



Military Small-Dollar Loan Template

This template for an affordable, small-dollar loan program was developed by bankers who attended the December 6, 2006 FDIC Conference, *"Affordable, Responsible Loans for the Military: Programs and Prototypes"*. Conference participants agreed that the range of options it sets forth would be useful in developing a responsible small-dollar loan program suitable to both a bank and its military customers.

Clearly, this type of bank loan product is a better alternative for the military than detrimental loan products offered by high-cost payday lenders and others. In addition, affordable, small-dollar loan products coupled with a savings component can lead to profitable, long-term customer relationships and receive favorable consideration during CRA examinations. Of course, all aspects of the loan program should be reviewed for compliance with consumer protection and other laws and regulations, including any upcoming regulation that would implement the Talent-Nelson Amendment.

The FDIC recognizes the efforts of financial institutions represented at the conference. We encourage more financial institutions to employ whatever model will work best for them to meet the need for affordable small-dollar credit and asset-building strategies for the military.

Loan Program Features

Loan Amount – up to \$1,000

Most short term “emergency” loans are in the \$500 range; this is also true for “rescue” loans that, for example, would extricate a member of the military from a treadmill of high-cost payday loans or other debt.

Amortization period – up to 12 months

Affordable, amortizing payments made over a suitable period of time are (1) preferable to repeated, consecutive and increasingly costly loan balance renewals that may occur with payday or other loans, and (2) provide the bank with an extended opportunity to cross-sell asset-building products beneficial to both the military customer and the bank.

Interest Rate – 12-18 percent

The experience of several lenders at the conference indicates some profit in this price range and, importantly, the beginning of a very profitable, long-term, multiple-account relationship.

No prepayment penalty

The loan amount is small, the term is relatively short, and it is held in the bank’s consumer loan portfolio; there is no call for a prepayment penalty.

Low/no Origination Fee

A reasonable and low-cost origination fee may help to cover costs in some cases; in others, an origination fee may not be necessary or desirable.

Mandatory Savings Component – 5% or more of the loan payment

A steady increase in savings with a tandem reduction in debt (1) provides the borrower with a source of a payment if a payment can not otherwise be made, (2) builds assets and a financial cushion to meet future emergency needs without borrowing, and (3) provides the bank with an anchor to continue the customer relationship after the loan is repaid.

Direct Deposit & Internet or Telephone Banking

A checking or statement savings account with direct deposit of some or all pay, and the ability of the borrower to transfer payments from the account to the loan by internet or cell phone, provides (1) convenience to a highly mobile military customer group, (2) improves the likelihood of timely repayment to the bank, and (3) locks in a profitable, long-term customer relationship.

Underwriting Considerations

Credit enhancements

- Members of the military are steadily employed with reliable income easily verified through a “leave and earnings” statement.
- The military must conform to a code of conduct that includes the timely repayment of debt.
- The loan amount is very small, far less than for most credit card lines, with lower and decreasing risk.
- A well managed affordable small-dollar loan program generally would fall outside any unusual capital requirements, or the need for additional examination scrutiny, even when considered to be sub prime.
- Direct deposit/EFT of federal wage, salary, and retirement payment is required by law, thus military personnel do establish deposit accounts.
- Additional program features such as tandem savings and checking accounts, with direct deposit and electronic loan payment capability, facilitate timely repayment.

Ease and Speed

- The application and approval process should take no longer than it takes a payday lender to make a pay day loan.
- An automated application, approval, and loan disbursement process would provide fast service to customers as well as lower an institution's origination costs.
- Existing deposit customers may already have been screened by the institution's customer due diligence program (CIP and other account opening procedures such as searches of national databases and/or credit reporting agencies).
- Seasoned customers may be pre-screened for a small closed-end, amortizing credit, or a small open-end line of credit with amortizing monthly payments.
- Current “leave and earnings” statements are readily available for employment and income verification.

Financial Education and Asset-Building

Financial institutions also should make every effort to provide financial education to military personnel requesting small-dollar loans. Improving financial skills can help consumers reduce reliance on short-term, emergency credit and build savings and other account relationships. Moreover, institutions that monitor borrower use of credit, and offer financial counseling or education when signs of financial stress are detected, will help them become better customers.