

Military Lending Act, Servicemembers Civil Relief Act, and State Military Law Updates

By Robert Savoie and Sarah Edwards*

INTRODUCTION

The federal and state laws governing the special benefits and protections afforded to servicemembers have been amended in various ways over the past couple of years. In 2020, the U.S. Department of Defense (“DoD”) revoked a portion of a prior interpretive rule under the Military Lending Act (“MLA”)¹ that created great controversy and reflected a position not subject to formal rulemaking with notice and comment. In 2018, Congress amended the Servicemembers Civil Relief Act (“SCRA”)² to create an optional safe harbor identification method for the 6 percent interest rate reduction benefit. In 2018 and 2019, some states also enacted entirely new laws providing benefits and protections to various categories of servicemembers or implemented amendments to existing laws providing such benefits and protections.

DEPARTMENT OF DEFENSE 2020 MLA Q&A AMENDMENTS

The MLA imposes disclosure obligations and structural product requirements upon certain loans extended to servicemembers and their dependents (“covered borrowers”).³ The regulations implementing the MLA were significantly modified and expanded in a final rule in 2015 (“2015 Final Rule”).⁴ In relevant part, the regulations confirmed an existing statutory exemption from the scope of the MLA for any credit transaction “that is expressly intended to finance the purchase of a motor vehicle when the credit is secured by the vehicle being purchased,” with a functionally identical exemption for the purchase of

* Robert Savoie and Sarah Edwards are consumer financial services regulatory compliance attorneys with McGlinchey Stafford PLLC, practicing at the firm’s Cleveland, Ohio, and New Orleans, Louisiana, offices, respectively.

1. Pub. L. No. 109-364, div. A, tit. VI, § 670(a), 120 Stat. 2083, 2266 (2006) (codified as amended at 10 U.S.C. § 987 (2018)).

2. Pub. L. No. 108-189, 117 Stat. 2835 (2003) (codified as amended at 50 U.S.C. §§ 3901– 4043 (2018)).

3. 10 U.S.C. § 987.

4. Limitations on Terms of Consumer Credit Extended to Service Members and Dependents, 80 Fed. Reg. 43559 (July 22, 2015) [hereinafter 2015 Final Rule].

other personal property as well.⁵ The DoD subsequently issued two interpretive rules for the stated reason of “assisting industry in complying with the July 2015 Final Rule” in a question and answer format.⁶

In its second interpretive rule issued in 2017 (“Second Interpretive Rule”), the DoD addressed whether the financing of ancillary products offered in connection with the purchase of motor vehicles or personal property would cause a purchase money transaction to lose its status as an MLA-exempt transaction.⁷ In its explanation, the DoD sought to make a distinction between the types of additional products and services that could be financed along with the purchase of personal property or motor vehicles without causing the transaction to become subject to the MLA, and those that may not.⁸ The DoD expressed the view that a purchase money transaction would remain MLA-exempt if the financing also included financing for optional leather seats and an extended warranty for service of the motor vehicle, or the installation of a purchased appliance with the purchase price of the appliance itself, because the DoD felt those products were “expressly related to that object.”⁹ The DoD similarly stated that a trade-in of a motor vehicle in connection with the purchase of a new motor vehicle, where that trade-in resulted in negative equity due to a greater amount owed on prior financing than the trade-in value, similarly should not render the transaction subject to the MLA because the trade-in of the motor vehicle was also inherently related to the purchase of the new motor vehicle.¹⁰ In contrast, the DoD determined that the financing of a “credit-related product or service” was not expressly related to the motor vehicle or personal property, and thus would render an otherwise exempt transaction subject to the MLA.¹¹ Examples of such products included “Guaranteed Auto Protection (‘GAP’) insurance or a credit insurance premium.”¹²

This element of the Second Interpretive Rule was controversial for two reasons. First, the DoD took the position that its interpretation was not subject to notice and comment requirements because it classified the interpretation as one that did not establish a new position, but rather one that “merely states the Department’s preexisting interpretations of an existing regulation,” thereby avoiding the need to formally solicit feedback on its position prior to publishing the Second Interpretive Rule.¹³ The DoD took this position despite the fact that there was no language reflecting this position in the 2015 Final Rule.

5. 32 C.F.R. § 232.3(f)(2)(ii), (iii) (2020).

6. Military Lending Act Limitations on Terms of Consumer Credit Extended to Service Members and Dependents, 81 Fed. Reg. 58840 (Aug. 26, 2016); Military Lending Act Limitations on Terms of Consumer Credit Extended to Service Members and Dependents, 82 Fed. Reg. 58739 (Dec. 14, 2017) [hereinafter Second Interpretive Rule].

7. Second Interpretive Rule, *supra* note 6, at 58740.

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.* at 58739.

Second, the practical impact of this aspect of the Second Interpretive Rule was that many auto dealers and auto lenders began to decline to provide products and services to military members because they feared that selling them would forfeit the exemption from the MLA's requirements.¹⁴ One example of a product impacted by the Second Interpretive Rule includes products designed to eliminate any amounts owed by a servicemember in the event of a total loss of the motor vehicle when the insurance payout was insufficient to pay off the financing, and without those products, some servicemembers owed thousands of dollars for cars that had been destroyed in accidents.¹⁵ While the DoD asserted that the Second Interpretive Rule was merely a clarification of existing law, the 2015 Final Rule did not assert or address this potential interpretation, nor did it analyze the potential impact of an effective ban on such products. Due to the criticism and controversy associated with this interpretation, the DoD issued an amendment to the Second Interpretive Rule in February 2020 to address uncertainty relating to the treatment of ancillary products under the MLA ("2020 Interpretive Rule").¹⁶ In the 2020 Interpretive Rule, the DoD expressly struck the controversial language from the Second Interpretive Rule and removed all reference to the interpretation of the purchase money exemptions for the purchase of motor vehicles and personal property.¹⁷ The DoD simply noted that after receiving feedback and comments on the Second Interpretive Rule, it agreed that additional analysis was necessary.¹⁸ The result of the 2020 Interpretive Rule is that there are no longer any interpretations indicating that the products described by the DoD as credit-related would cause an otherwise exempt transaction to become subject to the MLA.¹⁹

SCRA SAFE HARBOR FOR INTEREST RATE REDUCTIONS

The SCRA includes a wide range of protections and benefits for servicemembers. One of those protections is a provision that allows servicemembers to request that the rate of interest on any obligation or liability be limited to no more than 6 percent per year for the duration of their military service and one year thereafter for certain real estate secured obligations, as long as the obligation was incurred prior to the entry into military service.²⁰ The default mechanism through which a servicemember obtains this benefit is by submission of both a written notice requesting the rate reduction and a copy of military orders or other appropriate indicator of military service.²¹

14. See Hannah Lutz, *A Tussle Over GAP for Military Members*, AUTO. NEWS (Mar. 4, 2019), <https://www.autonews.com/dealers/tussle-over-gap-military-members>.

15. *Id.*

16. Military Lending Act Limitations on Terms of Consumer Credit Extended to Service Members and Dependents, 85 Fed. Reg. 11842 (Feb. 28, 2020).

17. *Id.* at 11843.

18. *Id.*

19. *Id.*

20. 50 U.S.C. § 3937(a)(1) (2018).

21. *Id.* § 3937(b)(1)(A).

In August 2018, the SCRA was amended to create an alternative identification method whereby a creditor may voluntarily opt to conduct a review of its accounts to identify eligible servicemembers and proactively extend the rate reduction without requiring notification by the servicemember.²² Under this voluntary approach, the creditor may rely upon information retrieved from the Defense Manpower Data Center (“DMDC”) in determining whether a borrower is a servicemember eligible for the rate reduction.²³ The benefit to the creditor is that, by utilizing this optional identification method, it is granted a safe harbor from potential liability for failure to grant the interest rate reduction as long as the DMDC data reflects that the borrower is not on military duty and the creditor has not received written notice from the servicemember.²⁴

Creditors have to evaluate the additional costs imposed by utilizing the safe harbor provision. Use of the safe harbor identification method requires periodic monitoring and utilization of DMDC certificates to be effective, in contrast to the traditional written notice method, which simply requires the creditor to react upon receipt of sufficient written documentation.²⁵ In the authors’ experience, however, some creditors adopted proactive monitoring prior to enactment of the safe harbor, and thus do not need to make any modifications to their business practices in order to benefit from the liability protection.

STATE BENEFITS AND PROTECTIONS TO SERVICEMEMBERS

There have also been several developments with respect to state laws providing benefits and protections similar to those provided under the federal SCRA. These developments continue a trend of states extending benefits similar to the SCRA to additional categories of servicemembers and also creating new types of benefits and protections. North Carolina and South Carolina enacted state servicemember protections for the first time, while California significantly amended its servicemember protections.

NORTH CAROLINA SERVICEMEMBERS CIVIL RELIEF ACT

Effective in October 2019, the North Carolina Servicemembers Civil Relief Act (“NC-SCRA”) incorporated into state law the rights, benefits, and protections of the SCRA.²⁶ The NC-SCRA also expressly extended those rights, benefits, and protections to members of the North Carolina National Guard serving on state active duty and to members of the National Guard of other states serving on state active duty who reside in North Carolina, individuals who otherwise would not be eligible for the benefits and protections of the SCRA.²⁷ Dependents

22. *Id.* § 3937(b)(1)(B).

23. *Id.* § 3937(b)(1)(B)(i).

24. *Id.* § 3937(b)(1)(B)(ii).

25. *Id.* § 3937(b).

26. N.C. GEN. STAT. §§ 127B-25–127B-36 (2020). The NC-SCRA applies to contracts entered into, renewed, or modified after October 1, 2019.

27. *Id.* § 127B-27(4)(b).

of covered servicemembers were also automatically granted rights regarding the termination of certain contracts under the NC-SCRA, in contrast to the federal SCRA's requirement that dependents apply to a court to receive protection, in addition to the rights granted to dependents under Subchapter III of the federal statute.²⁸ Subchapter III of the SCRA provides important protections against evictions and termination of residential or motor vehicle leases, among others.²⁹ The version of the NC-SCRA originally enacted effective on October 1, 2019, stated that dependents would be afforded the protections provided under Subchapter II of the SCRA.³⁰ However, the North Carolina legislature made a corrective amendment to the state's dependent protections in November 2019 to reference Subchapter III of the federal law.³¹ This amendment is retroactively effective to the October 1, 2019, effective date.³²

The NC-SCRA contains a number of other additional rights, benefits, and protections beyond those granted under federal law. For example, covered individuals under the NC-SCRA are granted expanded protections with respect to cancellation of consumer service contracts if the servicemember receives a military order to relocate for a period of military service of at least ninety days to a location that does not support the contract, e.g., if the covered individual relocates to place where his or her internet service provider does not provide coverage.³³ This expanded list of covered service contracts includes internet and television contracts.³⁴ The NC-SCRA also allows for enforcement by both the state attorney general and private individuals.³⁵ In an action by the attorney general, a court may assess a civil penalty of \$5,000 for each violation of the NC-SCRA, in addition to other remedies.³⁶ Remedies under the private right of action include restitution, an award of damages, and recovery of attorneys' fees and court costs.³⁷

SOUTH CAROLINA SERVICEMEMBERS CIVIL RELIEF ACT

Effective in April 2019, the South Carolina Servicemembers Civil Relief Act ("SC-SCRA") was enacted using language that matched the original enactment of the NC-SCRA and that similarly expanded and supplemented the rights, benefits, and protections of the SCRA.³⁸ Like the NC-SCRA, the SC-SCRA broadens the definition of a covered servicemember to include members of the South

28. Compare *id.* § 127B-29, with 50 U.S.C. § 3959 (2018).

29. 50 U.S.C. §§ 3951–3959 (2018).

30. See S.B. 420, 2019 Gen. Assemb., 1st Sess. (N.C. 2019) (to be codified at N.C. GEN. STAT. §§ 127B-25–127B-36).

31. See H.B. 470, 2019 Gen. Assemb., 1st Sess. (N.C. 2019) (to be codified at N.C. GEN. STAT. § 127B-29(a)).

32. *Id.*

33. N.C. GEN. STAT. § 127B-30 (2020).

34. *Id.* § 127B-30(c).

35. *Id.* §§ 127B-35, 127B-36.

36. *Id.* § 127B-35(b), (c).

37. *Id.* § 127B-36(b), (c).

38. S.C. CODE §§ 25-1-4010–25-1-4080 (2020).

Carolina National Guard called to active duty under South Carolina law for a period of more than thirty days.³⁹

The SC-SCRA also provides automatic rights, benefits, and protections for dependents of covered servicemembers.⁴⁰ However, protections for dependents under the SC-SCRA are different from those granted under the NC-SCRA because the material post-enactment corrective amendments to the NC-SCRA amending the reference to Subchapter II of the federal law to Subchapter III were not made in South Carolina.⁴¹ Due to the fact that similar post-enactment amendments were not made to the SC-SCRA, the South Carolina law provides that a dependent of a servicemember engaged in military service has the same rights and protections provided to a servicemember pursuant to the SC-SCRA and Subchapter II of the federal SCRA.⁴² As a result, certain dependents under the SC-SCRA may not receive the benefits of Subchapter III, such as residential eviction protections. Subchapter II of the federal SCRA contains general relief provisions for servicemembers which include protections from default judgments and the 6 percent interest rate reduction provision, discussed in the safe harbor section above.⁴³

Like the NC-SCRA, the SC-SCRA provides covered individuals with the option to terminate certain contracts upon receipt of military orders to relocate for a period of service of at least ninety days to a location that does not support the contract.⁴⁴ Covered contracts in the SC-SCRA include athletic club or gym memberships and satellite radio services, a definition that is more expansive than the federal provision.⁴⁵ The SC-SCRA also provides for enforcement through a private right of action or through a civil action by the South Carolina attorney general.⁴⁶ However, unlike the NC-SCRA, the South Carolina statutes do not provide for the collection of attorney's fees or court costs.⁴⁷

CALIFORNIA AMENDS ITS MILITARY PROTECTIONS

California substantially amended its Military and Veterans Code to provide a number of expanded benefits to covered servicemembers, effective in January 2019.⁴⁸ Significant amendments include changes to the scope of California's interest rate reduction provisions, expansion of repossession and lease termination protections, as well as loosened documentation requirements for deferral benefits.

39. *Id.* §§ 25-1-4030(c), 25-1-4050. Note that servicemembers on state active duty are obligated to provide a written or electronic copy of the order to military service to trigger the remedies or penalties of the SC-SCRA. *Id.* § 25-1-4040.

40. *Id.* § 25-1-4050.

41. See H.B. 470, 2019 Gen. Assemb., 1st Sess. (N.C. 2019).

42. S.C. CODE § 25-1-4050.

43. See 50 U.S.C. §§ 3931–3938a (2018).

44. S.C. CODE § 25-1-4060 (2020).

45. Compare *id.* § 25-1-4060(B), with 50 U.S.C. § 3956(b) (2018).

46. S.C. CODE § 25-1-4070(a) (2020).

47. See *id.* § 25-1-4070.

48. See CAL. MIL. & VET. CODE §§ 400–409.15, 800–830 (2020).

The 2019 amendments to California's Military and Veterans Code expand the federal interest rate reduction provisions in a few ways. First, the amendments extend the period of interest rate protections for non-mortgage loans. For student loans, the period of interest rate protection was extended to the one-year period after military service ends.⁴⁹ For other non-mortgage loans, the 6 percent interest rate reduction benefit extends to 120 days after the period of military service.⁵⁰ Prior to the 2019 amendments, the California interest rate protections mirrored the federal SCRA, meaning benefits did not extend past the period of military service for these types of loans.⁵¹ Second, the interest rate amendments require a person who receives an incomplete or insufficient request for interest rate protections from a servicemember to provide the servicemember with a written response.⁵² A written response is also required if such person believes that the servicemember is not entitled to the relief requested.⁵³ Prior to January 1, 2019, there was no written response requirement.

The California amendments also enlarge repossession and lease termination protections. Existing California law prohibited repossession without a court order for nonpayment or any other contract breach occurring prior to or during the period of military service, when the servicemember entered military service after paying a deposit or installment on a purchase contract. The protection now extends to 120 days after the period of military service.⁵⁴ California's lease termination protection provisions were also expanded to cover motor vehicles and mirror federal SCRA law protections for covered servicemembers who enter military service during the term of the lease.⁵⁵ California law allows covered servicemembers who terminate a vehicle lease to pay the arrearage and other obligations due at the time of termination in equal installments over a period equal to at least the period of military service.⁵⁶

Finally, the California amendments relaxed documentation requirements for reservists seeking to defer payments on certain obligations, including mortgage loans, credit card obligations, and retail contracts while serving on active duty. Prior law required a letter signed by the reservist under penalty of perjury requesting a deferral along with a copy of the reservist's military orders or other evidence of military service.⁵⁷ The law now requires only a request for a deferral instead of a letter signed under penalty of perjury.⁵⁸

49. *Id.* § 405(a)(1).

50. *Id.* § 405(a)(2).

51. CAL. MIL. & VET. CODE § 405 (2018).

52. CAL. MIL. & VET. CODE § 830 (2020).

53. *Id.*

54. *See id.* § 407.

55. *Id.* § 409.

56. *Id.* § 826(a).

57. CAL. MIL. & VET. CODE § 800(b) (2018).

58. CAL. MIL. & VET. CODE § 800(b) (2020).

