

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/HB 717 Consumer Credit

SPONSOR(S): Insurance & Banking Subcommittee; Burgess and others

TIED BILLS: **IDEN./SIM. BILLS:** CS/SB 626

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	10 Y, 1 N, As CS	Bauer	Luczynski
2) Government Operations Appropriations Subcommittee	11 Y, 0 N	Keith	Topp
3) Regulatory Affairs Committee	16 Y, 0 N	Bauer	Hamon

SUMMARY ANALYSIS

In 2006, Congress enacted the federal Military Lending Act (MLA) to provide protections to military personnel on active duty for more than 30 days, active National Guard or Reserve personnel, and their dependents from certain closed-end "consumer credit" products (tax refund anticipation loans, payday loans, and auto title loans with certain terms). The MLA protections, which have been implemented by the U.S. Department of Defense (DoD) by rule and are enforceable by various federal financial regulatory agencies, include:

- A 36 percent cap on military annual percentage rate, or MAPR;
- Written and oral disclosures;
- A ban on rollovers and refinancing, unless the new loan results in more favorable terms for the borrower;
- A ban on mandatory waivers of consumer protection laws, including the Servicemembers Civil Relief Act (which protects servicemembers from being sued while on active duty), and a ban on mandatory arbitration; and
- A ban on prepayment penalties and mandatory allotments (i.e., automatic payroll deductions used to repay the loan).

At the state level, various loan products such as payday, title, and consumer finance loans are regulated by the Office of Financial Regulation (OFR), which also charters and supervises state financial institutions such as banks and credit unions. These lenders are required by the Financial Institutions Codes and chs. 516, 537, and 560, F.S., to be licensed by the OFR and to comply with interest or annual percentage rate caps, disclosure requirements, and other provisions.

Due to the MLA's narrow definition of "consumer credit," many lending abuses against the military and their dependents have continued. In response, the DoD amended its MLA regulation this year to significantly expand the definition of "consumer credit," thus subjecting a greater class of loan products to the MLA's requirements, and to enhance some of the protections. The amended MLA regulation became effective on October 1, 2015, with various delayed compliance deadlines.

The bill authorizes the OFR to enforce the MLA and the MLA regulations at the state level by authorizing the OFR to take administrative action against state financial institutions, deferred presentment providers (payday lenders), consumer finance lenders, and title lenders for violations of the MLA and the MLA regulations.

The bill has an indeterminate, yet positive impact to state revenues and a potentially negative impact on state expenditures. According to the OFR, enforcement provisions of the bill will require additional workload that is not currently being performed. The OFR indicates that the additional workload will require the need for two full-time equivalent positions with associated salary rate of \$87,016 and \$126,132 recurring funds from the Regulatory Trust Fund to implement provisions of the bill. The bill does not have a fiscal impact on local government. The bill exposes certain consumer lenders in this state to additional penalties and fines; however, it may have a positive impact on service members and their dependents who engage in consumer credit transactions in Florida.

The bill provides an effective date of October 3, 2016.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Current Situation

Consumer Debt and the Military

In 2006, Congress requested that the U.S. Department of Defense (DoD) conduct a study on the impact of predatory lending on the U.S. military.¹ The 2006 DoD report included: short-term loans (such as payday, auto title, and tax refund anticipation loans) and installment loans (such as unsecured loans targeting military personnel and rent-to-own loan products) in its findings on predatory lending practices. The DoD concluded that the report shared the following characteristics:

- Predatory lending practices targeted young, financially inexperienced borrowers with bank accounts and steady jobs, but with small savings, flawed credit, or high debt; in addition, predatory lenders did not consider the borrowers' ability to repay.
- Predatory lenders targeted military personnel through proximity (around military bases) or through the use of affinity marketing techniques, especially through the internet.
- Predatory loans typically involve high fees or interest rates which circumvent state and federal limits, and also result in "debt traps" through refinancing and loan flipping.²

The 2006 DoD report noted that predatory lending negatively impacts servicemembers and their families by undermining military readiness and morale, and adds to the cost of an all-volunteer fighting force.³ While the DoD noted its own efforts to educate, counsel, and assist servicemembers from predatory lending practices, it noted that it cannot prevent predatory lending without assistance from both state and federal legislatures and enforcement agencies. Specifically, the DoD opined that the most effective state protections combine strict usury limits and vigorous enforcement.⁴

The DoD made several recommendations to Congress, including a 36 percent federal ceiling on annual percentage rate (APR), uniform price disclosures, prohibitions on mandatory arbitration, and a prohibition on lenders from making loans to servicemembers that violate consumer protections laws of the state in which their base is located.⁵

Federal Military Lending Act of 2006

Following the DoD's report and recommendations, in 2006 Congress enacted the Military Lending Act (MLA) to provide protections to military personnel on active duty for more than 30 days, active National Guard or Reserve personnel, and their dependents from certain "consumer credit" products.⁶ The MLA protections, which are enforceable by various federal financial regulators,⁷ include:

- A 36 percent cap on military annual percentage rate, or MAPR (which includes interest, fees, credit service and renewal charges, credit insurance premiums, and other fees for credit-related products sold in connection with the loan);

¹ Section 579 of the National Defense Authorization Act (FY 2006).

² U.S. DEPARTMENT OF DEFENSE, *Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents* (Aug. 9, 2006), on file with the Insurance & Banking Subcommittee staff.

³ *Id.* at p. 53.

⁴ *Id.* at pp. 46-48.

⁵ *Id.* at pp. 50-52.

⁶ H.R. 5122, Section 670 of the John Warner National Defense Authorization Act of 2007; codified at 10 U.S.C. § 987. Covered dependents include the spouse, child in specified situations, parent or parent-in-law, and an unmarried person for whom the covered servicemember has legal custody. 10 U.S.C. § 987(i)(2); 10 U.S.C. § 1072(2).

⁷ In addition to providing civil remedies to aggrieved servicemembers and their dependents, the MLA is enforceable by the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the National Credit Union Administration, the CFPB, the Federal Trade Commission, and other specified agencies. 10 U.S.C. § 986(f)(6).

- Written and oral disclosures;
- A ban on rollovers and refinancing, unless the new loan results in more favorable terms for the borrower;
- A ban on mandatory waivers of consumer protection laws, including the Servicemembers Civil Relief Act (which protects servicemembers from being sued while on active duty), and a ban on mandatory arbitration; and
- A ban on prepayment penalties and mandatory allotments (i.e., automatic payroll deductions used to repay the loan).

The DoD's regulation implementing the MLA currently defines the types of loans subject to these protections as only:

- Closed-end payday loans up to \$2,000 and with a term of 91 days or fewer;
- Closed-end auto title loans with a term of 181 days or fewer; and
- Closed-end tax refund anticipation loans.

However, the current MLA regulation specifically excludes many other loan products from the definition of "consumer credit," including residential mortgages, home equity lines of credit, loans to finance the purchase or lease of motor vehicles, credit cards, overdraft loans, military installment loans, and all forms of open-end credit.⁸

2015 MLA Amendments

Following the enactment of the MLA, several organizations, including the DoD, acknowledged some of the shortcomings of the MLA, particularly its narrow definition of "consumer credit" that allowed lenders to structure their loan products to circumvent the MLA⁹:

- A 2012 report by the Consumer Federation of America found that while the MLA was largely successful in curbing abusive lending to the military, the narrow definition of "consumer credit," allowed loopholes for problematic credit products to be exploited, including bank credit products (similar to payday lending) that were excluded from the MLA regulation, resulting in uneven enforcement by state and federal regulators.¹⁰
- The Consumer Financial Protection Bureau (CFPB), created by Congress in 2010, began its supervision of payday lenders in 2012.
 - In 2013, the CFPB concluded that payday loans cannot be defined simply as closed-end loans where the principal and interest are due the next payday (generally, within two weeks to a month). Payday loans can be of longer duration, be structured as open-end credit, and incorporate installment payments.¹¹
 - The CFPB's first enforcement action against a payday lender also included findings that the lender overcharged servicemembers and their families, in violation of the MLA's 36 percent APR cap.¹²
 - In 2014, the Consumer Financial Protection Bureau (CFPB) issued a report on high-cost credit and the military, citing several examples illustrating how consumer credit products can be structured to fall outside the scope of the current MLA, such as contracting for payday loans greater than 91 days or auto loans greater than 181 days.¹³

⁸ 32 C.F.R. § 232.3(2).

⁹ Hanging Chen, *What Military Families Need to Know About High-Cost Lenders*, PROPUBLICA (Oct. 9, 2014), <http://www.propublica.org/article/what-military-families-need-to-know-about-high-cost-lenders>; Herb Weisbaum, *Military Lending Act 'Loopholes' Are Costing Troops Money*, NBCNEWS (Jan. 14, 2015), at <http://www.nbcnews.com/business/personal-finance/military-lending-act-loopholes-are-costing-troops-money-n282961>.

¹⁰ Jean Ann Fox, *The Military Lending Act Five Years Later*, CONSUMER FEDERATION OF AMERICA (May 29, 2012), <http://consumerfed.org/pdfs/Studies.MilitaryLendingAct.5.29.12.pdf>.

¹¹ CONSUMER FINANCIAL PROTECTION BUREAU, *Payday Loans and Deposit Advance Products* (Apr. 24, 2013), at http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

¹² CONSUMER FINANCIAL PROTECTION BUREAU, *Consent Order In the Matter of: Cash America International, Inc.* (Nov. 20, 2013), at http://files.consumerfinance.gov/f/201311_cfpb_cashamerica_consent-order.pdf.

- In 2013, Congress requested that the DoD determine whether the MLA regulation should be enhanced to protect covered borrowers from “continuing and evolving predatory lending practices.”¹⁴ In April 2014, the DoD issued a report noting significant concerns about the loopholes in state policy and marketplace changes that have blurred the differences between payday, auto title, and installment loans.¹⁵

In July 2015, the DoD amended the MLA regulation to broaden the coverage of MLA protections by expanding the definition of “consumer credit.” The new MLA regulation eliminates the “closed-end” qualifier of consumer credit, and the limitation that consumer credit means only payday loans, vehicle title loans, and tax refund anticipation loans of certain duration. Instead, the MLA regulation will mean any “credit offered or extended to a covered borrower primarily for personal, family, or household purposes, and that is (I) subject to a finance charge; or (II) payable by a written agreement in more than four installments.” The new MLA regulation still excludes residential mortgages and auto finance loans.¹⁶ However, this new definition is more consistent with credit that is subject to the federal Truth in Lending Act (TILA), although the MAPR requires inclusion of some fees or charges that are not considered finance charges under the TILA regulation, Reg Z.¹⁷

Additionally, the new MLA regulation permits creditors to use two methods to ascertain whether a consumer is a covered borrower for purposes of the regulation's protections. Under the final rule, creditors are granted a safe harbor if they use either or both of the two methods -- the MLA database (maintained by the DoD) or consumer reports from a nationwide consumer credit reporting agency -- to verify borrower status and comply with recordkeeping requirements. Creditors are allowed to rely on the initial covered borrower check for up to 60 days after a firm offer of credit is extended to the borrower.

The new MLA regulation became effective on October 1, 2015; however, compliance is required for consumer credit transactions that begin or are established on or after October 3, 2016. The regulation provides a limited delayed compliance deadline of October 3, 2017 for credit card accounts, which may be extended by the DoD until October 3, 2018.¹⁸

The DoD acknowledged that the amended MLA regulation will not entirely eliminate financial distress among servicemembers; however, the DoD expects that the new regulation should reduce negative credit reporting consequences to servicemembers, improve their capacity to manage and pay debts, and improve military readiness and servicemember retention (through reduced involuntary separations due to revoked security clearances).¹⁹

MLA and State Regulation of Consumer Credit

While the MLA generally does not preempt state law (except to the extent of any inconsistency, and allows states to provide additional protections to borrowers), the MLA does prohibit states from authorizing creditors to violate any state APR, interest cap, or other state consumer lending protections in relation to a borrower who is a servicemember or dependent.²⁰

¹³ CONSUMER FINANCIAL PROTECTION BUREAU, *The Extension of High-Cost Credit to Servicemembers and Their Families* (Dec. 2014), at: http://files.consumerfinance.gov/f/201412_cfpb_the-extension-of-high-cost-credit-to-servicemembers-and-their-families.pdf.

¹⁴ H.R. 4319, National Defense Authorization Act for FY 2013.

¹⁵ U.S. DEPARTMENT OF DEFENSE, *Report: Enhancement of Protections on Consumer Credit for Members of the Armed Forces and Their Dependents* (Apr. 2014), on file with the Insurance & Banking Subcommittee staff.

¹⁶ 32 C.F.R. § 232.3(f).

¹⁷ The purpose of TILA (which applies to all borrowers, not just servicemembers) is to promote the informed use of credit through “a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him.” TILA and Reg Z requires the calculation and disclosure of Annual Percentage Rate (APR) for all “consumer loans,” which include mortgage loans, home equity lines of credit, reverse mortgages, open-credit, certain student loans, and installment loans. 15 U.S.C. §§ 1601(a), 1604-1606. TILA is codified at 15 U.S.C. §1601 *et seq.*, as implemented by Reg Z, 12 C.F.R. pt. 226.

¹⁸ 32 C.F.R. § 232.13.

¹⁹ Limitation on Terms of Consumer Credit Extended to Service Members and Dependents: Final Rule, 80 Fed. Reg. 43,560, 43,599-43,600 (Jul. 22, 2015) (to be codified at 32 C.F.R. pt. 232).

²⁰ 10 U.S.C. § 987(d)(2).

Below is an overview of current Florida laws regulating consumer credit, applicable to all consumers in Florida, which are enforced by the Office of Financial Regulation (OFR). Currently, none of these laws specifically authorize the OFR to take administrative action for lending practices specifically against a servicemember or a servicemember's dependents.

Regulation of State Financial Institutions

The OFR's Division of Financial Institutions charters and regulates depository entities that engage in financial institution business in Florida in accordance with the Florida Financial Institutions Codes (Codes).²¹ State-chartered financial institutions include banks, trust companies, credit unions, international banking entities, capital stock associations, and savings banks.²² The OFR may examine, investigate, and take disciplinary actions against state-chartered financial institutions for violation of the codes, including the imposition of a *cease and desist order* pursuant to s. 655.033, F.S., an injunction pursuant to s. 655.034, F.S., removal of a financial institution-affiliated party pursuant to s. 655.037, F.S., and imposition of administrative fines pursuant to s. 655.041, F.S.

Regulation of State Non-Depository Lenders

In addition, the OFR's Division of Consumer Finance is responsible for the licensing and regulation of *non-depository* financial service entities and individuals, and conducts examinations and compliance investigations for licensed entities to determine compliance with Florida law. The OFR's Division of Consumer Finance has regulatory authority over other small consumer loans authorized under ch. 520 (retail installment sellers), ch. 537 (title loans), and part IV of ch. 560 (deferred presentment or payday loans), F.S.:

- Deferred Presentment Providers (Payday Lenders)

A "money services business" (MSB) is generally any person who acts as a payment instrument seller, foreign currency exchanger, check casher, or money transmitter. If an MSB is located in or does business in Florida, or into this state from outside of Florida or the U.S., the MSB must be licensed with the OFR pursuant to the Money Services Businesses Act (ch. 560, F.S.).²³

An MSB licensed under Part II or Part III of ch. 560, F.S., may also file a declaration of intent with the OFR to conduct business as a deferred presentment provider (also known as a payday lender) pursuant to Part IV of ch. 560, F.S. A deferred presentment transaction (or payday loan) is a type of loan where a person exchanges a check, like a paycheck, up to \$500 in exchange for currency or a payment instrument (e.g., electronic funds transfer, check, or money order) and the lender agrees to hold the check for a specified period of time before depositing or redeeming the check. Repayment terms range from a minimum of 7 days to a maximum of 31 days. The maximum allowable fees are 10 percent of the currency or payment instrument provided, as well as a verification fee of up to \$5 per transaction. For each transaction, the deferred presentment provider must comply with the disclosure requirements of Regulation Z. Borrowers may have only one active payday loan at a time, but may secure a new loan 24 hours after paying off the original loan.²⁴

- Consumer Finance Lenders

The Florida Consumer Finance Act (ch. 516, F.S.) sets forth licensing and loan contract requirements for consumer finance lenders in Florida. Ch. 516, F.S., sets forth maximum interest rates for *consumer finance loans*, which are loans of money, credit, goods, or a

²¹ chs. 655, 657, 658, 660, 663, 665, and 667, F.S.

²² The OFR does not regulate financial institutions chartered under federal law or under other states' laws. Regardless of charter type, every financial institution has a primary federal regulator (the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, or the Office of the Comptroller of the Currency).

²³ ss. 560.103(22) and 560.125(1), F.S.

²⁴ s. 560.404, F.S.

provision of a line of credit, in an amount or to a value of \$25,000 or less at an interest rate greater than 18 percent per annum.²⁵ Consumer finance loans may be secured or unsecured. The maximum allowable interest rates on consumer finance loans are tiered and capped based on a range of principal within each tier:

- 30 percent per year, computed on the first \$3,000 of the principal amount,
- 24 percent per year on that part of principal between \$3,001 and \$4,000, and
- 18 percent per year on that part of principal between \$4,001 and \$25,000.

These principal amounts are the same as the financed amounts determined by the Federal Truth-in-Lending Act (TILA), and Regulation Z (Reg Z) of the Board of Governors of the Federal Reserve System.²⁶ The maximum interest rates and finance charges under ch. 516, F.S., are computed on a simple-interest basis, and not a compounding or other basis. The APR for all loans under ch. 516, F.S., may equal, but cannot exceed, the APR for the loan as required to be computed and disclosed by TILA and Reg Z.²⁷ In addition to the applicable interest described above, consumer finance lenders may also charge borrowers certain charges and fees, such as a credit check up to \$25, a bad check charge of up to \$20, and any insurance premiums.²⁸

- **Title Lenders**

The Florida Title Loan Act (ch. 537, F.S.), sets forth licensing and loan contract requirements for title loan lenders in Florida. A title lender provides loans secured through transfer of a motor vehicle certificate of title, with the loan amount dependent on the vehicle's value. Title lenders charge tiered interest rates according to principal amount, similar to consumer finance loans under ch. 516, F.S. The maturity date of a title loan is 30 days after the agreement date, but the loan can be extended for one or more 30-day periods by mutual consent of the lender and the borrower.²⁹ Unlike consumer finance lenders, title lenders are prohibited from selling or charging for any type of insurance in connection with a title loan.³⁰

Effect of the Bill

The bill amends the following provisions to authorize the OFR to take administrative action (denial, suspension, revocation of licensure or registration, or imposition of fines) for a violation of the MLA or the MLA regulation:

- Section 516.07, F.S., relating to the OFR's administrative authority over consumer finance lenders,
- Section 537.013, F.S., relating to the OFR's administrative authority over title lenders, and
- Section 560.114, F.S., relating to the OFR's administrative authority over money services businesses in connection with a deferred presentment transaction.

The bill also creates s. 655.035, F.S., to authorize the OFR to investigate financial institution entities or any person for violations of the MLA or MLA regulations, and authorizes the OFR to initiate a proceeding under its cease and desist, injunctive, removal, or administrative fines authority in the Codes.

The bill provides that it applies to a consumer credit transaction or account for consumer credit established on or after October 3, 2016, except it does not apply to a credit card account exempted under 32 C.F.R. s. 232.13(c) until the exemption expires.

B. SECTION DIRECTORY:

Section 1. Amends s. 516.07, F.S., regarding grounds for denial of license or for disciplinary action.

²⁵ s. 516.01(2), F.S.

²⁶ s. 560.031(1), F.S.

²⁷ s. 560.031(2), F.S.

²⁸ s. 516.031(3), F.S.

²⁹ s. 537.011(3), F.S.

³⁰ s. 537.013(1)(h), F.S.

Section 2. Amends s. 537.013, F.S., relating to prohibited acts.

Section 3. Amends s. 560.114, F.S., relating to disciplinary actions; penalties.

Section 4. Creates s. 655.035, F.S., relating to military lending.

Section 5. Provides a statement of applicability.

Section 6. Provides an effective date of October 3, 2016.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

Indeterminate. The amount of fines that the OFR would collect through enforcement of the MLA as a result of provisions in the bill is unknown.

2. Expenditures:

According to the OFR's Division of Consumer Finance, enforcement provisions of the bill will require additional workload that is not currently being performed. The OFR indicates that the additional workload will require the need for two full-time equivalent positions with associated salary rate of \$87,016 and \$126,132 recurring funds from the Regulatory Trust Fund to implement provisions of the bill.³¹

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Indeterminate. The bill exposes certain consumer lenders in this state to additional penalties and fines. However, it may have a positive impact on servicemembers and their dependents who engage in consumer credit transactions in Florida.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to affect county or municipal governments.

³¹ Florida Office of Financial Regulation, Agency Analysis of 2016 House Bill 717, p. 4 (Nov. 30, 2015). The OFR is self-supporting in that all of its operating revenues are derived from its regulated individuals and entities. Currently, application fees and other regulatory fees and fines collected by the Division of Consumer Finance are deposited into the Regulatory Trust Fund. See ss. 516.03(1); 537.004(10); 560.1092, F.S.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None provided by the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On January 13, 2016, the Insurance & Banking Subcommittee considered and adopted one amendment and reported the bill favorably as a committee substitute. The amendment made the bill identical to its Senate companion, CS/SB 626, and clarified the OFR's administrative authority in the Codes over financial institution entities that violate the MLA or MLA regulations.

This analysis is drafted to the committee substitute as passed by the Insurance & Banking Subcommittee.