No. 21-1697

IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

JERRY DAVIDSON, individually, and on behalf of all others similarly situated,

Plaintiff–Appellant,

v.

UNITED AUTO CREDIT CORPORATION, a California corporation,

Defendant–Appellee.

On Appeal from the United States District Court
for the Eastern District of Virginia

BRIEF FOR THE UNITED STATES OF AMERICA AS AMICUS CURIAE SUPPORTING APPELLANT

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INTRODUCTION AND STATEMENT OF INTEREST

Congress enacted the Military Lending Act (MLA) to enhance the consumer protections available to active-duty servicemembers and their dependents as they procure loan products. *See* John Warner National Defense Authorization Act for Fiscal Year 2007, Pub. L. No. 109-364, § 670(a), 120 Stat. 2083, 2266–69 (2006) (codified at 10 U.S.C. § 987). The MLA applies to all "consumer credit," 10 U.S.C. § 987(i)(6), which includes most loans, *see* 32 C.F.R. § 232.3(f)(1). But the statute's definition of "consumer credit" contains an exception for "a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured." 10 U.S.C. § 987(i)(6).

The district court incorrectly concluded that the loan in this case satisfied the MLA's exception for car loans. The loan here is a "hybrid" loan: it financed both an exempt product (a car) and a distinct non-exempt product (an optional financial product). The particular financial product at issue—guaranteed auto (or asset) protection (GAP coverage)—is not needed to buy a car and does not advance the purchase or use of the car. Lenders cannot invoke the statute's specific car-loan exception and bypass its consumer protections when they choose to bundle standalone financial products into a loan. Hybrid loans that include financing for GAP coverage do not satisfy the car-loan exception to consumer credit.

The United States has an interest in the proper interpretation of the MLA, which protects the Nation's servicemembers and their families. Additionally, the statute charges the U.S. Department of Defense with administering the regulatory scheme and authorizes the Secretary of Defense to issue regulations, including those defining consumer credit. 10 U.S.C. § 987(h)(1), (h)(2)(D). Numerous federal agencies—including the Federal Trade Commission (FTC), Board of Governors of the Federal Reserve System (FRB), Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, Consumer Financial Protection Bureau (CFPB), National Credit Union Administration, and U.S. Department of the Treasury—consult on the development of those regulations. *Id.* § 987(h)(3). The statute confers enforcement authority on several agencies, including the FTC and CFPB. *Id.* § 987(f)(6) (incorporating enforcement provisions of the Truth in Lending Act, 15 U.S.C. § 1607).

The Department of Defense has indicated that it is in the process of conducting "additional analysis" on GAP coverage and other financial products, *see* 85 Fed. Reg. 11,842, 11,843 (Feb. 28, 2020), which it anticipates will result in it issuing additional guidance following the appropriate multiagency process. The Defense Department strongly concurs with the position in this amicus brief.

The district court's decision misunderstands the statute's limited car-loan exception, while threatening the consumer protections that Congress afforded

servicemembers and the regulatory scheme that the government oversees. This Court should vacate that decision.

STATEMENT OF THE CASE

A. Military Lending Act

1. Servicemember protections for "consumer credit"

Enacted in 2006, the Military Lending Act protects active-duty servicemembers and their dependents as they procure "consumer credit" loan products. *See* 10 U.S.C. § 987. Congress passed the statute in response to a Department of Defense report 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." U.S. Dep't of Def., *Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents* 9 (2006), https://go.usa.gov/xtrJH (2006 Report). As the report found, "predatory loan practices and unsafe credit products are prevalent and targeted at military personnel through proximity and concentration around military installations." *Id.* at 45. Lenders often pushed loans with 300% or 400% annual percentage rates, which (among other consequences) led to servicemembers forfeiting their car titles and "losing essential transportation and key family assets." *Id.* at 16, 45.

Congress recognized that "military personnel and their families [had been] particularly attractive targets," because they were "often young and financially inexperienced." *A Review of the Department of Defense's Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents: Hearing Before the S. Comm. on Banking, Hous. & Urban Aff.*, 109th Cong. 1 (2006) (statement of Sen. Richard C. Shelby). Their situations could be especially precarious because defaulting on a loan could result in "military sanctions, including the loss of security clearance," *id.*, and indeed, "[f]inancial issues [had] account[ed] for 80 percent of security clearance revocations and denials for Navy personnel," 2006 Report 45.

In regulating "consumer credit," the MLA caps interest rates, requires lenders to disclose an interest rate that accounts for all fees and charges, and sets other restrictions on loan terms. *See* 10 U.S.C. § 987(b), (c), (e), (i)(4). The Secretary of Defense may, in consultation with other agencies, issue regulations further implementing the statute. *Id.* § 987(h).

The MLA provides that loans that violate its provisions are "void from the[ir] inception." 10 U.S.C. § 987(f)(3). The statute also creates a private right to sue the lender for any violations, and the lender is liable unless it had maintained reasonable procedures to prevent those violations. *See id.* § 987(f)(5). The statute confers enforcement authority on several federal agencies, including the FTC and CFPB. *See id.* § 987(f)(6) (incorporating enforcement provisions of the Truth in Lending

Act, 15 U.S.C. § 1607). And the U.S. Department of Justice may prosecute any knowing violation of the statute as a misdemeanor. *Id.* § 987(f)(1).

2. Definition of "consumer credit" and treatment of cars and other personal property

The MLA's protections reach only those loan products that qualify as "consumer credit" in the first place, as defined in Defense Department regulations. *See* 10 U.S.C. § 987(i)(6) (giving "'consumer credit' … the meaning provided for such term in regulations prescribed under this section"); *see also id.* § 987(h)(2)(D) (rulemaking authority to define "consumer credit"). The term "consumer credit" encompasses any loan product offered "primarily for personal, family, or household purposes" and that either includes "a finance charge" (such as interest or financing fees) or is contractually payable in more than four installments. 32 C.F.R. § 232.3(f)(1); *see id.* § 232.3(n) (defining "finance charge").

Relevant here, Congress crafted an exception for loans specifically intended to finance the purchase of cars or other personal items. The MLA provides that the term "consumer credit" does not include "a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured." 10 U.S.C. § 987(i)(6). The Department's regulations adopt that statutory exception for car and personal-property loans in materially identical terms. *See* 32 C.F.R. § 232.3(f)(2)(ii), (iii).

Whether a loan is consumer credit has consequences for car ownership as well. If a loan is consumer credit, lenders cannot use "the title of a vehicle as security for the obligation." 10 U.S.C. § 987(e)(5); *see* 32 C.F.R. § 232.8(f). That car-title restriction stems from the Defense Department's findings that "[o]utlets loaning money secured by car titles are heavily concentrated around some bases" and that such loans "can result in repossession of the vehicle." 2006 Report 16–17. If a loan falls within the car-loan exception to consumer credit, however, then that restriction and the other statutory limitations do not apply. *See* 10 U.S.C. § 987(i)(6).

In 2016, the Secretary issued an interpretive rule addressing questions about the statutory exception for car and personal-property loans, specifically as applied to personal property. *See* 81 Fed. Reg. 58,840 (Aug. 26, 2016) (2016 Guidance). That 2016 Guidance addressed "hybrid" loans that finance purchases of exempt products (such as personal property) and distinct non-exempt products (such as cash advances). *Id.* at 58,841. Those hybrid loans would be offered "for the purpose of purchasing personal property" and "simultaneously [be for] an amount greater than the purchase price" of the personal property. *Id.*

The 2016 Guidance made clear that, under the personal-property "exception from the definition of consumer credit, a loan must finance *only* the acquisition of personal property." 81 Fed. Reg. at 58,841. For instance, a hybrid loan for purchas-

ing personal property and a cash advance would not be "expressly intended to finance the purchase of personal property, because the loan provides additional financing that is unrelated to the purchase." *Id.* Thus, a loan that provides "secured financing of personal property" plus a financial product such as "additional 'cash-out' financing is not eligible for the exception." *Id.*

B. Guaranteed Auto Protection Coverage

1. GAP coverage is a debt-related product that addresses a financial contingency arising from a total loss of the car. *See* CFPB, *Supervisory Highlights: Issue 19, Summer 2019*, at 3 (Sept. 2019), https://go.usa.gov/xe6xW (CFPB Highlights); Patrick Brick & Patrick Campbell, *Servicemembers, Arm Yourself with Basic Car Buying Skills—Stand Your Guard When It Comes to Add-On Products*, CFPB Blog (Dec. 10, 2018), https://go.usa.gov/xeMew (CFPB Add-Ons).

When a car is totaled in a crash or stolen, a standard auto insurance policy will generally pay for the actual, present value of the car. *See* CFPB Highlights 3. The insurance payout, however, may be lower than the remaining balance on the car owner's loan (or, for a car being leased, the lease payoff), depending on the size of the loan and how much has been paid to date. *Id.*; *see* FRB, *Gap Coverage* (May 5, 2003), https://go.usa.gov/xept4 (FRB Gap Coverage) ("The gap amount exists because your vehicle usually depreciates faster at the beginning of the loan than as you pay down your loan balance."). In that situation, the owner may not have

enough cash to pay off the outstanding debt. GAP coverage covers the financial "gap" between the actual car value and the remaining loan balance in this particular contingency. *See* CFPB Highlights 3. It does not repair or replace the car.

Lenders sometimes offer GAP coverage in financing the purchase of a car. *See* CFPB, *What Is Guaranteed Auto Protection (GAP) Insurance?* (June 8, 2016), https://go.usa.gov/xeUJu (CFPB GAP Insurance). But it would be "highly unusual for a lender to *require* that you buy GAP insurance." *Id.* (emphasis added). GAP coverage "is usually not included in finance agreements" without being specifically added; rather, the borrower "may be able to buy it separately" or add it for "a one-time charge, or premium." FRB Gap Coverage. There can be upsides to obtaining coverage separately. When GAP coverage is not bought on its own but is bundled with the car and financed as an "add-on product," it results in "not just the upfront cost but also the cost of the interest when [the borrower] pay[s] for this product over the life of the loan." CFPB GAP Insurance; *see* CFPB Add-Ons.

When GAP coverage is offered with a loan that finances a car purchase, it is often at a marked-up price. *See* Nat'l Consumer Law Ctr., *Auto Add-Ons Add Up: How Dealer Discretion Drives Excessive, Arbitrary, and Discriminatory Pricing* 10 (Oct. 2017), https://perma.cc/THR2-KWKY (NCLC Report) (finding that, for "GAP products" and other ancillary products, "the combined average markup was 170%"). GAP coverage can thus unduly increase a consumer's total costs. *Id.* at 1, 3 (finding

financing costs and optional products like GAP coverage to be the "largest source of dealer profit"). Rather than buy coverage along with the car, consumers "can purchase GAP from different sources," including their auto-insurance provider, often for lower costs. CFPB Add-Ons.

Because a financial gap is more likely when the car loan is greater in relation to the car value, moreover, GAP coverage is also not valuable for many owners. *See* CFPB Highlights 3. In loans with "a low [loan-to-value ratio], the insurance payout for a totaled vehicle may cover the outstanding debt." *Id.* But as the CFPB observed, lenders have at times "sold a GAP product to consumers whose low [loan-to-value ratio] meant that they would not benefit from the product." *Id.*

2. The Defense Department has issued an interpretive rule specifically interpreting the MLA's treatment of GAP insurance, though that rule is no longer in effect. In 2017, the Department announced that, just as a hybrid loan for personal property and a cash advance would be consumer credit "under the statute and would not satisfy the exception for car and personal-property loans, a car loan that "includes financing for Guaranteed Auto Protection … would not qualify for the exception." 82 Fed. Reg. 58,739, 58,740 (Dec. 14, 2017) (2017 Guidance).

In 2020, the Department withdrew that portion of the 2017 Guidance to conduct "additional analysis" on "technical issues" that lenders had raised. 85 Fed.

Reg. at 11,843. The Department, however, did not withdraw its prior 2016 Guidance on hybrid loans, which confirmed that a loan with "additional financing that is unrelated to the purchase" of an exempt product such as personal property remains consumer credit. 81 Fed. Reg. at 58,841. And the Department made clear that it "takes no position on any of the arguments or assertions advanced as a basis for withdrawing" the 2017 Guidance. 85 Fed. Reg. at 11,843.

C. Factual and Procedural Background

Plaintiff Jerry Davidson brought this putative class action asserting various MLA violations against defendant United Auto Credit Corporation, which is allegedly a subprime lender. JA13. In 2018, plaintiff as an active-duty servicemember bought a used GMC Arcadia on a loan from defendant. JA20. The loan financed not only the purchase of the car for around $14,000 (after a down payment) but also the purchase of GAP coverage for $395, in addition to a processing fee and prepaid interest. JA20–21; *see* JA41 (Loan Agreement). Under the loan's terms, the entire amount was subject to interest and secured by plaintiff's car. JA42.

In May 2021, the district court entered judgment against plaintiff, dismissing his complaint. JA57. The court in its decision concluded that plaintiff's loan was not consumer credit under the MLA because it fell within the car-loan exception. JA51–55. Though GAP coverage is offered as a standalone financial product,

the court opined that it was "inextricably tied to plaintiff's purchase of the vehicle." JA55. The court indicated that "GAP coverage provides a form of insurance directly related to the motor vehicle and protects the purchaser in the event of theft or damage to the Vehicle that results in a total loss." JA55 (quotation omitted). The court similarly concluded that the processing fee and prepaid interest were "directly related" to the car purchase. JA55.

The district court refused to consult the Defense Department's 2016 Guidance on hybrid loans because it concluded that the 2016 Guidance "only applied to personal property and did not address motor vehicles," even though the statutory text of the exception for cars and personal-property loans (as addressed in that guidance) is the same. JA55; *see* 10 U.S.C. § 987(i)(6). The court also found significant that, though the Department "stated that it 'takes no position on any of the arguments or assertions advanced for withdrawing' the 2017 [Guidance]" on GAP coverage, "adopting plaintiff's position would essentially contradict the [Department's] withdrawal of the guidance by effectively reinstating it." JA55 (quoting 85 Fed. Reg. at 11,843). The court recognized, however, that the Department could issue guidance resulting in "the [loan] being governed by the MLA." JA54.

SUMMARY OF ARGUMENT

The Military Lending Act protects vulnerable servicemembers and their dependents as they procure "consumer credit" products. The statute and regulations define "consumer credit" to include most loans, *see* 32 C.F.R. § 232.3(f)(1), but the term does not encompass "a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured," 10 U.S.C. § 987(i)(6). The MLA's car-loan exception is not satisfied, however, by a hybrid loan—that is, a loan that finances a product bundle including both an exempt product (such as a car) and a distinct non-exempt product (such as optional GAP coverage). Such hybrid loans that bundle together standalone financial products like GAP coverage remain consumer credit subject to the statute's protections for servicemembers.

The MLA's car-loan exception applies only to loans for "the purchase" of "a car," and not bundles of disparate products. 10 U.S.C. § 987(i)(6). The exception further provides that the loan must be for "the express purpose" of that purchase, underscoring that it must be for the specific purpose of buying a car, and not for some distinct, unrelated purpose. *Id.* As the Department of Defense confirmed in its 2016 Guidance, hybrid loans that finance standalone financial products like cash advances fall outside the exception. *See* 81 Fed. Reg. at 58,841.

Just as a lender could not bypass the MLA's servicemember protections by bundling a standalone financial product such as a cash advance with a car loan, the same goes for GAP coverage. GAP coverage is a financial product, not a car product. It might help the owner pay off the loan when the car is totaled, but it does not help protect the car and does not further the purchase or use of the car. GAP coverage is thus distinct from and not appreciably related to the car being bought. And when a lender chooses to include financing for GAP coverage, that loan falls outside the statutory exception. This does not mean that lenders cannot offer hybrid loans, or a specific loan that finances GAP coverage; it just means that lenders must follow the statute's protections in doing so.

The district court erred in concluding that GAP coverage was so closely related to the car that a hybrid loan financing both items satisfied the MLA's car-loan exception. Rather than being meaningfully related to the car, GAP coverage can be bought "separately" for "a one-time charge, or premium," FRB Gap Coverage, and it would be "highly unusual for a lender to require that you buy GAP insurance," CFPB GAP Insurance. In misunderstanding the nature of GAP coverage, the court further erred in ignoring the Department's 2016 Guidance on hybrid loans that finance standalone financial products. This Court should vacate the decision below.

ARGUMENT

THE MILITARY LENDING ACT'S DEFINITION OF "CONSUMER CREDIT" INCLUDES HYBRID LOANS THAT FINANCE BOTH A CAR AND OPTIONAL GAP COVERAGE

The MLA affords significant consumer protections to servicemembers and their families as they procure "consumer credit" products, protecting them against predatory lending practices. The definition of "consumer credit" does not include "a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured." 10 U.S.C. § 987(i)(6). That exception is not satisfied by a hybrid loan that finances optional GAP coverage, however, and the district court erred in holding otherwise.

A. Hybrid Loans that Finance Optional GAP Coverage Do Not Satisfy the Statutory Exception to Consumer Credit

1. The statutory text, structure, and purpose indicate that hybrid loans are consumer credit

The traditional tools of statutory interpretation lead to the conclusion that a hybrid loan that finances a standalone financial product, as here, is consumer credit under the MLA. This Court interprets the statute's text based on its ordinary meaning, "with reference to the statutory context, structure, history, and purpose." *Abramski v. United States*, 573 U.S. 169, 179 (2014) (quotation omitted); *see United States v. Serafini*, 826 F.3d 146, 149 (4th Cir. 2016). The Court provides the statute's exceptions "a fair reading" but considers "textual indication[s] that its

exemptions should be construed narrowly." *Encino Motorcars, LLC v. Navarro*, 138 S. Ct. 1134, 1142 (2018) (quotation omitted).

a. The MLA's exception to the definition of consumer credit applies only to a loan "offered for the express purpose of financing the purchase," referring in particular to the servicemember's "purchas[e] [of] a car or other personal property." 10 U.S.C. § 987(i)(6). In designating cars and personal property as exempt products, Congress purposefully identified a limited category of transactions that can be financed without triggering the statute's consumer protections.

Common parlance, however, confirms that the purchase of a bundle of disparate products is not the same as "the purchase" of a specific product such as "a car or other personal property." *See Mohamad v. Palestinian Auth.*, 566 U.S. 449, 454 (2012) (consulting "everyday parlance"). Consumers make this distinction daily. A purchase of fries and a soda along with a burger is no longer the purchase of "a burger" in particular but the purchase of "a combo meal." A purchase of a hotel room and a rental car along with a plane ticket is no longer the purchase of "a plane ticket" in particular but the purchase of "a travel package."

Indeed, if Congress had intended for the exception to reach more broadly, it could have easily drafted that exception to include loans offered for a purchase *involving* a car or personal property, rather than loans offered for "purchasing a car or other personal property" specifically. 10 U.S.C. § 987(i)(6). That textual change

would have been straightforward. And if Congress wanted the exception "to have such an effect, it knew how to say so." *Rubin v. Islamic Republic of Iran*, 138 S. Ct. 816, 826 (2018).

By providing an exception only for loans that have "the express purpose" of financing a car or personal property, 10 U.S.C. § 987(i)(6), the MLA further underscores that the loan must be *specific* to the designated purchase, or at least related to that purchase. A loan that satisfies some distinct purpose unrelated to buying a car or personal property will not do. A loan that is offered for an "*express* purpose" means a loan "of a particular or special sort" of purpose and that is "specific" to the designated purpose. *Express*, Webster's Third New International Dictionary 803 (3d ed. 2002); *see Express*, American Heritage Dictionary 627 (4th ed. 2006) ("Particular; specific"). That is, the statute prescribes that the loan must be "[s]pecially designed or intended for [the] particular object" of financing a car or personal property, and not some distinct, unrelated product. *Express*, Oxford English Dictionary 445 (2d ed. 1978). Additionally, the statute's use of the definite article to specify "*the* express purpose," 10 U.S.C. § 987(i)(6) (emphasis added), highlights that there must be "generally only one" operative purpose to the loan, and not several disparate purposes. *Rumsfeld v. Padilla*, 542 U.S. 426, 434 (2004). The

statutory text thus confirms that, for the exception to apply, the loan must specifically finance the purchase of a car or personal property, and not a product bundle that includes items that are distinct from and unrelated to those products.

b. The MLA's structure and logic, and its evident purpose to protect servicemembers, reinforce the conclusion that hybrid loans are consumer credit. Indeed, if hybrid loans qualified for the statutory exception to consumer credit, that result would substantially undercut the statute's servicemember protections, contrary to its basic purpose. *See California Pawnbrokers Ass'n v. Carter*, No. 16-2141, 2016 WL 6599819, at *1 (E.D. Cal. Nov. 8, 2016) ("The purpose of the MLA is to protect members of the military and their dependents from the financial pitfalls related to consumer credit and ensure military readiness."); *Huntco Pawn Holdings, LLC v. U.S. Dep't of Def.*, 240 F. Supp. 3d 206, 211 (D.D.C. 2016) (similar); *see also Henderson ex rel. Henderson v. Shinseki*, 562 U.S. 428, 441 (2011) (construing "provisions for benefits to members of the Armed Services … in the beneficiaries' favor" (quotation omitted)).

For one, holding that hybrid loans satisfy the MLA's exception would undermine the statute's related provision that lenders offering consumer credit cannot use "the title of a vehicle as security for the obligation." 10 U.S.C. § 987(e)(5); *see* 32 C.F.R. § 232.8(f). To take an example, an ordinary cash advance is indisputably consumer credit, and a lender could not lawfully secure its repayment with a

servicemember's car title. But holding that hybrid loans fall within the statutory exception would permit a lender to do just that. If such loans satisfy the exception, the lender could simply bundle a disparate financial product such as a cash advance with an exempt product such as a car, and even the cash advance would be secured by the car title. Congress intended that car titles could secure only car loans in particular, *see* 10 U.S.C. § 987(i)(6), and a contrary reading of the statute would undermine its goal to prevent servicemembers from "losing essential transportation and key family assets" based on other loans, 2006 Report 16.

Indeed, absent an interpretation of consumer credit that encompasses hybrid loans, lenders could shield numerous predatory offerings of financial products such as usurious payday loans by bundling them into the financing for a car or personal property. Yet it is in those circumstances that a servicemember could be particularly vulnerable. The purchase of a car or personal property would itself have added to the servicemember's debts, leaving them with a diminished capacity to take on additional debt. A servicemember would predictably be *more* vulnerable when taking on a hybrid loan that includes a predatory offering than when taking on the predatory offering alone. It is difficult to imagine that Congress would regulated predatory loans when offered on their own, but not when offered to servicemembers along with a car loan that would have added to their debts. *See*

2006 Report 5 (discussing concerns with "predatory lending"). No statutory cue points to that result.

c. Consistent with the statute's text and broader context, the Defense Department's 2016 Guidance confirms that "hybrid" loans that include distinct, unrelated financial products do not satisfy the statutory exception. *See* 81 Fed. Reg. at 58,841. Though the 2016 Guidance addressed questions that had arisen regarding personal property in particular, there is a single statutory exception for car and personal-property loans that employs the same language with respect to both. Whatever principles apply to personal property necessarily apply to cars, and vice versa.

In the 2016 Guidance, the Secretary reasonably determined that loans for product bundles containing financial products distinct from and unrelated to any personal property do not satisfy the statutory exception. The Secretary explained that, under the personal-property "exception from the definition of consumer credit, a loan must finance *only* the acquisition of personal property." 81 Fed. Reg. at 58,841 (emphasis added). The Secretary elaborated that a "hybrid" loan for obtaining personal property and a cash advance would not be "expressly intended to finance the purchase of personal property, because the loan provides additional financing that is *unrelated* to the purchase." *Id.* (emphasis added).

The 2016 Guidance indicated that some items may be so related to the purchased personal property that a loan financing the overall purchase might still satisfy the MLA's exception. *Cf. United States v. Microsoft Corp.*, 253 F.3d 34, 86–87 (D.C. Cir. 2001) (inquiring whether multiple products were "usually" bundled together or whether they were "distinct goods"). The Secretary did not reject the view, for instance, that the purchase of optional side airbags or leather seats that are integrated into the car would be sufficiently related to the purchase of a car, such that a loan financing the entire purchase would qualify for the exception. There is no statutory indication, based on the 2016 Guidance, that the inclusion of commonplace car products would take a loan out of the exception. Commonplace car options such as splash guards or truck bed liners would be far more related to the car than standalone financial products (or in common parlance, the addition of bacon to a burger is still a burger purchase and a first-class upgrade to a plane ticket is still a plane-ticket purchase).

The Secretary did make clear, however, that standalone financial products like cash advances would be distinct from and unrelated to the personal property being purchased. *See* 81 Fed. Reg. at 58,841. As the 2016 Guidance put it, a loan that provides "secured financing of personal property along with additional 'cash-out' financing is not eligible for the exception." *Id.* When a lender chooses to offer

disparate financial products—whether they be cash advances or, as explained below, GAP coverage—those loans are consumer credit subject to the MLA.

2. A hybrid loan that finances optional GAP coverage is consumer credit

Optional GAP coverage is a standalone financial product that is meaningfully distinct from and unrelated to any car that a servicemember purchases. Just as a lender cannot bypass the MLA by bundling a financial product such as a cash advance with a car loan, the same goes for GAP coverage. A hybrid loan financing GAP coverage does not satisfy the statutory exception for a loan "offered for the express purpose of financing the purchase" of "a car." 10 U.S.C. § 987(i)(6).

GAP coverage is a financial product, not a car product. GAP coverage addresses a particular financial risk associated with the payment of car loans. Specifically, a borrower may be unable to pay off the car loan after a total loss of the car where the auto-insurance-policy payout is less than the outstanding loan balance. *See* CFPB Highlights 3; FRB Gap Coverage. GAP coverage bridges that "gap" in payment on the loan. It cancels a debt. In targeting that financial contingency relating to the *loan*, however, GAP coverage does not advance the purchase of a *car* (the car has been bought), and it does not repair or replace the purchased *car* (the car remains totaled).

Additionally, GAP coverage can be bought as a standalone financial product, which would in no respect be the purchase of a car or personal property. *See* FRB

Gap Coverage. If servicemembers want GAP coverage, they "may be able to buy it separately" for "a one-time charge, or premium." *Id.* And if they (for whatever reason) decided to take out a loan to cover that cost, such a loan would indisputably be consumer credit, subject to the MLA's consumer protections. This is because that loan would not be for the express purpose of financing a car or personal property. *See* 10 U.S.C. § 987(i)(6). The loan would be for a financial product.

Nor would an ordinary consumer with an understanding of the auto industry see GAP coverage as advancing the purchase or ownership of a car such that it would be sufficiently related to the car purchase to fall within the car-loan exception. It would be "highly unusual for a lender to *require* that you buy GAP insurance." CFPB GAP Insurance (emphasis added). And GAP coverage is "usually not included in finance agreements" without being specifically added. FRB Gap Coverage.

GAP coverage is thus a product that is appreciably distinct from and unrelated to the purchased car, and the loan here was for a bundle of disparate products, not just for a car. Unlike common items like side airbags or leather seats that a consumer might expect to see preinstalled on a car even if they are sometimes also available as optional purchases, GAP coverage is a standalone financial product. And unlike such everyday car products, GAP coverage does not assist the functioning of the car, further the enjoyment of the car, or facilitate the purchase of the

car. Indeed, the entire premise of GAP coverage is that the car has been irretrievably lost. When a car purchase and GAP coverage are bundled together, it is no longer the simple purchase of a car but the purchase of a car along with a separate financial product. The hybrid loan for the product bundle is not simply a car loan.

Permitting hybrid loans that include GAP coverage to satisfy the MLA's exception would undermine the statute's basic purpose to protect servicemembers. As noted, GAP coverage may be bought on its own based on "a one-time charge." FRB Gap Coverage. But when a lender offers GAP coverage on a loan, the result is "not just the upfront cost but also the cost of the interest when [the borrower] pay[s] for this product over the life of the loan." CFPB GAP Insurance; *see* CFPB Add-Ons ("If you purchase GAP from the dealer, the amount is added to your amount financed, and you'll pay interest on it, increasing your monthly payments and total cost."). And when GAP coverage is sold in connection with a car loan, it can often be at 170% markups. *See* NCLC Report 10. Consumers can instead shop around for GAP coverage, including from their auto-insurance providers, often at lower costs. CFPB Add-Ons.

The protections of the MLA are all the more necessary because GAP coverage does not deliver value across the board. Depending on a servicemember's car loan and the value of the car, "the insurance payout for the totaled vehicle may cover

the outstanding debt." CFPB Highlights 3. And many consumers may "not benefit from the product" at all. *Id.; see* CFPB Add-Ons.

This Court should confirm that the MLA's consumer protections apply to a hybrid loan that includes a standalone financial product like GAP coverage. If there remains any doubt whether the loan here falls outside the car-loan exception, however, the Court should adopt an interpretation consistent with the fundamental purpose of the statute to protect vulnerable servicemembers and, in turn, support their military service. *See* 2006 Report 9 (warning 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"). That reading is particularly warranted given the interpretive "canon that provisions for benefits to members of the Armed Services are to be construed in the beneficiaries' favor." *Henderson*, 562 U.S. at 441 (quoting *King v. St. Vincent's Hosp.*, 502 U. S. 215, 220 n.9 (1991)); *see Boone v. Lightner*, 319 U.S. 561, 575 (1943) (establishing that statutes benefiting servicemembers should be "liberally construed to protect those who have been obliged to drop their own affairs to take up the burdens of the nation").[1]

[1] The loan amount in dispute also purportedly included processing fees and prepaid interest. JA20–21. The government takes no position on whether a hypothetical loan for a car and certain fees or prepaid interest would, in the absence of GAP coverage, also fall outside the MLA's exception.

B. The District Court's Contrary Reasoning Is Incorrect

The district court offered two reasons for finding that the loan here satisfies the MLA's car-loan exception. Neither is persuasive.

1. The district court first held that GAP coverage was "inextricably tied to plaintiff's purchase of the vehicle" and "directly related" to the car. JA55. But as discussed, this misunderstands GAP coverage. Rather than being inextricable, it would be "highly unusual for a lender to require that you buy GAP insurance" as a condition of financing a car, CFPB GAP Insurance; and GAP coverage is "usually not included in finance agreements" unless specifically added, FRB Gap Coverage. Instead, consumers "may be able to buy it separately" for "a one-time charge, or premium." *Id.*

The district court further erred in relying on the fact that GAP coverage "protects the purchaser in the event of theft or damage to the Vehicle that results in a total loss." JA55. Whether a financial product benefits "the purchaser" is not the relevant statutory inquiry. Any number of disparate products—from dental coverage to life insurance to driving lessons—may protect a purchaser in some manner after a car crash. The point is not whether a car owner might need a financial product or other service in the future, however. The car-loan exception identifies only those loans that have "the express purpose" of financing "the purchase" of "a car." 10 U.S.C. § 987(i)(6).

2. The district court also ascribed interpretive significance to the Defense Department's 2020 withdrawal of its 2017 Guidance, which had specifically addressed how to treat GAP coverage under the statutory exception. In particular, the 2017 Guidance had explained that "a credit transaction that includes financing for Guaranteed Auto Protection insurance … would not qualify for the exception." 82 Fed. Reg. at 58,740.

The district court read too much into the withdrawal of the 2017 Guidance. The 2020 withdrawal—made to allow the Department to consider lenders' stated concerns—explicitly took "no position on any of the arguments or assertions advanced as a basis for withdrawing" the 2017 Guidance. 85 Fed. Reg. at 11,843. The withdrawal instead provided room for "additional analysis" from the Department. *Id.* The withdrawal did not offer a substantive interpretation of the statute that would alter the conclusion that the loan here is consumer credit.

Despite the 2020 withdrawal's plain terms, the district court reasoned that "adopting plaintiff's position would essentially contradict the [Department's] withdrawal of the [2017] guidance by effectively reinstating it." JA55. But the mere fact that an agency withdrew a guidance document does not preclude a court from adopting a legal interpretation of the statute. That is especially true here, as the Department made clear that it was taking "no position" on the merits of the 2017 Guidance. 85 Fed. Reg. at 11,843.

In any case, the lenders' stated concerns about the 2017 Guidance that led to its withdrawal do not compel the district court's conclusion, and the court should have assessed the issue on its own terms. Some lenders had asserted that, if hybrid loans that finance a car and GAP coverage were consumer credit, then the MLA (10 U.S.C. § 987(e)(5)) would prohibit those loans from being secured by the car. 85 Fed. Reg. at 11,843. The lenders stated that they might not extend hybrid loans in that situation. *Id.* Yet this is "a feature, not a bug," of the statute. *Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund*, 575 U.S. 175, 194 (2015). The statute closely guards servicemembers' car titles, *see* 10 U.S.C. § 987(e)(5), and a lender must satisfy the car-loan exception to secure a loan using a car, *see id.* § 987(i)(6). The statute covers hybrid loans precisely so lenders cannot bundle in standalone financial products like cash advances while using a car title as a security. Lenders can, however, offer ordinary car loans with standard terms that are secured with the car title. And if lenders want to finance GAP coverage, they can do so separately, too, so long as they follow the statute's consumer protections.

3. To its credit, the district court recognized that the Defense Department retained authority to issue an official interpretation that a loan that includes GAP coverage is "governed by the MLA" and not within the car-loan exception. JA54. Both sides "agree[d]" with that basic authority. JA54.

If this Court disagrees with the United States' statutory interpretation here, it should at a minimum (as the district court did) recognize that it leaves undisturbed the Secretary's authority to promulgate appropriate regulations through notice-and-comment rulemaking that address GAP coverage. Congress authorized the Secretary to "prescribe regulations," 10 U.S.C. § 987(h)(1), including regulations defining consumer credit, *see id.* § 987(h)(2)(D). At most, the statute is silent on the treatment of hybrid loans, and it is the Department that should—after consulting with numerous financial agencies with expertise in consumer affairs—address that issue. *See id.* § 987(h)(3).

CONCLUSION

For the foregoing reasons, the district court's judgment should be vacated.

Respectfully submitted,

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JANUARY 2022

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limit of Federal Rules of Appellate Procedure 29(a)(5) and 32(a)(7)(B) because it contains 6,495 words. This brief also complies with the typeface and type-style requirements of Federal Rules of Appellate Procedure 29(a)(4) and 32(a)(5)–(6) because it was prepared using Microsoft Word 2016 in Crimson Pro 14.5-point font, a proportionally spaced typeface.

/s/ Dennis Fan
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ADDENDUM

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10 U.S.C. § 987

§ 987. Terms of consumer credit extended to members and dependents: limitations

(a) Interest.—A creditor who extends consumer credit to a covered member of the armed forces or a dependent of such a member shall not require the member or dependent to pay interest with respect to the extension of such credit, except as—

(1) agreed to under the terms of the credit agreement or promissory note;

(2) authorized by applicable State or Federal law; and

(3) not specifically prohibited by this section.

(b) Annual Percentage Rate.—

A creditor described in subsection (a) may not impose an annual percentage rate of interest greater than 36 percent with respect to the consumer credit extended to a covered member or a dependent of a covered member.

(c) Mandatory Loan Disclosures.—

(1) Information required.—With respect to any extension of consumer credit (including any consumer credit originated or extended through the internet) to a covered member or a dependent of a covered member, a creditor shall provide to the member or dependent the following information orally and in writing before the issuance of the credit:

(A) A statement of the annual percentage rate of interest applicable to the extension of credit.

(B) Any disclosures required under the Truth in Lending Act (15 U.S.C. 1601 et seq.).

(C) A clear description of the payment obligations of the member or dependent, as applicable.

(2) Terms.—

Such disclosures shall be presented in accordance with terms prescribed by the regulations issued by the Board of Governors of the Federal Reserve System to implement the Truth in Lending Act (15 U.S.C. 1601 et seq.).

(d) Preemption.—

(1)Inconsistent laws.—

Except as provided in subsection (f)(2), this section preempts any State or Federal law, rule, or regulation, including any State usury law, to the extent that such law, rule, or regulation is inconsistent with this section, except that this section shall not preempt any such law, rule, or regulation that provides protection to a covered member or a dependent of such a member in addition to the protection provided by this section.

(2) Different treatment under state law of members and dependents prohibited.—States shall not—

(A) authorize creditors to charge covered members and their dependents annual percentage rates of interest for any consumer credit or loans higher than the legal limit for residents of the State; or

(B) permit violation or waiver of any State consumer lending protections covering consumer credit for the benefit of residents of the State on the basis of nonresident or military status of a covered member or dependent of such a member, regardless of the member's or dependent's domicile or permanent home of record.

(e) Limitations.—It shall be unlawful for any creditor to extend consumer credit to a covered member or a dependent of such a member with respect to which—

(1) the creditor rolls over, renews, repays, refinances, or consolidates any consumer credit extended to the borrower by the same creditor with the proceeds of other credit extended to the same covered member or a dependent;

(2) the borrower is required to waive the borrower's right to legal recourse under any otherwise applicable provision of State or Federal law, including any provision of the Servicemembers Civil Relief Act (50 U.S.C. 3901 et seq.);

(3) the creditor requires the borrower to submit to arbitration or imposes onerous legal notice provisions in the case of a dispute;

(4) the creditor demands unreasonable notice from the borrower as a condition for legal action;

(5) the creditor uses a check or other method of access to a deposit, savings, or other financial account maintained by the borrower, or the title of a vehicle as security for the obligation;

(6) the creditor requires as a condition for the extension of credit that the borrower establish an allotment to repay an obligation; or

(7) the borrower is prohibited from prepaying the loan or is charged a penalty or fee for prepaying all or part of the loan.

(f) Penalties and Remedies.—

(1) Misdemeanor.—

A creditor who knowingly violates this section shall be fined as provided in title 18, or imprisoned for not more than one year, or both.

(2) Preservation of other remedies.—

The remedies and rights provided under this section are in addition to and do not preclude any remedy otherwise available under law to the person claiming relief under this section, including any award for consequential and punitive damages.

(3) Contract void.—

Any credit agreement, promissory note, or other contract prohibited under this section is void from the inception of such contract.

(4) Arbitration.—

Notwithstanding section 2 of title 9, or any other Federal or State law, rule, or regulation, no agreement to arbitrate any dispute involving the extension of consumer credit shall be enforceable against any covered member or dependent of such a member, or any person who was a covered member or dependent of that member when the agreement was made.

(5) Civil liability.—

(A) In general.—A person who violates this section with respect to any person is civilly liable to such person for—

(i) any actual damage sustained as a result, but not less than $500 for each violation;

(ii) appropriate punitive damages;

(iii) appropriate equitable or declaratory relief; and

(iv) any other relief provided by law.

(B) Costs of the action.—

In any successful action to enforce the civil liability described in subparagraph (A), the person who violated this section is also liable for the costs of the action, together with reasonable attorney fees as determined by the court.

(C) Effect of finding of bad faith and harassment.—

In any successful action by a defendant under this section, if the court finds the action was brought in bad faith and for the purpose of harassment, the plaintiff is liable for the attorney fees of the defendant as determined by the court to be reasonable in relation to the work expended and costs incurred.

(D) Defenses.—

A person may not be held liable for civil liability under this paragraph if the person shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error. Examples of a bona fide error include clerical, calculation, computer malfunction and programming, and printing errors, except that an error of legal judgment with respect to a person's obligations under this section is not a bona fide error.

(E) Jurisdiction, venue, and statute of limitations.—An action for civil liability under this paragraph may be brought in any appropriate United States district court, without regard to the amount in controversy, or in any other court of competent jurisdiction, not later than the earlier of—

(i) two years after the date of discovery by the plaintiff of the violation that is the basis for such liability; or

(ii) five years after the date on which the violation that is the basis for such liability occurs.

(6) Administrative enforcement.—

The provisions of this section (other than paragraph (1) of this subsection) shall be enforced by the agencies specified in section 108 of the Truth in Lending Act (15 U.S.C. 1607) in the manner set forth in that section or under any other applicable authorities available to such agencies by law.

(g) Servicemembers Civil Relief Act Protections Unaffected.—

Nothing in this section may be construed to limit or otherwise affect the applicability of section 207 of the Servicemembers Civil Relief Act (50 U.S.C. 3937).

(h) Regulations.—

(1) The Secretary of Defense shall prescribe regulations to carry out this section.

(2) Such regulations shall establish the following:

(A) Disclosures required of any creditor that extends consumer credit to a covered member or dependent of such a member.

(B) The method for calculating the applicable annual percentage rate of interest on such obligations, in accordance with the limit established under this section.

(C) A maximum allowable amount of all fees, and the types of fees, associated with any such extension of credit, to be expressed and disclosed to the borrower as a total amount and as a percentage of the principal amount of the obligation, at the time at which the transaction is entered into.

(D) Definitions of "creditor" under paragraph (5) and "consumer credit" under paragraph (6) of subsection (i), consistent with the provisions of this section.

(E) Such other criteria or limitations as the Secretary of Defense determines appropriate, consistent with the provisions of this section.

(3) In prescribing regulations under this subsection, and not less often than once every two years thereafter, the Secretary of Defense shall consult with the following:

(A) The Federal Trade Commission.

(B) The Board of Governors of the Federal Reserve System.

(C) The Office of the Comptroller of the Currency.

(D) The Federal Deposit Insurance Corporation.

(E) The Bureau of Consumer Financial Protection.

(F) The National Credit Union Administration.

(G) The Treasury Department.

(i) Definitions.—In this section:

(1) Covered member.—The term "covered member" means a member of the armed forces who is—

(A) on active duty under a call or order that does not specify a period of 30 days or less; or

(B) on active Guard and Reserve Duty.

(2) Dependent.—

The term "dependent", with respect to a covered member, means a person described in subparagraph (A), (D), (E), or (I) of section 1072(2) of this title.

(3) Interest.—

The term "interest" includes all cost elements associated with the extension of credit, including fees, service charges, renewal charges, credit insurance premiums, any ancillary product sold with any extension of credit to a servicemember or the servicemember's dependent, as applicable, and any other charge or premium with respect to the extension of consumer credit.

(4) Annual percentage rate.—

The term "annual percentage rate" has the same meaning as in section 107 of the Truth and Lending Act (15 U.S.C. 1606), as implemented by regulations of the Board of Governors of the Federal Reserve System. For purposes of this section, such term includes all fees and charges, including charges and fees for single premium credit insurance and other ancillary products sold in connection with the credit transaction, and such fees and charges shall be included in the calculation of the annual percentage rate.

(5) Creditor.—The term "creditor" means a person—

(A)who—

(i) is engaged in the business of extending consumer credit; and

(ii) meets such additional criteria as are specified for such purpose in regulations prescribed under this section; or

(B) who is an assignee of a person described in subparagraph (A) with respect to any consumer credit extended.

(6) Consumer credit.—

The term "consumer credit" has the meaning provided for such term in regulations prescribed under this section, except that such term does not include (A) a residential mortgage, or (B) a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured.

UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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