated

the requirements will be held liable for the costs of the action along with reasonable attorney fees, as a court determines. If the violation was unintentional and resulted from a bona fide error, no civil liability will be imposed.

The Servicemembers Civil Relief Act protections remain unchanged and are not affected by the amended Military Lending Act and its implementing regulation.

What Does This Mean for You?

If your community bank offers consumer credit to borrowers, here are some next steps:

- Take a deep breath – you’ve got this!
- Familiarize yourself with the requirements of the final rule and the implementing regulation.
- Determine any process and system changes, and the budget that may be needed to comply with the new requirements.
- Determine how consumer loan applicants will be screened to determine “covered borrower” or “covered member” status. In other words, determine whether a safe harbor method will be used by the bank

to determine classification.

- Contact the nationwide credit bureau(s) your bank uses to pull credit reports to determine whether the bureau will be able to provide your bank with the safe harbor information.
- If the Department of Defense database will be used to verify borrower military status, update bank procedures and resources with the official weblink: <https://mla.dmdc.osd.mil>
- Check with your loan platform or loan documentation system to determine whether it will calculate the MAPR and generate the MLA disclosures.
- Update procedures and provide training to staff and management.
- Document your process changes, procedures and training.
- Be ready to start your new process by the compliance date of Oct. 3, 2016, for the majority of consumer credit products, and by Oct. 3, 2017, for credit card products.
- Then, periodically audit the process to ensure all procedures function as intended.

Ania Scanlan (ania.scanlan@icba.org) is vice president, Community Bank Compliance Center at ICBA.

Profile, continued from page 1

banks that have existed in our communities for generations (First Federal celebrated 92 years this year!), have established a history of giving, supporting and partnering with their neighborhoods. Relationships have been built and maintained over decades of interaction with and service to our customers.

What makes you most proud about your bank?

Trump: The commitment of our employees who frequently go that “extra mile” for our customers, consistently helping to create a friendly, welcoming atmosphere for our customers, always manifesting great pride for our association. Equally as impressive, the generosity of First Federal to various groups and nonprofit organizations in our communities always inspires me. The giving nature of the bank and its employees, through talent, time, and treasure, is so meaningful. We truly help to create and nurture the care and touching experiences that seem to concentrate the tight-knit nature of our towns and neighborhoods.

How did you find your way into banking?

Trump: A friend of mine invited me to apply for a mortgage officer position ... and so began the adventure!

Tell us your biggest and best accomplishment.

Trump: Personally, fatherhood seems like a clear first place. Professionally, an MBA and the ICBA certifications are probably my best!

What do you like best about the work you do?

Trump: Every day presents new challenges, which keeps each day interesting and boredom-free. Additionally, I am blessed to work with the group of employees who care for our association and for one another. First Federal is truly a special place to work.

What is your bank’s customer-service philosophy?

Trump: In many banking and financial services environments leaders continue to

drive employees to perform as part of a “sales culture.” More strategically, we feel that encouraging employees to perform in a “service culture” is much more effective. This philosophy aids in building the rapport and relationship with our customers that helps meet their needs and strengthens the likelihood that they will remain customers.

What’s your best advice to a new bank employee?

Trump: During your career, align yourself with leaders and institutions that maintain and hold true to convictions similar to those you have. It brings such satisfaction to know that you are working on behalf of reputable, trusted institution and providing a great service to the public. Always look to find the good in each person and situation, and know that with perseverance, focus and humility great things can happen.

Runay Olson (runay.olson@icba.org) is vice president, education seminars, Community Banker University at ICBA.



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COMPLIANCE DATES TO REMEMBER

In June, the Consumer Financial Protection Bureau amended the regulatory text of Regulation Z to update the dollar amounts of various thresholds which are adjusted annually. The majority of the updated thresholds take effect on Jan. 1, 2017. However, the amendment to 1026.52(b)(1)(ii)(B)—which addresses limitations on penalty fees—increased the fee from \$37 to \$38 and becomes effective immediately.

Effective Date	Regulatory Change
Oct. 3, 2016	Military Lending Act effective date
Jan. 1, 2017	HMDA effective date for excluding low-volume depository institutions from coverage
Jan. 1, 2017	Updated Regulation Z Threshold adjustments become effective
Oct. 3, 2017	Military Lending Act effective date for credit cards
Jan. 1, 2018	HMDA final rule effective date for provisions related to institutional and transactional coverage, data collection, recording, reporting and disclosure. Lenders will collect the new information in 2018 and report it by March 1, 2019
May 11, 2018	Must comply with Bank Secrecy Act customer due diligence requirements (beneficial owner rule)

