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FINANCIAL SERVICES NEEDS OF MILITARY PERSONNEL AND THEIR FAMILIES

HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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FINANCIAL SERVICES NEEDS OF MILITARY PERSONNEL AND THEIR FAMILIES

Wednesday, May 18, 2006

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:15 a.m., in room 2128, Rayburn House Office Building, Hon. Sue W. Kelly [chairwoman of the subcommittee] presiding.

Present: Representatives Kelly, Barrett, Davis, Israel, McHenry, Gutierrez, Moore of Kansas, Waters, and Cleaver.

Chairwoman KELLY. This hearing of the Subcommittee on Oversight and Investigations will come to order. And without objection, all members' opening statements will be made part of the record.

Today's hearing is on financial services needs of military personnel and their families. Since the terrorist attacks on September 11th, the men and women of our armed forces have been deployed around the world and here at home to defeat the evildoers and guard our country against future attack. Active duty, Reserve, and Guard forces have all been involved, often being deployed overseas for more than a year at a time.

In my district, the 124th Airlift Wing of the New York Air National Guard and Marine Reserve Refueling Squadron 542 at Stewart National Guard Base have been deployed, along with many other units. Each of the men and women deployed and their families depend on knowing that their finances will be secure when they return, and that criminals and fraudsters will not steal the funds that they have earned in serving our country.

The Defense Department understands that financial issues have an important impact on readiness and morale, and has taken several steps to improve the quality of financial education and services to military personnel and their families.

Every member of the military is now required to take classes in personal finance management, and each command is required to have a command financial counselor to turn to for advice. Unfortunately, this over-reliance on the chain of command gives many junior enlisted personnel the feeling that they will hurt their careers if they come forward and ask for help.

The DoD still does not seem to have a system for determining the financial status of its personnel, or calculating the impact of financial problems on recruiting and retention. I believe that Congress has a duty to make sure that our entire financial services

regulatory system is geared to making sure that military personnel and their families are the primary focus of regulatory activity.

I am disappointed that the DoD recordkeeping is poor, that the performance measurers are nonexistent, and that DoD has not used its position on the Financial Literacy Education Commission this committee authorized to develop systemic programs for protecting its most vulnerable members. In that gap, institutions like NASD, credit unions, and private financial counselors and interested members of the public work hard to overcome these problems.

Today's hearing will examine what is being done to address these needs, and what challenges remain that need to be faced, and where Congress needs to act. I look forward to hearing from today's witnesses, and I am very pleased that we are able to have all of you combined on this one panel today. I think it is going to make this go more smoothly. I turn now to Mr. Gutierrez.

Mr. GUTIERREZ. Good morning. Ever since I was elected to Congress, I have served on this committee—but it was called "Banking" back then—and the Veterans' Affairs Committee. Today's hearing is of particular interest to me because of my work on both of these committees, and I thank Chairwoman Kelly for calling this hearing.

At this time, I would also ask unanimous consent that our colleague, Steve Israel, a member of the Full Committee, be permitted to fully participate in this hearing, and at the appropriate time, make an opening statement.

Chairwoman KELLY. So moved.

Mr. GUTIERREZ. Last year, this committee passed the Military Personnel Financial Services Protection Act, designed to prevent predatory companies from using the U.S. military to prey on financially vulnerable service members by selling them insurance and investment products with little or no value.

During consideration of the bill in the Financial Services Committee, I offered an amendment to extend these protections to abusive lenders who prey on our troops, such as payday lenders. These payday loans are the most abusive financial product being offered to our troops today. And according to military personnel, payday loans threaten troop readiness.

The New York Times and other news outlets have reported extensively on this problem. During last year's committee markup, Chairman Oxley agreed to work with me to include provisions regarding abusive lending in the amendment for Floor consideration. Our work resulted in the inclusion of some basic but important protections for our troops against payday lenders and other abusive lenders who target our troops.

Under this legislation, lenders of both payday and other small loans who target the military can no longer continue a number of egregious practices, including: requiring the involuntary assignment of military wages to secure payment of a loan; contacting or threatening to contact the borrower's commanding officer in the military chain of command in an effort to collect a loan; requiring the borrower to waive any rights under Federal or State law, including the Service Member Civil Relief Act; or using any words or symbols that create the impression that any department of the military endorses the lender or any service or product of the lender.

I am sorry to say that all of these unconscionable practices are currently used by certain payday and short-term lenders.

In addition, extremely high-cost loans must be accompanied by a disclosure notice that informs the consumer of these protections. And there are other options available, including grants and interest-free loans from the military relief societies in the case of a family or other emergency.

It may not sound like a lot, and I do wish that it contained additional limitations on loan amount and the number of turnovers by payday lenders, similar to legislation recently enacted in my home State of Illinois, but this is a good start, since many of these payday and other short-term lenders completely evade regulation by States and the Federal Government.

I look forward to continuing to work on this issue, and I hope that the Senate will pass this worthy legislation, perhaps with these improvements, before we adjourn.

Some may say these protections are not enough. I couldn't agree more. However, I am very pleased that we were able to accomplish this first step in a bipartisan manner, and it passed the House overwhelmingly, 505 to 2, putting us on the record for the first time against exploitation of our troops by these abusive lenders. And I believe that it is always better to light a single candle than to sit and curse the dark.

I am disappointed that the Department of Defense is not here to testify regarding any efforts they may be making in this area, but I look forward to the testimony of the other witnesses here today. Thank you, and I yield back the rest of my time.

Chairwoman KELLY. Thank you. Mr. Davis, do you have an opening statement?

Mr. DAVIS. Yes, Madam Chairwoman. Thank you, Chairwoman Kelly, I appreciate your leadership on this issue. And this is a personal priority for me, going back 30 years this June, and the anniversary of my enlistment in the United States Army. As a commissioned officer, as a unit commander, I dealt with troop credit issues at a wide number of posts around the United States and also overseas.

The military community fosters a sense of trust, and this pervading value has led many service members, including myself and my wife, many years ago, to fall victim to predatory sales schemes. My goal in H.R. 458, The Military Personnel Financial Services Protection Act, was to target the financial services products offered by a number of predatory sales people that were unfairly taking advantage of this military culture of trust.

I think that one thing we need to keep in mind in the process is the best and most practical pieces of legislation are those that have a narrow focus. The broader a bill becomes, the more difficult it becomes to get that bill passed. H.R. 458 is not a catch-all bill. It was specifically designed to do certain things.

Last June, as my Democratic colleague noted, the House resoundingly approved H.R. 458, 405 to 2, with only 2 members voting against the bill. One can only conclude that the House agrees that our service members should not be targeted by the deceptive and predatory practices that H.R. 458 effectively eliminates.

I think that one other thing that we want to keep in mind as well is that the abuses, when we deal with payday lending—one I have dealt with, firsthand, dealing with troop issues—are not large financial services companies. One of the things that I have personally seen in this process are competition for market share that's taking place between financial services providers that are very large in scope. And frankly, what I don't want to see is DoD get caught in the middle of something with fine-sounding language that actually would create a tremendous problem for agencies participating directly with one organization eliminating market share of others.

I think the practicality here, as those of us who have been platoon leaders, company commanders, and battalion commanders understand, is the large community financial services provider, the large financial services firms that are accountable and have internal mechanisms, are not the problem. The problem is the pawnshops, sole proprietorships, those who are not accountable to any professional organization, and take advantage of our troops are the ones who create the problems for those in the command, and for young families.

And I think if we understand the isolation of that abuse, and we focus on very practical and powerful results that give local commanders, and local leaders, the opportunity to enforce State law on post and also to eliminate those pernicious sole proprietorships that really are the root of the problem, and avoid this becoming a smoke screen for competition between other financial services organizations, I think we will have a great piece of legislation.

H.R. 458 effectively eliminates certain practices that have been a problem. Colleagues of mine from the military have told me that they would eliminate certain firms from coming on their post now, were this a piece of legislation. And like Representative Gutierrez, I am hopeful that the Senate will take this up. I encourage all of my colleagues to urge the Senate Committee on Banking, Housing, and Urban Affairs to act on H.R. 458 in the coming weeks.

Thank you again, Chairwoman Kelly, and Ranking Member Gutierrez. Thank you to the witnesses for coming today on both panels, and I look forward to hearing your testimony today.

Chairwoman KELLY. Thank you, Mr. Davis. Mr. Moore?

Mr. MOORE OF KANSAS. Thank you, Madam Chairwoman. And welcome to the witnesses who will be testifying today. Making decisions related to financial matters can be a difficult and overwhelming undertaking for any person. For our military service members and their families, this task can be especially challenging.

With the service member away and often completely unavailable, military families must deal with not only separation from their loved ones, but increased financial hardship as well. Added complexities and costs frequently arise in household budgets with servicemen and women overseas, the strain of which can affect both the deployed individual and their families at home.

A recent study published by the GAO found that adverse consequences resulting from service members' financial problems include a negative effect on overall unit readiness. This is a concern to me, as well as many of the people on this panel, and our colleagues.

Increasingly, service members are faced with more frequent and lengthy deployments, as a result of the involvement of the United States in the war on terror, and our continued presence in Iraq and Afghanistan. Congress and the Department of Defense have taken steps in recent years to help decrease the likelihood that deployed soldiers will experience financial problems, including granting increases in basic military pay, providing special pay increases for active service members deployed to hostile environments, and mandating personal financial management programs to provide service members with financial literacy training and counseling.

Additionally, in November of 2003, I introduced legislation with my colleague, Jim Ramstad, that would require the Department of Defense to pay for domestic trouble for troops home on R&R leave. I understand that this panel is dealing primarily with the financial concerns and loans, things of that nature, that military personnel may become involved in. But the hearing notice said, "The hearing will focus on the financial services needs of U.S. military service members, including active duty personnel as well as those serving in the Reserve and National Guards, and their dependents," so I think it's important to mention these things, as well.

While the DoD—and I'm talking about reimbursement for troop travel, now—would cover the cost of flights from the deployment sites to various hubs, namely Baltimore and Atlanta, when they were brought back on R&R after 6 months in country, they were brought back for 2 weeks of R&R, and I was just really astounded when I learned that they were required to pay for their own domestic travel.

In fact, I talked to soldiers after the fact who told me, "Congressman, I didn't even come home for the R&R with my family, because I didn't have $1,000 for the domestic travel." And what an insult to the people that we say we value.

Jim Ramstad and my bill never came up for a hearing, but I did talk to Secretary Rumsfeld personally, and presented him a copy of a letter that described the need here. And 3 weeks later, it became law. I think that this is a military burden that families should not have to bear, and I am glad that now our government is paying for the service members' entire trip home.

I also did a bill with my friend and colleague on this committee—not here on this subcommittee, but on this committee—Spencer Bachus. When I learned that young persons killed in Afghanistan and Iraq and their families get three things from the United States government—a letter of condolence, "We're sorry about the loss of your loved one," which is very appropriate; an American flag; and the third thing was a so-called death gratuity benefit of $12,000, which again, I thought was a slap in the face to a family who had just made the ultimate sacrifice—I filed a bill and Spencer and I got 243 House Members on the bill which would increase the benefit to $100,000.

I contacted Senator Hagel's office in Nebraska, and he filed our bill in the United States Senate. Again, this never went through a committee, never got called up for a hearing, but is now the law. We made a lot of noise about this, and somebody in the Administration heard about this. And sometimes things work in strange and wonderful ways, even if it's not traditional.

And I think this is another area where we owe the people who serve our country and their families, and I am glad that we are able to accomplish this. And we will get on with the hearing now. Thank you very much.

Chairwoman KELLY. Thank you very much. Mr. Israel, you have been recognized.

Mr. ISRAEL. Thank you, Madam Chairwoman. Let me thank you and the ranking member for allowing me to sit in on this very important hearing.

I am one of four members of the Financial Services Committee who also serve on the House Armed Services Committee. My friend, Mr. Davis, also has that distinction. And I am very proud of the work that Congress did in passing the Military Personnel Financial Service Protection Act. It is a very important step.

I do have one concern, and that is what brings me to this hearing today, with respect to the credit protections that our service members have, which are not effectively enforced.

I had a town meeting in my district last year, and one of the things that I heard consistently was that long and frequent deployments are actually wreaking havoc on the credit reports of our service members. Many of them are not aware of the protections that they have under the Service Members Civil Relief Act. In fact, some creditors are not aware of those protections.

And so, you end up with situations that have been reported in our media nationally, soldiers who are in Humvees having their cars repossessed back home. Soldiers who have gone to fight for our country having their homes foreclosed on back home. Credit reports that are being seriously damaged.

You know, it's one thing to go and fight our country's battles, but then when you have to come home and fight with a creditor because your report was adversely affected because somebody may not have known about the Service Member's Civil Relief Act, that's completely unfair, and we can do better.

Mr. Davis and I have introduced the Service Members Credit Protection Act. It was introduced in consultation with our military, as well as folks who have been involved in the credit industry. And it takes the following common sense steps.

Number one, it requires the Department of Defense to give the national credit bureaus a detailed description of the rights that a service member has under the Service Member's Civil Relief Act.

Number two, it requires national credit bureaus to be informed of the deployment of a service member to a combat zone. The credit agencies would then make a notation on the service member's—in the service member's file, so that when a creditor contacts the agency, they are—they know, absolutely, without any doubt, that the individual that they are looking at, that they may want to file a complaint on, that they're getting a credit history on, is in a combat situation and is protected by Federal law in the Service Member's Civil Relief Act. If they still violate that and go ahead and try to foreclose on a property, or repossess a car, the penalty is doubled.

Just a couple of final points, Madam Chairwoman. This does not exempt our service members from having to pay their bills and having to pay their bills on time. It doesn't stop information from

being reported to the credit agencies. All it does is make sure that everybody knows what the Federal protection is, who is under the Federal protection, and if they still insist on violating that Federal protection by seeking to repossess or foreclose, or adversely affect one's credit, they have to pay a higher price.

And frankly, I know we all agree on both sides of the aisle, if somebody is willing to pay the high price of going to Iraq, Afghanistan, or elsewhere in defense of this country, then unscrupulous creditors should have to pay a high price for violating the law and ruining their credit, taking their personal property away, their cars, and other things.

I am hopeful that our committee and the Armed Services Committee will have hearings on this, and I appreciate the chairwoman's indulgence in letting me come today.

Chairwoman KELLY. Thank you. We have been joined, and by unanimous consent, would welcome any comment by Congresswoman Waters.

Ms. WATERS. Thank you very much. I appreciate the opportunity to come today to share one of my concerns, something that's been nagging me for a long time.

I am very concerned, angered even, about the payday loan industry, and the fact that they are—have increasingly targeted members of the military. They set up near the bases—you must know about this; our service personnel don't make a lot of money. I almost laugh when I see a lot of talk about teaching them how to save and invest. They don't have a lot to save or invest.

That's why they become the targets of these payday loan operations, who realize that they run out of money, and they lend them money at 400 percent interest rates. They are basically robbing them of the opportunity to ever get a handle on their finances. Because when they can't pay, they just roll it over and charge more interest, and it never stops.

I have not seen any effort by the military to do anything about this. And I think we can do something about it. Some thoughts that have come to mind, Madam Chairwoman, is wondering about the ability of the military to set up credit unions where they could be responsible for assisting the military personnel, and/or some way by which there is a warning about these operations that set up near the bases and exploit military personnel because they don't have a lot of money.

I have not seen anything that is being done to protect them, or to educate them to basically serve as a buffer between our military personnel and these predators with the payday loan industry. So I wanted to put that on the record here today. And Madam Chairwoman, I am hoping that one of our witnesses here today can address that issue.

Chairwoman KELLY. Thank you very much. We welcome your presence here.

A couple of things have been said that I want to touch on before I introduce the witnesses. There was some discussion about pawn shops and sole proprietorships and MSB's, the payday loans and check-cashing people. We all understand that not everyone who is in those businesses is predacious. And they serve a purpose for some people.

So, I want to make clear to the panel, that this is—we are here to collect information, and in fact, a payday loan sometimes is cheaper than a bounced check at a bank. I think it's important that people understand that we're not here to voice our own prejudice, but to hear the facts about what actually is there, and what you think—we should be doing, about rectifying a situation which can be badly abused.

Our first witness today is Valerie C. Melvin. Ms. Melvin is currently acting director of military and DoD civilian personnel issues within the U.S. Government Accountability Office, Defense Capability and Management Team. She was appointed to this position in October of 2005, after being accepted into the GAO senior executive service candidate development program. Prior to this appointment, she was an assistant director in GAO's information technology team, where she manages and reviews in the areas of social security, veterans affairs, commerce, energy, and science and technology.

Ms. Melvin graduated from the University of Maryland, with a bachelor's degree in business administration, and a master's degree in management information systems. She is a certified government financial manager. Ms. Melvin has received many GAO awards during her career, including meritorious service awards, and the excellence in human capital management award. Ms. Melvin, we are honored by your presence, and we look forward to your testimony. Please begin.

STATEMENT OF VALERIE C. MELVIN, ACTING DIRECTOR, DEFENSE CAPABILITIES AND MANAGEMENT TEAM, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Ms. MELVIN. Thank you. Madam Chairwoman, Ranking Member Gutierrez, and members of the subcommittee, I am pleased to be here today to discuss the financial management issues of military personnel and their families.

The ability to understand and make informed decisions regarding the management and use of financial resources is a critical issue. DoD has noted that mission readiness, as well as quality of life, in part, depend on whether service members use their financial resources responsibly.

Over the past 4 years, GAO has conducted a number of studies on financial management issues affecting service members, both active duty and Reservists. Among these reports, one issued in April 2005 highlighted some of DoD's efforts to address service members' financial difficulties. At your request, my testimony today will summarize the results of that study, as well as selected findings from other reports.

In this regard, a fundamental message from our work is that service members and their families face a number of challenges that reflect an important and continuing need for assistance and education on financial matters. DoD is the largest employer and trainer of young adults in the United States, with many entry-level service members having limited experience with handling finances.

Moreover, many service members move frequently, and are separated from their families during overseas deployments. A 2002 study noted that 20 percent of junior enlisted service members re-

ported that they struggled to make ends meet, financially. And another 4 percent regarded themselves as in over their heads with respect to their finances.

As further evidence of their difficulties, a 2003 DoD survey, which asks service members whether they had experienced three types of negative financial events, found: 19 percent of deployed and 17 percent of non-deployed pressured by creditors; 21 percent of deployed and 17 percent of non-deployed behind in paying bills; and 16 percent of deployed, and 13 percent of non-deployed who had bounced 2 or more checks.

Both Congress and DoD, as you have noted, have taken important steps to decrease the likelihood that service members will experience financial problems. Since 1999, DoD has requested, and Congress has granted, annual increases in basic pay for all active duty service members that exceeded the average increases in private sector wages, as well as increases in special pays and allowances for deployed service members.

Also, as you have noted, the military has developed personal financial management programs to provide service members with training, counseling, and other assistance to avoid and mitigate the adverse affects of financial problems.

However, while these actions have been a necessary step in the right direction, achieving effective results will require additional efforts by the Department and the service members. Our study found, for example, that some service members had not received the required financial management training, and only one service, the Army, was maintaining data to show who had actually completed the training.

At the same time, we found that some service members were reluctant to seek assistance through the programs that exist, often out of fear that doing so would limit their career progression.

Underlying all of this is that DoD lacks an oversight framework with results-oriented performance measures and reporting requirements to evaluate the effectiveness of its financial management programs across the services. Without such a framework, neither DoD nor Congress will have the necessary visibility into and oversight to ensure the most effective delivery of financial training and assistance to service members.

In closing, Madam Chairwoman, I would like to emphasize that DoD has recognized the importance of financial literacy, and the potentially adverse effects on military readiness when service members experience serious financial problems.

Moreover, the programs that exist to assist service members are positive. Nonetheless, more effort is needed to increase awareness and use of these programs, and ultimately bring about lasting solutions in this critical area. Your hearing today will go far in focusing attention on this important matter.

This concludes my prepared statement. I would be happy to respond to any questions that you may have.

[The prepared statement of Ms. Melvin can be found on page 41 of the appendix.]

Chairwoman KELLY. Thank you very much, and thank you very much, Ms. Melvin, for staying within the 5-minute time line. I neglected to mention, if you haven't testified before us before, that

the boxes there have three colored lights. Green means you have 5 minutes. When it gets to be yellow, it means there is one minute, sum-up period, and when it's red, that's obvious.

We turn now to the—our second witness, Vice Admiral Cutler Dawson, president of Navy Federal Credit Union, and Elisse B. Walter, senior executive vie president, regulatory policy and programs, for NASD.

Admiral Dawson is the president of Navy Federal Credit Union, and it's the world's largest credit union, from what I understand. Prior to his retirement from the Navy, ADM Dawson was the captain of four different Navy ships, the USS Enterprise Battle Group, and the United States Second Fleet.

Elisse B. Walter is the executive vice president of NASD, and leads NASD's investor education foundation. Prior to her service with NASD, Ms. Walter worked for the Commodities Futures Trading Commission and the SEC. Ms. Walter is a graduate of Yale University and Harvard Law. We welcome both of you, and we look forward to your testimony. You may begin, please, Admiral.

STATEMENT OF CUTLER DAWSON, VICE ADMIRAL USN (RET.), PRESIDENT AND CHIEF EXECUTIVE OFFICER, NAVY FEDERAL CREDIT UNION

VADM DAWSON. Thank you, Chairwoman Kelly. Chairwoman Kelly, Ranking Member Gutierrez, and members of the subcommittee, as mentioned, I am Vice Admiral Retired Cutler Dawson, and president of Navy Federal Credit Union. I am here today on behalf of Navy Federal, my credit union, to provide you with an overview of the financial products and services we provide to sailors and Marines and their families, worldwide.

In late 2004, I completed 34 years of service in the Navy, and was chosen to take the helm at Navy Federal. During my time on active duty, I saw what the credit union did and continues to do for sailors and Marines. It is truly their credit union.

Navy Federal began operations over 70 years ago, with a group of Navy Department employees, when they pooled their surplus dollars to make emergency loans to fellow employees. At the end of the first year, the credit union included 49 members, 18 borrowers, and assets of $450. We now serve sailors and Marines worldwide with 112 branch offices, including 21 overseas. Our motto is, "We serve where you serve."

We have not strayed from our mission of serving those members who share a common bond of military or civilian service with the Department of the Navy.

While we provide a full range of financial products and services to all of our members, we continue to focus specifically on our core active duty members. We recognize that military life is always unique, and even more so today, especially for the families of our sailors and Marines.

To meet these unique requirements, we operate in overseas locations, where our members are serving the Nation. We conduct personal financial management training and pre-deployment counseling through Navy and Marine Corps programs in our branch offices. Last year, we conducted over 1,500 such sessions, reaching almost 100,000 members.

We also assist members in financial difficulty through budgetary counseling and debt management services at no cost to the member. We assist survivors of deceased members, serving as a liaison between family members, attorneys, and the military service. And sadly, I will say that we have lost over 400 members in Iraq and Afghanistan since 2001.

We guarantee utility deposits and security deposits for members in areas of major Navy and Marine Corps installations, and we provide members remote access to their accounts, via the Internet worldwide, even on ships at sea.

And we seek to offer financial alternatives to provide lower loan rates and higher savings dividends than are typically found outside the Navy and the Marine Corps installations. And Ms. Waters, I have visited a payday lender, just to see what they were all about.

Over the years, this steady focus on active duty members and their families, and the affinity of our members have, for the Navy and Marine Corps, resulted in a very loyal membership. Recent member focus groups have reaffirmed that the vast majority of our members believe that we do support our active duty members, particularly in today's world.

In summary, Madam Chairwoman, Navy Federal Credit Union recognizes that providing financial products and services needed by our sailors and Marines and their families, wherever they might be, is our mission. And I believe that we are meeting that mission.

I thank you for the opportunity of being here today, and I look forward to your questions.

[The prepared statement of VADM Dawson can be found on page 38 of the appendix.]

Chairwoman KELLY. Thank you very much, Admiral.

Ms. Walter?

STATEMENT OF ELISSE B. WALTER, SENIOR EXECUTIVE VICE PRESIDENT, REGULATORY POLICY AND PROGRAMS, NASD

Ms. WALTER. Thank you. Madam Chairwoman, Ranking Member Gutierrez, members of the subcommittee, and of the committee, good morning. I am Elisse Walter, of NASD, and I am grateful to the committee for inviting us to testify about our efforts to protect members of the armed forces from abusive and misleading sales practices.

We have prepared a comprehensive written statement, and with your permission will submit it for inclusion in the record.

My focus today is on a recently launched NASD effort to educate service members and their families. The program is designed to help them make better financial decisions and avoid fraudulent and inappropriate products and sales pitches.

As you know, Madam Chairwoman, America's men and women in uniform make great personal sacrifices to protect our Nation's security. They should not have to worry about the honesty and integrity of those who offer to help them make sound financial decisions for themselves and their families. In 2003, NASD learned that a Texas broker-dealer was targeting members of the armed forces with misleading sales pitches and improper sales tactics.

As a result, more than a half-million of complicated and often extremely expensive products called systematic investment plans, or

periodic payment plans, were sold to service persons. Not surprisingly, most of the service persons who bought the plans were young and inexperienced.

Since this matter has come to light, as Mr. Davis stated, the House has passed legislation outlying the plans. We responded forcefully to end these practices, sanctioned those responsible, and ensured that victims were being compensated for their losses. We also are taking action to educate military personnel broadly about saving and investing.

We did this first by bringing an enforcement case against the firm selling these plans. The firm was censured and fined $12 million in December 2004. That amount included restitution to thousands of customers who had terminated plans after January 1, 1999, and had paid effective sales charges greater than 5 percent. As of today, more than $4.4 million has been returned to these customers, and we are currently working with the Department of Defense to locate additional service members owed reimbursement.

The remaining funds from our enforcement settlement, about $6.8 million, were transferred to the NASD Investor Education Foundation to be dedicated to the development and deployment of comprehensive financial education programs for members of the armed services and their families. Working closely with the Department of Defense, the NASD foundation has launched a campaign to help service members and their families manage their money with confidence by helping them to understand basic financial concepts, including saving, investing, and the markets.

This program is being implemented online and in military installations worldwide. It encourages members of the armed forces to take control of their financial futures, by providing them and their spouses with financial information to help them make more intelligent saving and investing decisions.

The multi-faceted program includes: an online resource, saveandinvest.org, which has had over 280,000 visitors since it was launched in February of this year; on-the-ground training to support the military's current personal financial management program; a spousal fellowship program that will train a corps of military spouses to provide financial counseling and education within the military community; and for our first training session with 200 slots—we received over 2,600 applicants.

A printed online publication—see it right here—which we put out, in combination with the National Endowment for Financial Education and the National Military Family Association, to help service members and their families deal with the financial issues surrounding deployment and duty station changes. We are working in partnership with DoD, the SEC, the National Military Family Association, and other organizations.

In the last 2 months, NASD has conducted a series of free education forums at bases and duty stations around the world. I should add as an aside, we do financial forums for the general public at large, and I am pleased to see that we have done them with several members of the committee who are here today.

The first of our military education forums took place in Honolulu. It was closely followed by three programs at two bases in Japan, and aboard the USS Ronald Reagan, now on a tour of duty in the

Arabian Gulf. These events have been well attended. In Honolulu, we drew almost 500 members of the military and their families from all branches of the armed services.

The other programs have drawn almost 1,300 additional members of the military and their families. The programming that we offer is designed to meet the needs of both officers and enlisted personnel. Our programs have included seminars on stock scams, predatory lending—a terribly important issue for members of the military—saving for retirement and investing in mutual funds, 529 college savings plans, bonds, and annuities.

These events give us valuable insight into what issues are important to members of the military. In both Okinawa and Yokosuka, for example, there was a great deal of interest in predatory lending, and how to dig out of debt. We have also found there is a lack of clear knowledge about 529 plans.

And importantly, it has become clear, from audience questions, that the thrift savings plan is not well understood. And we plan to create additional content to explain the TSP clearly and concisely to military personnel.

The NASD Investor Education Foundation continues to schedule on-base events. The next two are at the Naval submarine base in Kings Bay, Georgia, in June. Madam Chairwoman, this concludes my statement. I thank you again for the opportunity to testify, and would be happy to answer any questions you and the committee members may have.

[The prepared statement of Ms. Walter can be found on page 67 of the appendix.]

Chairwoman KELLY. Thank you so much, Ms. Walter. Yes, I—Ms. Walter brought to my mind that I neglected to say that, without objection, your full written statements will be made part of the record. And I appreciate the fact that you did that, Ms. Walter.

Ms. Melvin, I am going to start my questioning with you. I was distressed when I noticed that you had said that in—and I'm reading from the GAO report—based on DoD pay data for January 2005, almost 6,000 of 71,000 deployed service members who had dependents did not obtain their family separation allowance in a timely manner.

I would like you to talk to us about this problem, and what has taken place to avoid a repetition of this kind of thing.

Ms. MELVIN. At the time that we did our work, what we found was that in talking to service members—we went to 13 installations in the United States and in Germany—that a number of them had encountered problems in receiving the family separation allowance, difficulties that resulted largely from the fact that there were no procedures in place, necessarily, to make sure that the proper forms could get entered, the proper information, I should say, could be entered into DoD's pay systems.

Beyond that, we also found that, in some cases, the service members themselves simply didn't know enough about the separation allowance to have taken all of the necessary steps to have their paperwork in order, and to make sure that their information was provided to DoD.

So, it was a situation in terms of both DoD not having taken some steps through its policies and procedures, as well as the serv-

ice members not having sufficient awareness in all cases. And I think some of that goes back to the issues that I have heard mentioned in the statements relative to the fact that many of these service members are junior enlisted personnel who don't have the financial literacy or the financial know-how necessary, to address these matters.

In our report, we did make a recommendation—make recommendations, I should say—asking that DoD take steps toward making sure that the service members' family separation allowances were computed, and that they receive them. DoD did agree with our recommendation, and indicated that it was taking measures to actually have policies and procedures in place that would address that particular issue.

Chairwoman KELLY. Thank you. I want to know if you can tell us what the DoD needs to get a results-oriented, department-wide database put together, so that they can assess the effectiveness of their—the PFM's, the personal financial management programs. That's another thing you pointed out down at the bottom of one of your pages.

I am concerned about this, because if we're doing things we have no metric to find out if they're effective. Can you talk to us about that, and tell us what you think can be a comprehensive approach by the DoD to cover the problem?

Ms. MELVIN. You're exactly right, that the oversight issue is very significant, and it is one that we take very seriously in looking at DoD's actions. It's pervasive across a number of programs that DoD has.

In this case, our position is that DoD does need to have performance-based metrics, evaluation tools, and measures that it can use across its systems to, in fact, make more results-oriented decisions relative to the programs that it has.

As far as what DoD can do, I think there are a lot of steps that the Department will have to figure out, relative to how it wants to address it. One of the things I can say, though, is that there are a number of ways in which DoD can take some immediate steps toward that, through looking at some metrics, perhaps, that already exist, perhaps going to looking more at, for example, what service members have their paychecks garnished. There are a number of ways in which they might start to take incremental steps toward putting in place a framework that would have results-oriented measures.

But the Department itself will have to look at this closely. It will have to make decisions relative to what will constitute the types of measures that it needs to have, and ultimately, to have the mechanisms, the framework, the measures there to make sure that it can have a results-oriented approach.

Right now, much of what the Department does is output-oriented, versus outcome-oriented.

Chairwoman KELLY. Thank you. I would like to ask the whole panel what—my colleague, Ms. Waters, brought up predatory lenders. And I would like to ask the whole panel to answer the question about how the DoD and the individual services themselves can approach, especially the young and newly enlisted personnel, to help

them protect themselves from predatory lenders and from people who are doing similar things. I will start with you, Ms. Walter.

Ms. WALTER. Well we, of course, are working with DoD on these issues. And as I noted in my opening statement, predatory lending is a very big concern among the audience members that we have seen at our onsite forums. And I guess that's the bad news and the good news. Bad news, obviously, because this is a terribly important issue, and it's frequently abused, but good news because it shows that people really are interested in learning more.

In fact, in terms of our online resources, the page that we have that's entitled, "Stay Away From Payday Lenders," has, in fact, received—it is the most popular page, other than the homepage on our site. So there is a great deal of interest among military service members in learning more about the practices of payday lenders, and we are more than happy to continue to work and to expand our efforts on that important subject.

Chairwoman KELLY. Thank you. I am out of time, so I turn to my—I'm sorry, I asked the whole panel that, right. Good thing Mike reminded me. Admiral?

VADM DAWSON. I have offices in Hampton Roads, branches in Hampton Roads. As I mentioned to Ms. Waters, I was visiting them last year, and three doors down from one of our branches was a payday lender. I had never been in a payday lender office before, so I went over there to check it out.

It was a nice office. It was clean. The people in there were very courteous and nice. I couldn't get up to the counter to talk to anyone, because there was a line.

I read the disclosure while I was there, and it wasn't 400 percent APR, it was 782 percent APR for a $500 payday loan. At my credit union, we talk about payday lending, and we say that payday lending is the spiral of doom for people who get involved with it. We do what we can to offer alternatives, so people do not have to take payday loans. But 782 percent is a big bite.

But I also would like to say that financial education is not unique to the military. It's unique to our whole country. We talk about this at credit unions all the time, that we all need to do a better job at financial management education. And that's one of the ways that we can all get there.

One last thing. I mentioned that I saw a very nice message that went out to everyone in the Navy the other day. They even—sometimes retired people get those. But it was from the chief of naval personnel, and he was discussing payday lending. And he was instructing all those in the Navy that counsel individuals to do so.

And so, Ms. Waters, there are some things that are starting to be done, the Navy being one of them. And I hope that it continues.

Chairwoman KELLY. Thank you. Ms. Melvin?

Ms. MELVIN. Yes. I would reiterate the financial education as a large piece of what can be done to help our service members, making sure that they're aware of what their options are, and having the choices to make that don't necessarily include going to a particular type of creditor that might take advantage of them in that way.

Beyond that, I would also go back to the oversight issue that I spoke to earlier. I think it's important for DoD to have a full

awareness of what types of situations exist on and off its bases, relative to the use of creditors and resources of that nature.

And then thirdly, there is a mechanism that DoD could use, and that's the Armed Services Disciplinary Control Boards. And while they don't exist solely to perform that function, they are a valuable resource.

When we did issue our report on predatory lending, one of the things we noted, however, was that those boards weren't meeting routinely to make the types of assessments of the businesses that the service members were using. One option and a recommendation that we made was that DoD, in fact, increase the use of such boards to have more oversight and more insight into what the businesses are, and to be able to provide information to service members, to help them make more informed decisions regarding their use.

Chairwoman KELLY. Thank you. My time is up. Mr. Gutierrez?

Mr. GUTIERREZ. Thank you very much. I want to, first of all, thank Congressman Davis for working with me on getting the minimum changes and protections into the law, and hoping the Senate will take up the legislation, as we have heard from the witnesses here, including the vice admiral, about the state of predatory lending and payday loans.

I am always astonished at how difficult it is to get action, either in this committee or the Congress, to protect the public in general, but in this case particularly the military, against those who wish to charge 700, 750, 800 percent interest rates.

I know that we live in a free market system, but sometimes those free markets need to be curbed in when there are abuses, especially when they look like they're from the military, and they use military logo and are right outside military bases.

Anyway, let me follow up. I want to follow up on the chairwoman's questioning, because she is right on, and headed in the right direction. I would like to ask Ms. Melvin from GAO. In its report on predatory lending, the GAO recommended that the armed forces' disciplinary control boards meet at least semi-annually to determine whether to put offices of payday lenders off limits. DoD's response says it would be ineffectual. Do you accept the DoD response?

Ms. MELVIN. Actually, in the response that DoD made to us, they actually agreed with our recommendation, and at least informing us what their actions would be, stated that they would actually do more meetings—I believe our recommendation was that they meet at least semi-annually. And their response to us was that they would take action to meet at least quarterly, I believe.

So, that was their intent. We have not gone back—we have actually gone back and followed up on a routine basis, but we have not seen evidence, I should say, yet as to how routinely they are meeting at this point.

Mr. GUTIERREZ. Okay. So DoD responded that they thought they should meet quarterly on this issue?

Ms. MELVIN. Yes, they—

Mr. GUTIERREZ. Have they ever met, to your knowledge, on this issue with the Armed Forces Disciplinary Control Board?

Ms. MELVIN. We have not looked at that at that level. And I'm sorry, but I am not able to respond to that at this particular—

Mr. GUTIERREZ. So they said they would meet quarterly as to whether or not they should put the offices of payday lenders off limits?

Ms. MELVIN. They said that their boards would meet quarterly to consider the businesses, and the other practices of payday lenders, and also other businesses which have adverse effects for the military.

Mr. GUTIERREZ. Does the DoD have a single point of contact for Federal and State enforcement officials who are investigating predatory lenders?

Ms. MELVIN. No, there is no single—

Mr. GUTIERREZ. Do you think the DoD should have a point of contact so that Federal and State enforcement officials who have investigated predatory lending would have a communications level with them?

Ms. MELVIN. One of the things that we have noted in our work is that, especially across States, when it comes to certain types of lending and insurance there are concerns relative to the differences among States. Our work has actually talked to the need for more coordination across the different States, and with State regulators, and in that regard, to make sure that there are some designated offices or individuals who, in fact, can hear the complaints of consumers, military consumers, in this case and be able to share that information with the regulatory agencies.

Mr. GUTIERREZ. So, in response to the GAO's report on financial product sales, DoD concurred in the GAO's recommendation that the DoD solicitation policy be revised to require that service members' complaints related to financial products be provided to relevant State and Federal financial regulators.

DoD provided you with an estimated completion date of January 1, 2006. Did they meet that date? Are complaints actually being referred?

Ms. MELVIN. It's our understanding that the policy is still in draft and hasn't been issued yet.

Mr. GUTIERREZ. So they didn't meet the completion date of January 1, 2006?

Ms. MELVIN. Yes.

Mr. GUTIERREZ. Okay.

Ms. MELVIN. That's correct.

Mr. GUTIERREZ. So no complaints can be referred since they haven't done that. I think it's going to be pretty quick—still got a green light—it's going to be pretty critical to get the DoD in here, so that we can hear from them, especially hearing from the vice admiral, who said that the admiral went around telling people—that's why I'm going back to the Armed Forces Disciplinary Control Board, because if they do make this an issue, then commanders at all levels can speak to those under their command about not going and forming them, actually instructing them not to go to payday lenders, not to go here, and what places they should or shouldn't go.

I have one last question, and this one is for Elisse Walter. Has the DoD established a single point of contact for NASD to discuss

enforcement and disciplinary actions? If you want to notify DoD that a particular individual or firm that targets military personnel has been subject to disciplinary action by your agency, who would you contact in the DoD?

Ms. WALTER. Well, we have a number of contacts in DoD that we could inform. What we have done, really, relates—we have taken action with respect to the flow of information in the other direction. We want to encourage complaints that come in, either through personal financial managers or otherwise to be referred either to us or to the governmental securities regulators for investigation.

And we have facilitated that on our end by assuring—we have a centralized process for looking at complaints. So we have a single point of contact, a single office to contact at our end, and that is open and available. I'm not aware that DoD has established a particular point of contact with respect to this matter, but I think we feel that we have good channels of communication to provide them with information.

Mr. GUTIERREZ. So the DoD hasn't established a single point of contact for you, in terms of enforcement and disciplinary actions?

Ms. WALTER. Not that I am aware of.

Mr. GUTIERREZ. Okay. And if you want to discuss the matter, in terms of a particular targeting of personnel, you contact various people at DoD?

Ms. WALTER. Well, we would either—

Mr. GUTIERREZ. I mean, I guess—and I will just—I guess my point is because you do what you do, and you protect people by taking action and you've got a $12 million judgement, I just want to know how it is when you do your work, you communicate to DoD so that all the—so that then DoD can do its job and inform all the members of our armed forces that, you know, you found somebody corrupt, fined them $12 million. You said they're still looking to distribute approximately $7 million of the $12 million to armed services personnel.

So, I—it's not about you, I assure you it's not about you. I'm just trying to figure out, for future hearings, what kinds of things we might want to ask DoD to do to better do their job.

Chairwoman KELLY. If the gentleman would yield, I would like to ask if anyone on the panel knows whether the DoJ—I'm sorry, DHS—the DHS, does anybody know if the Coast Guard is having a similar kind of problem as the DoD?

Ms. MELVIN. I'm not aware of any problems in that area, but we have not looked at that.

Chairwoman KELLY. Well, perhaps in addition to getting the DoD, we should perhaps bring in DHS to find out if both—if that service, as well, is affected.

Mr. GUTIERREZ. Yes, I think that's important. I wanted to—and I want to thank you, Vice Admiral, for all you do and the credit union does to help service our military with good financial products. Thank you very much.

Chairwoman KELLY. Thank you. Mr. Davis?

Mr. DAVIS. Thank you, Madam Chairwoman. I could speak as a multiple decades member of what's now Pentagon Federal Credit Union, and also dealing with these issues.

I hear a lot about, you know, these issues. Payday lending, for some reason, has come up repeatedly over and over again. And I think the fundamental issue that we're dealing with, the command is dealing with the rule of law at State level. A business, a legitimate business that's off post can do business—there are certain prescriptions—the reason that we tried to pass H.R. 458, dealing with insurance and mutual funds, is to make sure that we gave that ability to allow State enforcement on the Federal jurisdiction, and also to identify businesses for the command.

But I hear these numbers of interest rates in the hundreds of percent. And I'm just curious, from having dealt with many, many organizations, what the basis of that is, what was the basis of that 782 percent insurance rate that you quoted when you went into the payday lending operation?

VADM DAWSON. It was simply the interest that was charged if someone were to borrow $500 cash advance for payday and have it for a week. That was the annual percentage rate that they were charged.

Mr. DAVIS. So what you were doing was taking all of the fees that were associated—

VADM DAWSON. I was just reading from their disclosure statement on their wall of what they did at the payday lender. And it was quite plain. It was well disclosed, that it would be 782 percent, with everything rolled in to what they charged for that $500.

Mr. DAVIS. I would appreciate it if you would possibly submit that information for the record, so that we could see that.

One of the reasons that I want to bring this up is a little bit deeper. When my family was hurt by a military financial services provider who became the subject of H.R. 458, what caused that hurt was not the practices that were disclosed, I want to make that very clear. What caused the problem was a perceived inter-relationship between retired military personnel who served as executives, as salespeople, as managers in that firm, and it—that was what breached the trust barrier in such a big way here.

And you know, my question would come back, are you going to do away with ATM's? Because under the proposed—you know, we hear this 36 percent interest rate that's thrown around in so many of these dialogues around this, if you go to an out-of-network ATM and a soldier borrows $100 a week, which I used to do things like that, even though ATM's were kind of a new concept before I was commissioned, and it was $2 a transaction for that out-of-network fee, you're dealing with 100 percent interest, automatically, on that loan on an APR basis.

But one would come back from a bank and say that's a fee. And I think the thing that we need to clarify very much, because nobody with common sense is going to take a loan out at 500 or 1,000 percent, or something, you know, like that. What they're going to do is they're going to be dealing with fees.

And the reason that I bring this up is a question that I would like to ask Ms. Walter. You know, it seems that there is a little bit of a question on my mind. We're talking about payday lending. But are you aware of DoD's relationship with other financial services providers who have many, many fees that technically are not interest rates and aren't talked about in a lot of competing legisla-

tion, but actually if you lay that out side by side on the table, what you end up actually having is a higher fee from a firm that is allowed, publicly, to associate with the DoD organizations?

Ms. WALTER. I'm not specifically aware of particular entities. But in general, as you know, we're a securities regulator. One of the most important things to be disclosed to investors—and the same is true in consumer situations that do not involve securities—are not just interest rates in terms of payback for loans, but also the fees associated with it.

Because, obviously, from the point of view of the consumer, the payment is the same. It is money that they have to pay in connection with the transaction. So all of that is really terribly important, and is something that people have to understand before they enter into a transaction.

VADM DAWSON. And sir, I would like to add that Navy Federal has a little over 300 ATM's that we own and provide a service to our members. And we charge no fee at all for any of our members that use those ATM's.

Mr. DAVIS. How about for out-of-network members that use it?

VADM DAWSON. It's $1.50 for out-of-network—

Mr. DAVIS. So 75 percent APR?

VADM DAWSON. It depends on how much they take out. But these are non-members. In other words, these are members that do not belong to our credit union. I think the industry standard for those charges is probably between $1.50 and $4. It is a fee to withdraw their own funds. It is not a loan.

Mr. DAVIS. My point, Admiral, is not to challenge your ability to operate in the free market, it's simply when we bring this issue up I think it's important that we—you know, when we talk about these alleged high interest rates—and I am, again, intimately familiar with this issue, having dealt with a number of credit issues—that there is a difference between fees that are fully disclosed in a market environment, and then the true predatory lender—you know, like I can think of Victory Pawn and Gun, or whatever, on Victory Drive, outside of Fort Bragg, you know, other types of organizations.

And the reason that I bring this question of breach of trust up, as a faithful credit union member—it has nothing to do with your organization, but the more pernicious aspect of this is what I am seeing right now in DoD is being drawn into a very dangerous aspect on this credit issue of true monopolistic competition between a very large financial services provider, which is, you know, seeking to avoid these types of protections we talk about putting in in order to gain market share.

And that's what concerns me with former military members on the board, disorganization showing up at the AUSA convention, when in fact, the Community Financial Services Association, which is the legitimate payday lending open market businesses have sought full cooperation with DoD, and yet those—that cooperation has been rejected. And I personally met with Dr. Chu on this issue to incorporate all changes and questions.

And I would like to just make it a matter of the record that the deeper issue here in credit probably ought to be devoted to a separate hearing. And I would ask Chairwoman Kelly that perhaps we

consider a separate hearing on that issue alone, so that we can focus on the more broad-based financial needs.

I think, at the end of the day, what we're dealing with here are issues of cash flow for families, learning to manage that, and often times, in the emotion of the media or those not connected with the service, we want an immediate scapegoat, somebody that we can hang something on, without necessarily solving the problem. And I think that what I don't want to see is a set of laws passed that gives unfair market advantage to one firm over another that actually charges the same alleged high fees, but it's just disclosed in a slightly different way.

And if you would like to have some private discussion at a later time, we would be glad to share this information with you, that I think you would find particularly disturbing. I yield back my time.

Chairwoman KELLY. I thank you, Mr. Davis. I agree. I think what we're discovering here this morning indicates that we should be having follow-up hearings. I would like to bring in DHS and the DoD. And we should look at a much more broad picture here. I think it would serve us well, in trying to figure out what needs to be done to help and protect our service people. I turn now to Mr. Cleaver.

Mr. CLEAVER. Thank you. My concerns are related to foreclosure; is there any tracking system in place whereby you would know the number of, or the percentage of, members of the military who end up in foreclosure?

Ms. MELVIN. I don't have any information that I could share with you, sir, regarding that.

VADM DAWSON. At my credit union I have that information. I don't have it with me today in that detail. But yes, we track delinquency. And in worst case, when it goes to foreclosure, our numbers are very small. Our membership—we have very few foreclosures. But we track it, and I would be happy to provide you that data from our credit union, if you would like, at any time.

Mr. CLEAVER. I think I would like that information. The Civil Relief Act prohibits an increase in the interest rates and the foreclosures. And I'm wondering—I was looking through the—this is very good, incidentally. I was looking through here, but I couldn't find any information related to either the interest rates issue or foreclosures. And I'm just wondering how many service men and women would even know that they are a victim if they don't know that the Civil Relief Act exists.

VADM DAWSON. I understand your question. It's possible they would probably know, but foreclosures are not conducted if they fall under the Serviceman's Civil Relief Act. I don't think—we don't do it, and I don't know about other institutions, but that's—members are protected under that, should they know that they're protected.

Chairwoman KELLY. We would be very happy—and I just made a note of this, and I think it's a very good point—we will make sure that point gets picked up in our programs on a going forward basis, and so we can help to play a role in educating people about the rights that are available to them.

Mr. CLEAVER. Yes. I don't know if it's anecdotal or not, but many Members of Congress, from time to time, hear from servicemen and

women that, after they were called up to duty, after a certain period of time they ended up losing their homes.

And if it's happening because there is a lack of information going out—you know, it's an injustice in the first place, but I think that the second level of injustice—and maybe the first—is that they don't have the information.

VADM DAWSON. Sir, maybe I can give you some information that might be helpful to you. Just to put it in perspective, I ran some numbers from my credit union on how many folks fell under the—how many people that we have right now who have the protections of the Servicemen's Civil Relief Act, and it's about 980. And we track them very closely, and that number has gone down over the last couple of years. We have been running about an average of maybe 1,000 to 1,200.

And we are very meticulous in following the tenets of the Act in regard to their rights. And we even go one step further. If they apply for relief, it's granted unconditionally, without even an explanation if it's a—if they're under a hardship, which the Act calls for. So they send their documentation in of their orders that brought them to military service, which they all have, and then they fall under the tenets of the Act, and we would not foreclose anyone while they were under that relief.

Chairwoman KELLY. Would the gentleman yield for a comment?

Mr. CLEAVER. Yes.

Chairwoman KELLY. If a service member is not in this country, and there is an action, a proceeding, if the family doesn't know to notify the local sheriff, or whatever, that they are protected by the Act, then the proceeding could go on because they don't know. And I think that's part of your point, is it not?

VADM DAWSON. Well, let's take our case in point, I mean, just what we do, if you're interested in that. Let's say they fail to notify us, in the very worst case. As soon as we found out that they were eligible, we would tell them how to do it, we would make everything retroactive to the date that they entered the service, and—or were called up, and take care of them.

Mr. CLEAVER. I'm not sure it's that simple, because people in Afghanistan and Iraq, and 122 other places around the globe, and I'm just not sure the information is reaching the people who need to know it, whether it's the military person or the families.

And as I said, maybe there has never been an incident, and I'm just going in the wrong direction. But you hear that, you know. It may be like the thing that, you know, everybody—there is something going around the Internet that Members of Congress receive their salaries for life, I think, or—and so maybe it's one of those things. But it is out there, and it bears some attention.

And if I could just close out with a question, I—before I was in Congress, I did a radio show on NPR, and I guess one of the things I kind of campaigned on the air against was the payday loans. One of the things I did eventually discover, and that is because of circumstances, people felt that was the only place they had to go to get financial help. And I'm wondering if the Navy has a payday loan program. I mean, they're going to go somewhere if they're in a crunch.

VADM DAWSON. I can answer that from experience.

Mr. CLEAVER. Yes.

VADM DAWSON. I suppose that it is—all service members are offered the opportunity—and we refer to it in the Navy as, "to take a dead horse." What that is, is you remember advance pay, when you make a PCS change of station, and then you pay it back over 2 years, and it's an interest-free loan of up to 3 months of your base pay.

The reason it's called a dead horse is back in the days of sailing ships, it was like sailing into horse latitudes where there was no wind, and it felt like it took forever to pay it back. That's why it's called a dead horse. But that's—and that's the expression, "beating a dead horse." But that's a form of a loan that I think you're talking about.

Mr. CLEAVER. Well, it's not quite. I know my time is running out. Thank you, Madam Chairwoman.

Chairwoman KELLY. Thank you. Mr. Barrett?

Mr. BARRETT. Thank you, Madam Chairwoman. Ladies and Admiral, thank you for being here today. We greatly appreciate it.

Ms. Melvin, let me address this first question to you. I was reading in your report about personal financial management, PFM—love these acronyms, you Army guys, I'll tell you—the Army requires about 12 hours of PFM; the Navy 16; Marines and Air Force, I think at their first duty station.

If this is a problem—and obviously, it might be—does it make sense to have a standard throughout all the services, whether it's at their first duty station, whether it's every time they change duty stations, something that is similar across the board, so we know that each service member is getting adequate training on personal financial matters?

Ms. MELVIN. Certainly it's possible that, you know, having a standard form of training would provide that. I think the bigger issue, though, is in terms of DoD needing to make sure that it emphasizes what the services need to do and that it has the mechanism to make sure that, regardless of whether the training is standardized or whether it's given at different points by different services, that it has an oversight, a means of knowing that that training is taking place.

So, on the one hand, you could say that standardization would, in fact, provide at least an element of information that says it's occurring at a certain point in time. But the reality is that, given the circumstances that are in play and the number of people involved, I think it would still be questionable as to whether, in fact, even with standardized training, unless there is a reporting mechanism and a tracking mechanism in place to ensure that—to see that that training is actually taking place, it may not necessarily solve the problem.

Mr. BARRETT. But if you had some type of tracking mechanism where you followed up, I mean, I'm looking here. I was in the Army 12 hours, the Navy 16. I'm probably not that much smarter than the Navy guys—I'd like to think maybe I am—but I mean, it doesn't matter, I think, whether you're in the Navy or Marines or Air Force.

Ms. MELVIN. Exactly.

Mr. BARRETT. Financial training is financial training. Wouldn't you agree with that?

Ms. MELVIN. Yes, I do.

Mr. BARRETT. Okay, great. Thank you. Admiral, let's talk a little bit about payday lending. And I know the interest can be high. Let's look at a $200 loan for 2 weeks with a $30 fee. That's about a 391 percent APR.

But when you weigh that versus the cost of bounced checks, the problems it could have with your career and other things, what would these service men and women do, what alternatives do they have—and I know you mentioned one, and I don't know if that is applicable in every situation, because I think you said when you change a duty station, and you certainly don't change all the time—if payday lending is outlawed, what option do these service men and women have? I mean, where can they go for help from week to week if they get in a bind, or something like that?

VADM DAWSON. A couple of things, sir. If they are really in distress, the answer to your question of where they can go, in the Navy and Marine Corps we have a wonderful organization called the Navy and Marine Corps Relief Society that is headquartered here in Washington, but has offices throughout where sailors and Marines serve.

The head of that organization, ADM Abbot, would tell you that they're probably the lender of last resort. And that's a place that sailors and Marines and their families can turn to. And they can get a grant or a loan from them, if they're in distress. That's one place.

I did a data—I asked my people recently to put together some information for me on how much could an E–4 borrow from a credit union, specifically, our credit union. And they ran some numbers for me. And essentially, let's say that they—if they have a good credit rating, an E–4 can essentially borrow pretty much up to a year of his salary.

Mr. BARRETT. Which is how much?

VADM DAWSON. About $24,000.

Mr. BARRETT. $24,000?

VADM DAWSON. Yes.

Mr. BARRETT. Okay.

VADM DAWSON. And if he bought a home and had a mortgage, it could be up to much higher than that, $180,000 to $200,000.

Mr. BARRETT. Sure.

VADM DAWSON. That's a lot of money. And—but what's the safety net after that? That's the question. And the safety net after that would be a payday lender, which as I mentioned earlier, is—I consider to be a spiral of doom, or the Navy Marine Corps Relief Society for, really, when they're in distress.

Mr. BARRETT. Well, and I'm not going to agree—I mean, I am going to agree with you that there probably are some payday lenders or some organizations out there that are not doing it like they're supposed to be doing. I think that's a given, and I think that's one of the reasons why we're here today.

Would you agree, Admiral, that in any legislation that moves forward we need to make sure that we cover how to deal with, for lack

of better words, unscrupulous payday lenders, or organizations that are trying to really take advantage of servicemen and women?

VADM DAWSON. For sure. But 782 percent APR is pretty high. And I have no idea whether that office that I went into was scrupulous or unscrupulous. It's just the way it was.

I would like to make another point, though. I have made some discoveries over this year. I didn't know anything about payday lenders before I started looking at it this year. We have 27 financial budget counselors. If our members are in trouble, they can call these folks, and they will work them through their difficulties. And they will help them work with other creditors and organize their affairs. And we do that at no charge to the member.

I talked to my folks about payday lenders one day, and I said, "How do you find them to deal with when you go to organize someone's debts?" And they—very interesting observation. They said, "We find that folks have multiple payday lenders that they use. And when we go to call them, we end up talking to a back shop that covers a whole network of different storefronts that have different names."

And also, we find that they very much know their members. They know who they're dealing with. They know them by name, and they know them by situation. But it's still a very high percentage that people have to pay when they go into that path.

Mr. BARRETT. And—

Chairwoman KELLY. Mr. Barrett?

Mr. BARRETT. Yes, ma'am?

Chairwoman KELLY. I'm sorry, but you're out of time.

Mr. BARRETT. Thank you.

Chairwoman KELLY. You may submit that in writing, or if we have time, we will try to go back to it. Mr. McHenry?

Mr. MCHENRY. Thank you, Madam Chairwoman. Thank you so much for having this committee hearing, and thank you for your leadership on this issue.

And thank you for your testimony. I was able to listen to your testimony before I had to step out. And so I have missed some of the questions. So just nod and smile if I ask a similar one. That never happens on Capitol Hill, of course, asking similar questions.

But I want to commend my colleague, Geoff Davis, for the legislation he has filed—and I am proud to be a co-sponsor of it—dealing with predatory lending of sorts against military personnel.

You know, Ms. Walter described cracking down on a company that was putting into practice some unethical behavior that was really going beyond the bounds with military personnel, and I want to commend you for doing that. That's a proper role that you play, and I appreciate you stepping up to do that.

It's also come to my attention that certain lending institutions, or certain financial institutions, are requiring service members to waive their rights under the Servicemembers' Civil Relief Act. And I wanted to see if any of you three could address that as something that is ethical or legal. Any of you three?

Ms. MELVIN. I am not aware of the circumstances of them waiving their rights. What I would say, though, is that my understanding of the Servicemembers' Civil Relief Act is that there are specific rights that they do have, and I believe that the legislation

that is being put forward to attempt to strengthen that hopefully would go a long way toward, in fact, preventing that type of situation from occurring.

As I understand, the intent is to achieve more awareness, more information on the part of both the service member, as well as the actual lender. And in that case, hopefully that would lead to those kinds of circumstances not occurring.

Mr. MCHENRY. Admiral?

VADM DAWSON. I discussed this with my folks before I came here, and to the memory of everyone in the credit union, we have never had an issue with the SCRA. And I just don't—I'm not aware of other instances where it's occurred. I just don't have any knowledge on that. But we meticulously follow the tenets.

Mr. MCHENRY. Ms. Walter?

Ms. WALTER. I don't have any specific information about that, either. I will say that in the securities industry, which of course is of limited scope, we have a rule that requires people who operate in the securities industry to adhere to high standards of commercial honor and just and equitable principles of trade.

And the advantage to having that kind of standard applied is that if people behave in a way that violates it, we have the ability to fine them, or in the extreme, to actually kick them out of the industry entirely. And I don't think, in other industries, there are comparable protections, so you would be relying more on common law principles in those kinds of situations.

Mr. MCHENRY. Okay. Ms. Melvin, actually, if I could come back to you about this, if this were occurring—how about I approach the subject this way—if this were occurring, where a financial institution is asking a service member to waive their rights under this Act, is that lawful?

Ms. MELVIN. I would suspect not, but I would respectfully like to defer to our attorneys to make sure that I understood all of the requirements. My understanding is that there are specific rights that the service members have, and that the law protects them against violations of those rights.

Mr. MCHENRY. And so it's something that's really protecting a class of people, and as an individual you can't simply waive that right?

Ms. MELVIN. I'm sorry, waive the right to be protected?

Mr. MCHENRY. Yes.

Ms. MELVIN. Again, I would want to consult with our legal attorneys on whether, in fact, they would. I'm not sure I would—

Mr. MCHENRY. Perhaps I could send that to you in written form, and you and your staff could respond.

Ms. MELVIN. Most certainly. We would be glad to.

Mr. MCHENRY. I would appreciate that. You know, additionally, as the chairwoman said, this isn't really about payday lending, this hearing, but you know, I do have concerns that some institutions, non-payday lenders, for instance, are able to get around the APR limits, or in order to get around disclosing what the APR is for a member of the military or the general public, but specifically the military, that by getting around that, they have all these hidden fees in there, such as insurance policies you have to purchase in order to gain lending.

And I wanted to see if you could address that in any way, shape, or form. Admiral, you made a fatal error at testifying on Capitol Hill. You actually acknowledged my question. So I will direct it towards you.

VADM DAWSON. I don't really have any experience on that. I read some material the other day that said the average bank makes 50 percent of its income on fees. And—but as far as schemes to move around and manipulate people, I'm just not familiar with it.

Mr. MCHENRY. Well, it's probably a helpful thing, running your credit union.

VADM DAWSON. Well, we don't do it. And as Mr. Davis said, the biggest thing that we hold of value is our trust of our members. And if you violate that trust, it would be a terrible thing. So we work very hard at that.

Mr. MCHENRY. Thank you, Congresswoman Kelly.

Chairwoman KELLY. Thank you. Ms. Waters, would you like to ask some questions?

Ms. WATERS. Yes.

Chairwoman KELLY. We recognize you for 5 minutes.

Ms. WATERS. I have a number of questions. Let me ask VADM Cutler Dawson whether or not credit unions are afforded space on every base.

VADM DAWSON. I believe probably they are. There are a variety of credit unions that serve DoD, and there may be some exception to that, but I would say that on the majority of installations, a credit union is welcomed and has a relationship on the base.

Ms. WATERS. And are the new service members given this information when they first come to the base, to let them know that there are credit unions on the base and financial services assistance to help them to understand lending and interest. Is something disseminated to them that would help them to know where to go to get help?

VADM DAWSON. I don't know for sure. I would say that it probably varies from base to base. We participate with many bases where we're located. We're on 22 Navy and Marine Corps bases, and we participate in financial seminars to answer those questions you just posed.

Ms. WATERS. Well, let me just say this, Madam Chairwoman and Members, the payday loan operations and other sharks and predators that operate around bases usually have big, gaudy flashing signs. They are called green money stores, they are called, "Rapid Money," I mean, all kind of names that attract attention. They have neon lights and sometimes they will offer a few other services to go along with it, to attract business.

What I find is, oftentimes, people don't know where the credit union is, but some bases have 50 payday loan operations surrounding the base. And they can't miss them, even if they tried. And so, it becomes very attractive to someone who is making $24,000 a year, who runs out of money, to go to one. And when they find out how they operate, they may go to one, two, three, or four and pick up this $100 or this $200. And when they can't pay it back, it gets rolled over, and it gets rolled over, and it gets rolled over again.

And while our chairwoman made it quite clear we're not here to criticize anybody—I, of course, appreciate the opportunity to be here, but I reserve the right to criticize anybody that I want to criticize. And I criticize payday loan operations and the way that they operate, and the amount of interest that they charge.

Now, having said that, I am talking about any predatory lender. I don't care what shape or form it comes in, whether it's rent to own, or these people who allow, you know, people to pawn their automobile titles or these tax refund loan types. I think it's the responsibility of the military to protect our servicemen and women, and I don't think we're doing a good enough job of it.

We have young people who leave home at 18 or 19 years old. They've never had a checking account. They don't know anything about borrowing money or managing money. And so, I think it's the military's responsibility to not only embrace credit unions and to—these boards, disciplinary control boards have to get a little bit stronger.

I think they should make it off limits some of these predatory operations, and I think they should be very aggressive in doing so. In addition to the disciplinary boards exercising their power and meeting and understanding what's going on around them, I really do believe that the military can be more aggressive in helping to protect these young men and women from predators.

I don't care what shape or form they come in. I don't care about limiting competition with these predators. If the credit unions are able to take over all of these financial services operations and literally close out these predators, I don't care. I mean, you know, free market only goes so far.

And to say that you have somebody who is exploiting and undermining the very people that we say we care so much about, who are preparing to go off to war, or who may be returning from war, or may be on active duty, to say, "Well, you know, let the market place work." I think that's irresponsible.

So, I am pleased to be here today, and I am awfully appreciative for the opportunity, Madam Chairwoman, to be able to voice my opinion and to raise these questions. It's an area that I am going to spend a little bit more time studying.

And let me just close by saying we discovered that these predatory lenders come in all shapes, forms, fashion, and they're more creative. One veteran, we read, received $80,000 in exchange for 10 years of his benefits worth $300,000, according to the Law Center Study. Somebody found a way to buy the benefits of a veteran.

So, you have people who don't give a darn about the future of these people, they don't give a darn about these young people who come with very little knowledge or understanding.

And I'm not talking about young people from any one area of the country. We have young people from the urban areas, but God bless some of those who come from the rural area, I mean, who have never interacted with some of these operations.

So, I just want my members to feel a little bit more passionate about it, as we talk about these things, and I want the military to feel more responsible and take stronger steps to do something about these issues.

And having said that, Madam Chairwoman, I will thank you for the time, and I yield back the balance of my time.

Chairwoman KELLY. We welcome your being here. When I opened this hearing, I spoke of the fact that we were focused on getting information. We need information from you about whether or not we should take a deeper look. I think that question has been answered. The needs of the service people are there. And the things we're talking about are the needs for the very people who are at the margins of what—of being involved in a standardized financial service in this Nation.

So, I believe we will probably be holding a second hearing on this. So right now, let me just note that some members have additional questions for this panel, and they may wish to resubmit them in writing.

So, without objection, the hearing record will remain open for 30 days for the members to submit their written questions to these witnesses, and to place the responses in the record.

And with that, we thank you. We are very grateful for your presence here today. And thank you for being here. This hearing is adjourned.

[Whereupon, at 4:35 p.m., the subcommittee was adjourned.]

A P P E N D I X

May 18, 2006

Opening Statement

Chairman Michael G. Oxley

Committee on Financial Services

Subcommittee on Oversight and Investigations
Financial Services Needs of Military Personnel and Their Families
May 18, 2006

Good morning to our witnesses. Thank you, Chairwoman Kelly, for scheduling this important hearing.

The financial well-being of our nation's military personnel and their families is an issue of great concern to me, this Committee and the Congress as a whole. As I have noted on many occasions, we have a special responsibility to ensure the financial well-being and protection of the young men and women who serve this nation in our armed services.

Last year, this Committee and the whole House of Representatives passed for the second time by an almost unanimous vote legislation to address one problem faced by our young GIs: outrageous on-base sales practices. Hopefully, the Other Body will act soon so we can see this vital legislation enacted.

But these unfair insurance practices are only part of the story. As we will hear today, there are other areas in the financial field where our soldiers need education and guidance. Individual as well as unit consequences can be quite substantial. I am pleased to see that our military recognizes this and is acting to address at least some of the problem areas.

In particular, the now-mandated Personal Financial Management (PFM) training program adopted by the military can, if properly applied and monitored, assist young enlisted personnel in particular to make sound financial decisions early in their military careers.

I am eager to hear from our witnesses and look forward to a productive discussion.

Madame Chairwoman, my thanks again for your efforts to help us all contribute to the financial education and health of our fellow citizens who serve in the military, both at home and abroad.

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Statement of the Honorable Sue Kelly

This hearing will come to order.

Today's hearing of the Oversight and Investigations Subcommittee is on the Financial Services Needs of Military Personnel and their families. Since the terrorist attacks of September 11, 2001 the men and women of our Armed Forces have been deployed around the world and here at home to defeat the evildoers and guard our country against future attack. Active duty, reserve, and guard forces have all been involved, often being deployed overseas for more than a year at a time. In my own district the 124th Airlift Wing of the New York Air National Guard and Marine Reserve Refueling Squadron 452 at Stewart Air National Guard Base have been deployed, along with many other units. Each of the men and women deployed, and their families, depend on knowing that their finances will be secure when they return, and that criminals and fraudsters will not steal the funds they have earned serving our country.

The Defense Department understands that financial issues have an important impact on readiness and morale, and has taken several steps to improve the quality of financial education and services to military personnel and their families. Every member of the military is now required to take classes in personal financial management, and each command is required to have a command financial counselor to turn to for advice. Unfortunately, this over reliance on the chain of command gives many junior enlisted personnel the feeling that they will hurt their careers if they come forward for help. DoD still does not have a systemic system for determining the financial status of its personnel or

calculating the impact of financial problems on recruiting and retention.

I believe Congress has a duty to make sure that our entire financial services regulatory system is geared to making sure military personnel and their families are at the primary focus of regulatory activity. I am disappointed that DoD recordkeeping is poor, that performance measurers are non-existent, and that DoD has not used its position on the Financial Literacy Education Commission (FLEC) this Committee authorized to develop systemic programs for protecting its most vulnerable members. In that gap, institutions like NASD, Credit Unions, private financial counselors and interested members of the public work hard to overcome these problems.

Today's hearing will examine what is being done to meet these needs, what challenges remain to be faced, and where Congress needs to act. I look forward to hearing from today's witnesses.

Congresswoman Debbie Wasserman Schultz (FL-20)
Statement for the Record
House Financial Services Committee – Subcommittee on Oversight & Investigations
"Financial Services Needs of Military Personnel & Their Families" (5/18/06)

Thank you Chairwoman Kelly and Ranking Member Gutierrez for convening what I hope will be the first of many hearings to help us better understand what is really happening in the military credit marketplace. Like most of my colleagues, I have a number of military personnel and reservists in my district, and I am committed to ensuring their financial needs be met fairly and adequately.

Most Americans simply do not receive the training they need during high school and college to manage their personal finances, which is why I joined the House Financial Literacy Caucus when I first came to Congress. When it comes to our service members, we must do all we can to provide them with the tools they need to successfully manage their finances.

I believe it is essential that the Department of Defense and branches of the Armed Forces continue to focus their efforts on improving personal financial management training for all enlisted personnel. I am especially concerned that more junior enlisted personnel, who are paid only modest wages, may be vulnerable to predatory lenders without additional training.

While financial counseling and educational programs are important, I urge my colleagues to consider additional legislative protections if we find that certain widespread abusive lending practices target service members and their families.

During my time in the Florida legislature, I learned about many cases in which payday lenders engaged in improper practices by repeatedly rolling over loans to military personnel. Like Florida, most states now regulate payday lending, and the industry has since adopted a series of best practices based, in part, on my state's laws.

However – since coming to Congress, I have heard anecdotes about other types of lenders that may be actively engaged in unsavory business practices – such as charging service members very high rates, topping off loans with grossly expensive single premium credit insurance and extraneous service fees, and then rolling over the loans.

While today's hearing is a start, I encourage my colleagues and this Committee to continue investigating businesses that may engage in this practice, as rolled loans all too often keep our military personnel in a vicious cycle of debt. I ask this Committee to hold as many hearings as necessary to fully expose predatory actions against our service members and to consider legislative solutions to this devastating problem.

Thank you, I yield the balance of my time.

Testimony Before the House Committee on Financial Services Subcommittee on Investigations and Oversight

of

Cutler Dawson
President/CEO Navy Federal Credit Union

May 18, 2006

Chairman Kelly, ranking member Gutierrez, and members of the Subcommittee, I am VADM (retired) Cutler Dawson, President and CEO of Navy Federal Credit Union. I am here today on behalf of Navy Federal, my credit union, to provide you with an overview of the financial products and services we provide to Sailors and Marines, and their families, worldwide.

In late 2004, I completed a 34-year career in the Navy and was chosen to take the helm at Navy Federal. During that time on active duty, I saw what the credit union did, and continues to do, for Sailors and Marines—it is truly their credit union.

Navy Federal began operations over 70 years ago when a group of Navy Department employees pooled their surplus dollars to make emergency loans to fellow employees. At the end of the first year, the credit union included 49 members, 18 borrowers, and total assets of 450 dollars. We now serve Sailors, Marines and Navy Department employees and their families around the world through 112 branch offices, including 20 overseas. Our motto is "We Serve Where You Serve." We have not strayed from our mission of serving those members who share a common bond of military or civilian service with the Department of the Navy.

While we provide a full range of financial products and services to all of our members, we continue to focus specifically on our core of active duty members. We recognize that military life is always unique, and even more so today, especially for the families of our Sailors and Marines. To meet those unique requirements, we:

► Operate in overseas locations where our members are serving our nation.

► Conduct personal financial management training and predeployment counseling through Navy and Marine Corps programs and our own branch offices; last year we conducted over 1500 such sessions, reaching almost 100,000 members.

► Assist members in financial difficulty through budgetary counseling and debt management services at no cost to the member.

► Assist survivors of deceased members; serving as liaison between family members, attorneys and the military service.

► Guarantee utility company security deposits for members in areas of major Navy and Marine Corps installations.

▶ Provide members remote access to their accounts via the Internet worldwide—even ships at sea. And,

▶ Offer financial alternatives that provide lower loan rates and higher savings dividends than are typically found outside Navy and Marine Corps installations.

Over the years, this steady focus on active duty members and their families and the affinity our members have for the Navy and Marine Corps, have resulted in a very loyal membership. Recent member focus groups have reaffirmed that the vast majority of our members believe that what we do to support our active duty members, particularly in today's world, is the most important service we provide.

In summary, Madam Chairman, Navy Federal Credit Union recognizes that providing the financial products and services needed by our Sailors and Marines and their families, wherever they might be, is our mission. And, I believe that we are meeting that mission.

I thank you for the opportunity to appear before you today and I would be happy to answer any questions you may have.

- Navy Federal was organized in 1933 with only seven members.
- Navy Federal is the world's largest credit union with 2.7 million members and over 5,300 employees. One-third of our employees work in our branch offices worldwide.
- Navy Federal has $25 billion in assets.
- Navy Federal's field of membership includes all Department of the Navy personnel and contractors, other military and civilian personnel assigned or stationed at a Department of the Navy installation, and family members.
- Navy Federal is not for profit, not for charity, but for service.
- Navy Federal's mission: Operate a federal credit union serving a Department of the Navy field of membership to meet the financial needs of the members.
- Navy Federal's vision: Navy Federal Credit Union will perform with such excellence that all present and potential members will choose Navy Federal as the preferred source for their primary, lifetime financial services.
- Navy Federal Credit Union has 112 branch offices and 308 ATMs worldwide.
- Navy Federal offers a full range of financial products and services, including:

  - Share Savings Accounts
  - Share Check Accounts
  - Car Loans
  - Home Loans
  - Credit Cards
  - 24/7 Telephone Access
  - Internet Banking
  - Web Bill Pay
  - Equity Loans
  - Budgetary Counseling

- Navy Federal Financial Group, a wholly/owned subsidiary of Navy Federal, offers our members a wide array of investment and insurance services including, home settlement services, discounted car insurance, financial planning, and brokerage services.

May 2006

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on Oversight and Investigations, Committee on Financial Services, House of Representatives

For Release on Delivery
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MILITARY PERSONNEL

DOD Has Taken Steps to Address Servicemembers' Financial Needs, but Additional Effort Is Warranted

Statement of Valerie C. Melvin, Acting Director
Defense Capabilities and Management

GAO-06-749T

May 18, 2006

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Highlights

Highlights of GAO-06-749T, a testimony before the Subcommittee on Oversight and Investigations, Committee on Financial Services, House of Representatives

MILITARY PERSONNEL

DOD Has Taken Steps to Address Servicemembers' Financial Needs, but Additional Effort Is Warranted

Why GAO Did This Study

The finances of servicemembers and their families have been an ongoing concern of Congress and the Department of Defense (DOD), especially in light of more frequent deployments to support conflicts in Iraq and Afghanistan. Adverse effects that may result when servicemembers experience financial problems include loss of security clearances, criminal or nonjudicial sanctions, adverse personnel actions, or adverse impacts on unit readiness. To decrease the likelihood that servicemembers will experience financial problems, DOD has requested and Congress has granted annual increases in military basic pay for all active duty servicemembers and increases in special pays and allowances for deployed servicemembers The military has also developed personal financial management (PFM) programs to help avoid or mitigate adverse effects associated with personal financial problems. However, studies published in 2002 showed that servicemembers continue to report financial problems

This testimony provides a summary of GAO's prior work examining (1) the extent to which deployments have affected the financial conditions of active duty servicemembers and their families, and (2) steps that DOD has taken to assist servicemembers with their financial needs

www.gao gov/cgi-bin/getrpt?GAO-06-749T

To view the full product, including the scope and methodology, click on the link above For more information, contact Valerie C Melvin at (202) 512-6304 or MelvinV@gao gov.

What GAO Found

DOD data suggests that deployment status does not affect the financial condition of active duty servicemembers, although some deployed servicemembers faced certain problems. Data from a 2003 DOD-wide survey suggests that servicemembers who were deployed for at least 30 days reported similar levels of financial health or problems as those who had not deployed. For example, of junior enlisted personnel, 3 percent of the deployed group and 2 percent of the nondeployed group indicated that they were in "over their heads" financially; and 13 percent of the deployed group and 15 percent of the nondeployed group responded that they found it "tough to make ends meet but keeping your head above water" financially. However, problems receiving family separation allowance and communicating with creditors may result in financial difficulties for some deployed servicemembers. Based on DOD pay data for January 2005, almost 6,000 of 71,000 deployed servicemembers who had dependents did not obtain their family separation allowance in a timely manner. Furthermore, problems communicating with creditors—caused by limited Internet access, few telephones and high fees, and delays in receiving ground mail—can affect deployed servicemembers' abilities to resolve financial issues. Additionally, some financial products marketed to servicemembers may negatively affect their financial condition.

DOD has taken a number of steps to assist servicemembers with their financial needs, although some of this assistance has been underutilized. These steps include PFM training for servicemembers, which is required by all four military services. DOD also provides free legal assistance on purchase contracts for large items and other financial documents. However, according to the attorneys and other personnel, servicemembers do not make full use of available legal services because they may not take the time to visit the attorney's office or they fear information about a financial problem would get back to the command and limit their career progression. In addition, each service has a relief or aid society designed to provide financial assistance through counseling and education as well as financial relief through grants or no-interest loans. Some servicemembers in our focus groups stated that they would not use relief from a service society because they take too long, are intrusive, require too much in-depth financial information, or may be career limiting if the command found out. Servicemembers may use non-DOD resources if they do not want the command to be aware of their financial conditions or they need products or support not offered through DOD, the services, or the installation. Although DOD has taken these steps to assist servicemembers with their financial needs, it does not have the results-oriented departmentwide data needed to assess the effectiveness of its PFM programs and provide necessary oversight. Without an oversight framework requiring evaluation and a reporting relationship between DOD and the services, DOD and Congress do not have the visibility or oversight needed to assess the effectiveness of DOD's financial management training and assistance to servicemembers.

Madam Chairwoman and Members of the Subcommittee:

I am pleased to be here today to discuss the financial service needs of military personnel and their families. The finances of servicemembers and their families have been an ongoing concern of Congress and the Department of Defense (DOD), especially in light of more frequent deployments to support the war on terrorism and conflicts in Iraq and Afghanistan. DOD's Social Compact, which is part of its human capital strategic plan, notes that mission readiness and quality of life depend on whether servicemembers use their financial resources responsibly. Some adverse effects that may result when servicemembers experience serious financial problems include loss of security clearances, criminal or nonjudicial sanctions, or adverse personnel actions including possible discharge from the military. Servicemembers with serious financial issues may also have an adverse impact on the readiness of the unit. For example, servicemembers' financial problems may take the servicemembers and possibly their unit commanders away from their primary duties in order to address problems with creditors. In a 2002 report to Congress, the Navy identified an estimated $250 million in productivity and salary losses due to servicemembers' poor personal financial management.[1]

Congress and DOD have taken steps to decrease the likelihood that deployed and nondeployed servicemembers will experience financial problems. DOD has requested and Congress has granted annual increases in military basic pay for all active duty servicemembers and increases in special pays and allowances for deployed servicemembers, such as the family separation allowance and hostile fire/imminent danger pay. The military also has developed personal financial management (PFM) programs to provide servicemembers with financial literacy training, financial counseling, and other assistance to avoid or mitigate the adverse effects associated with personal financial problems."

Despite the added compensation and the assistance provided through the PFM programs, studies in recent years by DOD and others show that active duty servicemembers continue to report financial problems. For

[1] See Department of Defense, *Report on Personal and Family Financial Management Programs* (Mar. 31, 2002) in response to a House Committee on Armed Services requirement in the National Defense Authorization Act for Fiscal Year 2002.

example, a 2002 study[2] noted that 20 percent of junior enlisted servicemembers reported that they struggled to make ends meet financially and another 4 percent regarded themselves as "in over their heads" with respect to their finances.

In this context, my testimony today will summarize our prior work examining (1) the extent to which deployments have affected the financial conditions of active duty servicemembers and their families and (2) steps that DOD has taken to assist servicemembers with their financial needs.

My statement is based primarily on our work completed in April 2005[3] and our institutional knowledge from prior reviews examining financial issues of servicemembers and their families (see GAO Related Products at the end of this testimony statement). Other information, such as the current status of our recommendations to DOD that were pending at the time when the reports were issued, will also be discussed. We conducted our work in accordance with generally accepted government auditing standards during May 2006.

Summary

DOD-wide survey data suggest that deployment status does not affect active duty servicemembers' financial conditions, although some deployed servicemembers faced additional problems with receiving family separation allowances and communicating with creditors and family. DOD data based on servicemember responses to a 2003 DOD-wide survey suggest that servicemembers who were deployed for at least 30 days reported similar levels of financial health or problems as those who had not deployed. For example, of the junior enlisted personnel, 3 percent of the deployed group and 2 percent of the nondeployed group indicated that they were in "over their heads" financially; and 13 percent of the deployed group and 15 percent of the nondeployed group responded that they found it "tough to make ends meet but keeping your head above water"

[2] See RAND, *Assessing the Personal Financial Problems of Junior Enlisted Personnel*, MR-1444-OSD (2002). This report defines junior enlisted as those enlisted servicemembers with fewer than 10 years of service. Our report defines junior enlisted as servicemembers in pay grades E1 to E4.

[3] The findings cited in this testimony were primarily taken from GAO, *Military Personnel: More DOD Actions Needed to Address Servicemembers' Personal Financial Management Issues*, GAO-05-348 (Washington, D.C.: Apr. 26, 2005); and GAO, *Military Personnel: DOD's Tools for Curbing the Use and Effects of Predatory Lending Not Fully Utilized*, GAO-05-349 (Washington, D.C.: Apr. 26, 2005).

financially. These responses are consistent with the findings that we obtained in a survey of all PFM program managers and in focus groups conducted during our 13 site visits. However, problems receiving family separation allowance promptly and communicating with creditors and families may result in financial difficulties for some deployed servicemembers. Based on DOD pay data for January 2005, almost 6,000 of 71,000 deployed servicemembers who have dependents did not obtain their family separation allowance in a timely manner. The family separation allowance of $250 per month is designed to compensate servicemembers for extra expenses (e.g., childcare costs) that result when they are involuntarily separated from their families. Not receiving this compensation each month to help defray household costs can place a financial strain on the family when the servicemembers are deployed. Furthermore, problems communicating with creditors—caused by limited Internet access, few telephones and high fees, and delays in receiving ground mail—can affect deployed servicemembers' abilities to resolve financial issues. Failure to avoid or promptly correct serious financial problems can result in consequences for these servicemembers, such as bad credit ratings or adverse effects on unit readiness and morale. Additionally, some financial products marketed to servicemembers may negatively affect their financial conditions.

DOD has taken a number of steps to assist servicemembers with their financial needs; however, some of this assistance is underutilized. One step is PFM training for servicemembers, which is required by all four military services, although the extent to which the training is not received is unknown because servicewide totals are not always collected. DOD also provides legal assistance on purchase contracts for large items and other financial documents. According to the attorneys and other personnel, servicemembers do not make full use of available legal services because they may not take the time to visit the attorney's office or they fear information about their financial problems would get back to the command and limit their career progression. In addition, each service has a relief or aid society designed to provide financial assistance through counseling and education as well as financial relief through grants or no-interest loans. Some servicemembers in our focus groups stated that they would not use grants or no-interest loans from a society because they take too long, are intrusive because the financial institution or relief/aid society requires in-depth financial information in the loan or grant application, or could be career limiting if the command found out the servicemember was having financial problems. Servicemembers may choose to use non-DOD resources if they do not want the command to be aware of their financial conditions or they need products or support not offered through DOD, the

services, or the installation. Furthermore, DOD established Armed Forces Disciplinary Control Boards that can make recommendations to place businesses off-limits to servicemembers, which can be an effective tool for avoiding or correcting unfair practices, but data gathered during some of our site visits revealed few times when boards were used to address predatory lending practices. Although DOD has taken these many steps to assist servicemembers with their financial needs, it does not have the results-oriented, departmentwide data needed to assess the effectiveness of its PFM programs and provide necessary oversight. Without an oversight framework requiring evaluation and a reporting relationship between DOD and the services, DOD and Congress do not have the visibility or oversight needed to assess the effectiveness of DOD's financial management training and assistance to servicemembers.

Background

Because large numbers of Americans lack knowledge about basic personal economics and financial planning, U.S. policymakers and others have focused on financial literacy, i.e., the ability to make informed judgments and to take effective actions regarding the current and future use and management of money.[4] While informed consumers can choose appropriate financial investments, products, and services, those who exercise poor money management and financial decision making can lower their family's standard of living and interfere with their crucial long-term goals.

One vehicle for promoting the financial literacy of Americans is the congressionally created Financial Literacy and Education Commission.[5] Created in 2003, the Commission is charged with (1) developing a national strategy to promote financial literacy and education for all Americans; (2) coordinating financial education efforts among federal agencies and among the federal, state, and local governments; nonprofit organizations; and private enterprises; and (3) identifying areas of overlap and duplication among federal financial literacy activities.

[4] See GAO, *Highlights of a GAO Forum: The Federal Government's Role in Improving Financial Literacy*, GAO-05-93SP (Washington, D.C.: Nov. 15, 2004) for an overview of financial literacy issues. This report resulted from a July 28, 2004, forum that GAO hosted to develop recommendations on the role of the federal government in improving financial literacy. The forum's participants included a select group of individuals with expertise in financial literacy and education. They included representatives of federal and state agencies, the financial industry, nonprofit organizations, and academic institutions.

[5] Pub. L. No. 108-159, Title V, (2003).

Since at least the 1980s, the military services have offered PFM programs to help servicemembers address their financial conditions. Among other things, the PFM programs provide financial literacy training to servicemembers, particularly to junior enlisted personnel during their first months in the military. The group-provided financial literacy training is supplemented with other types of financial management assistance, often on a one-on-one basis. For example, servicemembers might obtain one-on-one counseling from staff in their unit or legal assistance attorneys at the installation.

In May 2003, the Office of the Under Secretary of Defense for Personnel and Readiness, DOD's policy office for the PFM programs, established its Financial Readiness Campaign, with objectives that include increasing personal readiness by, among other things, (1) increasing financial awareness and abilities and (2) increasing savings and reducing dependence on credit. The campaign attempted to accomplish these objectives largely by providing on-installation PFM program providers with access to national-level programs, products, and support.

To minimize financial burdens on servicemembers, DOD has requested and Congress has increased cash compensation for active duty military personnel. For example, the average increases in military basic pay exceeded the average increases in private-sector wages for each of the 5 years prior to when we issued our April 2005 report. Also, in April 2003, Congress increased the family separation allowance from $100 per month to $250 per month and hostile fire/imminent danger pay from $150 per month to $225 per month for eligible deployed servicemembers. The family separation allowance is designed to provide compensation to servicemembers with dependents for the added expenses (e.g., extra childcare costs, automobile maintenance, or home repairs) incurred because of involuntary separations such as deployments in support of contingency operations like Operation Iraqi Freedom. Hostile fire/imminent danger pay provides special pay for "duty subject to hostile fire or imminent danger" and is designed to compensate servicemembers for physical danger. Iraq, Afghanistan, Kuwait, Saudi Arabia, and many other nearby countries have been declared imminent danger zones. In

addition to these special pays, some or all income that active duty servicemembers earn in a combat zone is tax free.[6]

Financial Conditions Similar for Deployed and Nondeployed Servicemembers, but Pay Administration and Communication Problems Existed for Deployed Members

Data from DOD suggest that the financial conditions for deployed and nondeployed servicemembers and their families were similar. However, deployed servicemembers faced problems with the administration of an allowance as well as an inability to communicate with creditors. Additionally, some financial products marketed to servicemembers may negatively affect their financial condition.

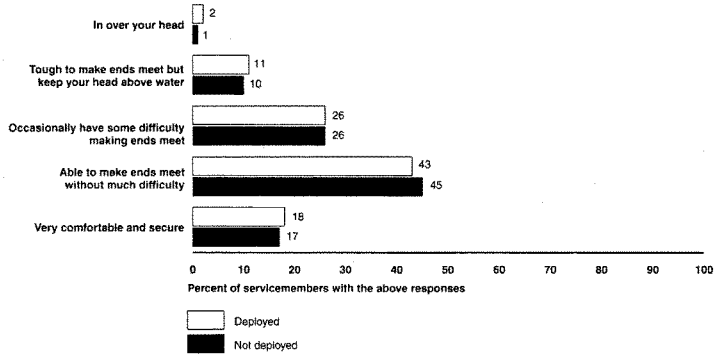
Data Suggest Financial Conditions of Deployed Servicemembers and Their Families Similar to Nondeployed Servicemembers and Their Families

In a 2003 DOD-wide survey, servicemembers who were deployed for at least 30 days reported similar levels of financial health or problems as those who had not deployed. For example, an analysis of the responses for only junior enlisted personnel showed that 3 percent of the deployed group and 2 percent of the nondeployed group indicated that they were in "over their heads" financially; and 13 percent of the deployed group and 15 percent of the nondeployed group responded that they found it "tough to make ends meet but keeping your head above water" financially. Figure 1 shows estimates of financial conditions for all servicemembers based on their responses to this survey.[7]

[6] Department of Treasury, Internal Revenue Service, *Armed Forces' Tax Guide: For Use in Preparing 2005 Returns*, Publication 3, Cat. No. 46072M. This publication noted that all military pay for the month is excluded from income when an enlisted servicemember, a warrant officer, or commissioned officer served in a combat zone during any part of a month or while hospitalized as a result of service in the combat zone. The amount of the exclusion for a commissioned officer (other than a warrant officer) is limited to the highest rate of enlisted pay, plus hostile fire/imminent danger pay for each month during any part of which an officer served in a combat zone or while hospitalized as a result of service there.

[7] DOD's March 2003 survey sample consisted of 34,929 individuals identified by stratified random sampling procedures. DOD reported that completed surveys were received from 10,828 respondents, which resulted in an overall weighted response rate for eligible servicemembers, corrected for nonproportional sampling of 35 percent.

Figure 1: Self-Reported Financial Condition of Servicemembers Who Were and Were Not Deployed for at Least 30 Days at the Time They Completed the 2003 DOD Survey[a]



Source: GAO analysis of DOD data.

[a]Sampling errors of estimates for servicemembers who were not deployed do not exceed +/-2 percentage points. Sampling errors of estimates for servicemembers who were deployed do not exceed +/-5 percentage points. These sampling errors do not include errors due to other sources, such as potential bias attributable to the overall 35 percent response rate. DOD conducted research to assess the impact of this response rate on overall estimates. We have no reason to believe that potential nonresponse bias not otherwise accounted for by DOD's research is substantial for the variables we studied in this report.

These responses are consistent with the findings that we obtained in a survey of all PFM program managers and during our 13 site visits. In the survey of PFM program managers, about 21 percent indicated that they believed servicemembers are better off financially after a deployment; about 54 percent indicated that the servicemembers are about the same financially after a deployment; and about 25 percent believed the servicemembers are worse off financially after a deployment. Also, 90 percent of the 232 recently deployed servicemembers surveyed in our focus groups said that their financial situations either improved or remained about the same after a deployment.

The 2003 DOD survey also asked servicemembers whether they had experienced three types of negative financial events: pressure by creditors, falling behind in paying bills, and bouncing two or more checks. Again, the

findings for deployed and nondeployed servicemembers were similar. For example, 19 percent of the deployed group and 17 percent of the nondeployed group said they were pressured by creditors; 21 percent of the deployed group and 17 percent of the nondeployed group said they fell behind in paying bills; and 16 percent of the deployed group and 13 percent of the nondeployed group said they had bounced two or more checks.[8]

The special pays and allowances that some servicemembers receive when deployed, particularly to dangerous locations, may be one reason for the similar findings for the deployed and nondeployed groups. Deployment-related special pays and allowances can increase servicemembers' total cash compensation by hundreds of dollars per month. Moreover, some or all income that servicemembers earn while serving in a combat zone is tax free.

Deployed Servicemembers Faced Problems Receiving Family Separation Allowance and Communicating with Creditors

Deployed servicemembers experienced problems receiving their family's separation allowance promptly and communicating with creditors and families. Regarding family separation allowance, DOD pay data for January 2005 showed that almost 6,000 of 71,000 deployed servicemembers who have dependents did not receive their family separation allowance in a timely manner. The family separation allowance of $250 per month is designed to compensate servicemembers for extra expenses (e.g., childcare costs) that result when they are involuntarily separated from their families. Delays in obtaining this allowance could cause undue hardship for some families faced with such extra expenses. We previously reported similar findings for the administration of family separation allowance to Army Reserve soldiers and recommended that the Secretary of the Army, in conjunction with the DOD Comptroller, clarify and simplify procedures and forms for implementing the family separation allowance entitlement policy.[9]

The services had different, sometimes confusing, procedures that servicemembers performed to obtain their family separation allowance. DOD officials suggested other factors to explain why some eligible servicemembers had not received their family separation allowance on a

[8] The sampling errors cited for fig. 1 also apply for these findings.

[9] See GAO, *Military Pay: Army Reserve Soldiers Mobilized to Active Duty Experienced Significant Pay Problems*, GAO-04-911 (Washington, D.C.: Aug. 20, 2004).

monthly basis. These factors included servicemembers might not have been aware of the benefit, they may not have filed the required eligibility form, or errors or delays might have occurred when their unit entered data into the pay system. In response to our recommendation that DOD take steps to correct the delayed payment of this allowance, DOD notified finance offices that they should emphasize the prompt processing of such transactions so that payment for the entitlement would begin within 30 days of deployment.

Servicemembers may also experience financial difficulties as a result of communication constraints while deployed. For example, individuals in the focus groups for our April 2005 report suggested that deployed junior enlisted personnel sometimes had less access to the Internet than did senior deployed personnel, making it difficult for the former to keep up with their bills. In addition, some Army servicemembers told us that they (1) could not call stateside toll-free numbers because the numbers were inaccessible from overseas or (2) incurred substantial costs—sometimes $1 per minute—to call stateside creditors. Furthermore, in our March 2004 testimony,[10] we documented some of the problems associated with mail delivery to deployed troops.

Failure to avoid or promptly correct financial problems can result in negative consequences for servicemembers. These include increased debt for servicemembers, bad credit histories, and poor performance of their duties when distracted by financial problems. In our April 2005 report, we recommended and DOD partially concurred that DOD identify and implement steps to allow deployed servicemembers better communications with creditors. In their comments, DOD cited operational requirements as a reason that communications with creditors may not be appropriate. In addition, DOD noted that servicemembers should have extended absence plans for their personal finances to ensure that their obligations are covered.

[10] See GAO, *Military Personnel: Observations Related to Reserve Compensation, Selective Reenlistment Bonuses, and Mail Delivery to Deployed Troops*, GAO-04-582T (Washington, D.C.: Mar. 24, 2004).

Some Financial Products May Negatively Affect Servicemembers' Financial Conditions

Some financial products may also negatively affect servicemembers' financial conditions. For example, although servicemembers already receive substantial, low-cost government-sponsored life insurance, we found that a small group of companies sold products that combine life insurance with a savings fund.[11] These products promised high returns but included provisions that reduced the likelihood that military purchasers would benefit. These products usually provided a small amount of additional death benefits and had much higher premiums than those for the government insurance. These products also had provisions to use accumulated savings to pay the insurance premiums if the servicemembers stopped making payments. Moreover, servicemembers were being marketed a securities product, known as a mutual fund contractual plan, which features higher up-front sales charges than other mutual fund products and has largely disappeared from the civilian marketplace. For both types of products, the servicemembers who stopped making regular payments in the early years paid higher sales charges and likely received lower returns than if they had invested in other products.

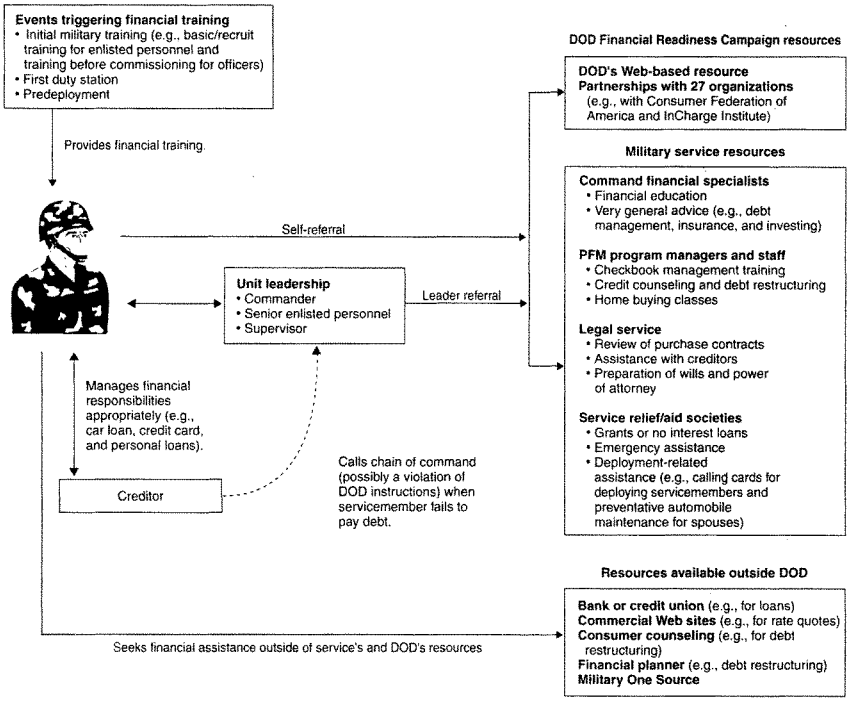
Our November 2005 report made recommendations that included asking Congress to consider banning contractual plans and direct regulators to work cooperatively with DOD to develop appropriateness or suitability standards for financial products sold to servicemembers. We also recommended that regulators ensure that products being sold to servicemembers meet existing insurance requirements and that DOD and financial regulators take steps to improve information sharing between them. In response to the concerns over the products being marketed to servicemembers, securities and insurance regulators have begun cooperating with DOD to expand financial literacy.

[11] See GAO, *Financial Product Sales: Actions Needed to Protect Military Members*, GAO-06-245T (Washington, D.C.: Nov. 17, 2005) and *Financial Product Sales: Actions Needed to Better Protect Military Members*, GAO-06-23 (Washington, D.C.: Nov. 2, 2005).

DOD Has Taken Steps to Assist Servicemembers with Financial Concerns, but Some Assistance Is Underutilized

DOD has taken a number of steps to assist servicemembers with their financial concerns, including providing military-sponsored PFM training, establishing a Financial Readiness Campaign, providing command financial specialists, and using Armed Forces Disciplinary Control Boards. Servicemembers can also access resources available outside of DOD (see fig. 2). However, servicemembers and DOD are not fully utilizing some of this assistance. In addition, DOD does not have an oversight framework to assess the effectiveness of the steps taken to assist servicemembers.

Figure 2: Financial Management Assistance and Training Available to Servicemembers



Sources: GAO analysis of DOD data; Image Art Explosion.

Services Require Financial Management Training

All four military services require PFM training for servicemembers, and the timing and location of the training varies by service. The Army begins this training at initial military, or basic, where soldiers receive 2 hours of

PFM training. The training continues at Advanced Individual Training schools, where soldiers receive an additional 2 hours of training and at the soldiers' first duty station, where they are to receive an additional 8 hours of PFM training. In contrast, Navy personnel receive 16 hours of PFM training during Advanced Individual Training; while, the Marine Corps and the Air Force begin training servicemembers on financial issues at their first duty stations.

Events, such as deployments or permanent changes of station, can trigger additional financial management training for servicemembers. The length of this additional training and the topics covered can vary by installation and command. Unit leadership also may refer a servicemember for financial management training or counseling if the command is aware of an individual's financial problems (e.g., abusing check-cashing privileges).

Despite these policies, some servicemembers have not received the required training, but the extent to which the training is not received is unknown because servicewide totals are not always collected. The Army, which is the only service that collected installation-level PFM data, estimated that about 82 percent of its junior enlisted soldiers completed PFM training in fiscal year 2003. Some senior Army officers at visited installations acknowledged the need to provide PFM training to junior enlisted servicemembers, but also noted that deployment schedules limited the time available to prepare soldiers for their warfighting mission (e.g., firing a weapon). While some services reported taking steps to improve their monitoring of PFM training completion—an important output—they still do not address the larger issue of training outcomes, such as whether PFM training helps servicemembers manage their finances better.[12]

[12] The DOD Instruction 1342.27, dated November 2004, states that "within 3 months after arriving at the first permanent duty station, a servicemember shall demonstrate a basic understanding of pay and entitlements, banking and allotments, checkbook management, budgeting and saving (to include the thrift savings plan), insurance, credit management, car buying, permanent change of station moves . . . and information on obtaining counseling or assistance on financial matters." The instruction, however, does not specify how this is to be measured. It simply says that such an understanding means to comprehend the underlying principles of a subject and apply them to everyday life situations.

DOD's Financial Readiness Campaign Provides Resources Developed with Assistance from External Organizations

DOD's Financial Readiness Campaign, which was launched in May 2003, supplements PFM programs offered by the individual services through Web-based sources developed with assistance from external organizations. The Under Secretary of Defense for Personnel and Readiness stated that the department initiated the campaign to improve the financial management resources available to servicemembers and their families and to stimulate a culture that values financial health and savings. The campaign allows installation-level providers of PFM programs to access national programs and services developed by federal agencies and nonprofit organizations.

The primary tool of the Financial Readiness Campaign has been a Web site designed to assist PFM program managers in developing installation-level campaigns to meet the financial management needs of their local military community. This Web site is linked to the campaign's 27 partner organizations (e.g., federal agencies, Consumer Federation of America, and service relief/aid societies) that have pledged to support DOD in implementing the Financial Readiness Campaign. DOD's May 2004 assessment of the campaign[13] noted, however, that installation-level PFM staffs had made minimal use of the campaign's Web site. DOD campaign officials stated that it was early in implementation of campaign efforts and that they had been brainstorming ideas to repackage information given to PFM program managers, as well as servicemembers and their families.

Command Financial Specialists and PFM Program Staff Are Available for Financial Education and Counseling

At the installation level, the military services provide command financial specialists, who are usually senior enlisted personnel trained by PFM program managers, to assist servicemembers with financial issues. These noncommissioned officers may perform the education and counseling role of the command financial specialist as a collateral or full-time duty. The Navy, Marine Corps, and Army use command financial specialists to provide unit assistance to servicemembers in financial difficulties. The Air Force does not use command financial specialists within the unit, but has the squadron First Sergeant provide first-level counseling.

Individual servicemembers who require counseling beyond the capability of the command financial specialists or First Sergeants in the Air Force

[13] Office of the Deputy Under Secretary of Defense (Military Community and Family Policy), *Initial Assessment and Follow-on Plan for the Department of Defense Financial Readiness Campaign* (May 27, 2004).

can see the installation's PFM program manager or PFM staff. The PFM program manager is a professional staff member designated and trained to organize and execute financial planning and counseling programs for the military community. PFM program managers and staff offer individual financial counseling as well as group classes on financial issues.

Free Legal Assistance Offered, but Servicemembers Do Not Make Full Use of This Assistance

DOD provides free legal assistance on contracts and other financial documents at installations, but servicemembers do not make full use this assistance. For example, legal assistance attorneys may review purchase contracts for large items such as homes and cars. In addition, the legal assistance attorneys offer classes on varying financial issues including powers of attorney, wills, and divorces. However, legal assistance attorneys at the 13 installations we visited for our April 2005 report stated that servicemembers rarely seek their assistance before entering into financial contracts for goods or services such as purchasing cars or lifetime film developing.

Instead, according to the attorneys, servicemembers are more likely to seek their assistance after encountering problems. For example, used car dealers offered low interest rates for financing a vehicle, but the contract stated that the interest rate could be converted to a higher rate later if the lender did not approve the loan. Servicemembers were later called to sign a new contract with a higher rate. By that time, some servicemembers found it difficult to terminate the transaction because their trade-in vehicles had been sold.

Legal assistance attorneys, as well as other personnel in our interviews and focus groups, noted reasons why servicemembers might not take greater advantage of the free legal assistance before entering into business agreements. They stated that junior enlisted servicemembers who want their purchases or loans immediately may not take the time to visit the attorney's office for such a review. Additionally, the legal assistance attorneys noted that some servicemembers feared information about their financial problems would get back to the command and limit their career progression.

Service Relief/Aid Societies Provide Financial Assistance

Each service has a relief or aid society designed to provide financial assistance to servicemembers. The Army Emergency Relief Society, Navy-Marine Corps Relief Society, and the Air Force Aid Society are all private, nonprofit organizations. These societies provide counseling and education as well as financial relief through grants or no-interest loans to eligible

servicemembers experiencing emergencies. Emergencies include funds needed to attend the funeral of a family member, repair a primary vehicle, or buy food. For example, in 2003, the Navy-Marine Corps Relief Society provided $26.6 million in interest-free loans and $4.8 million in grants to servicemembers for emergencies.

Some servicemembers in our focus groups stated that they would not use grants or no-interest loans from a service society because they take too long, are intrusive because the financial institution or relief/aid society requires in-depth financial information in the loan or grant application, or could be career limiting if the command found out the servicemembers were having financial problems. The Army Emergency Relief Society attempted to address the time and intrusiveness concerns with its test program, Commander's Referral, for active duty soldiers lacking funds to meet monthly obligations of $500 or less. After the commander approves the loans, the servicemembers can expect to receive funds quickly. However, noncommissioned officers in our individual interviews and focus groups said the program still did not address servicemembers' fears that revealing financial problems to the command could jeopardize their careers.

Non-DOD Resources May Be Used When Sevicemembers Need Additional Financial Support or Confidentiality

Servicemembers may choose to use non-DOD resources if they do not want the command to be aware of their financial conditions or they need financial products or support not offered through DOD, the services, or the installation. In such cases, servicemembers may use other financial resources outside of DOD, which are available to the general public. These can include banks or credit unions for competitive rates on home or automobile loans, commercial Web sites for interest rate quotes on other consumer loans, consumer counseling for debt restructuring, and financial planners for advice on issues such as retirement planning.

Armed Forces Disciplinary Control Boards Can Help Curb Predatory Lending Practices

DOD has used Armed Forces Disciplinary Control Boards to help curb predatory lending practices and minimize their effects. These boards and the recommendations that they make to an installation commander to place businesses off-limits to servicemembers can be effective tools for avoiding or correcting unfair practices. However, data gathered during some of our site visits to the various installations revealed few times when the boards were used to address predatory lending practices. For example, the board at Fort Drum, New York, had not met in about 4 years, and the board's director was unaware of two lawsuits filed by the New York Attorney General that involved Fort Drum servicemembers.

- The Attorney General settled a lawsuit in 2004 on behalf of 177 plaintiffs—most of whom were Fort Drum servicemembers—involving a furniture store that had improperly garnished wages pursuant to unlawful agreements it had required customers to sign at the time of purchase.
- The Attorney General filed a lawsuit in 2004 involving catalog sales stores. He characterized the stores as payday-lending firms that charged excessive interest rates on loans disguised as payments toward catalog purchases. Some servicemembers and family members at Fort Drum fell prey to this practice. The Attorney General stated that he found it particularly troubling that two of the catalog stores were located near the Fort Drum gate.

In contrast to the Fort Drum situations, businesses near two other installations we visited changed their lending practices after boards recommended that commanders place or threaten to place the businesses on off-limits lists. Despite such successes, boards might not be used as a tool for dealing with predatory lenders for a variety of reasons. For example, as a result of high deployments, commanders may minimize some administrative duties, such as convening the boards, to use their personnel for other purposes. In addition, the boards may have little basis to recommend placing or threatening to place businesses on the list if the lenders operate within state laws. Furthermore, significant effort may be required to put businesses on off-limits lists. While recognizing these limitations, in our April 2005 report we nonetheless recommended that all Armed Forces Disciplinary Control Boards be required to meet twice a year. In responding to our recommendation, DOD indicated that it intended to establish a requirement for the boards to meet even more frequently—four times a year—and direct that businesses on the off-limits list for one service be off-limits for all services.

DOD Lacks Oversight Framework for Assessing and Monitoring PFM Program Effectiveness

Although DOD has made resources available to assist servicemembers, it lacks the results-oriented, departmentwide data needed to assess the effectiveness of its PFM programs and provide necessary oversight. The November 2004 DOD instruction that provides guidance to the services on servicemembers' financial management does not address program evaluation or the reports that services should supply to DOD for its

oversight role.[14] In our 2003 report,[15] we noted that an earlier draft of the instruction emphasized evaluating the programs and cited metrics such as the number of servicemembers with wages garnished. DOD officials said that these metrics were eliminated because the services did not want the additional reporting requirements.

The only DOD-wide evaluative data available for assessing the PFM programs and servicemembers' financial conditions were obtained from a general-purpose annual survey that focuses on the financial conditions of servicemembers as well as a range of other unrelated issues. The data were limited because (1) DOD policy officials for the PFM programs can only include a few financial-related items to this general purpose survey, (2) a response rate of 35 percent on a March 2003 active duty survey leads to questions about the generalizability of the findings, and (3) DOD has no means for confirming the self-reported information for survey items that ask about objective events such as filing for bankruptcy. Without an oversight framework requiring common evaluation DOD-wide and reporting relationships among DOD and the services, DOD and Congress do not have the visibility or oversight they need to assess the effectiveness of DOD's financial management training and assistance to servicemembers. In response to a recommendation in our April 2005 report for DOD to develop a DOD-wide oversight framework and formalize its oversight role for the PFM programs, the department indicated that it is pursuing management information that includes personal finances to support its implementation of the President's Management Agenda and to comply with the Government Performance Results Act.

Concluding Observations

In summary, as mentioned earlier in my testimony, Congress and DOD have taken steps to decrease the likelihood that deployed and nondeployed servicemembers will experience financial problems. The prior increases in compensation, efforts to increase the financial literacy of servicemembers, and fuller utilization of the tools that DOD has provided for addressing the use of predatory lenders should positively affect the financial conditions of military personnel. While additional efforts are warranted to implement our recommendations on issues such

[14] DOD Instruction 1342.27, *Personal Financial Management for Service Members* (Nov. 12, 2004).

[15] See GAO, *Military Personnel: DOD Needs More Data to Address Financial and Health Care Issues Affecting Reservists*, GAO-03-1004 (Washington, D.C.: Sept. 10, 2003).

as improving DOD's oversight framework for assessing its PFM programs, some of these efforts to address the personal financial conditions of servicemembers and correct past programmatic shortcomings are well underway. Sustaining this momentum will be key to minimizing the adverse effects that personal financial management problems can have on the servicemember, unit, and service.

Madam Chairwoman and Members of the Subcommittee, this concludes my prepared statement. I would be happy to respond to any questions you may have.

Staff Contact and Acknowledgments

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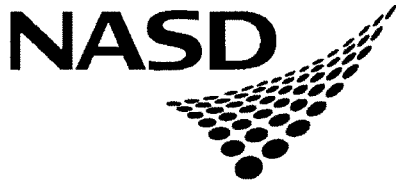

Testimony

Of

Elisse B. Walter

Senior Executive Vice President
Regulatory Policy and Programs

Before the
Committee on Financial Services
Subcommittee on Oversight and Investigations

Hearing on the Financial Services Needs of
Military Personnel and Their Families

United States House of Representatives

May 18, 2006

Mr. Chairman and Members of the Subcommittee: NASD is grateful to the committee for inviting us to testify on NASD's regulatory activities regarding inappropriate sales of certain investment products to members of the armed forces and NASD's financial education programs focused on military servicemembers and their families, and for allowing us to submit this statement for the record.

NASD

Founded in 1936, NASD is the world's pre-eminent private-sector securities regulator. In 1939, the SEC approved NASD's registration as a national securities association under authority granted by the 1938 Maloney Act Amendments to the Securities Exchange Act of 1934. We regulate every broker-dealer in the United States that conducts a securities business with the public—about 5,200 securities firms that operate more than 108,000 branch offices and employ about 664,000 registered representatives.

Our rules regulate every aspect of the brokerage business. Our market integrity and investor protection responsibilities include compliance examinations, rule writing, enforcement, professional training, licensing and registration, dispute resolution and investor education. NASD examines broker-dealers for compliance with NASD rules, MSRB rules and the federal securities laws, and we discipline those who fail to comply. Last year, NASD filed a record number of new enforcement actions (1,410) and barred or suspended more individuals (830) from the securities industry than in any previous year. NASD has a nationwide staff of more than 2,400 and is overseen by a Board of Governors, more than half of whom are not in the securities industry. During the last four years, NASD has been in the process of separating from The NASDAQ Stock Market.

Executive Summary

America's men and women in uniform make great personal sacrifices to protect our nation's security. They should not have to worry about the honesty and integrity of those who offer to help them make sound financial decisions for themselves and their families. Yet thousands of mostly young servicepersons have been disadvantaged by inappropriate sales of products and services, including the sale of an investment product called Periodic Payment Plans or PPPs.

NASD learned in 2003 that a broker-dealer was targeting U.S. servicemen and women with these investment products, and was doing so using improper sales practices. We have responded forcefully to end these practices, sanction those responsible for them, ensure that their victims are recompensed for their losses, and educate military personnel broadly about saving and investing.

My testimony today will focus on this last item—our recently launched efforts to educate servicepersons and civilians so that they are able to avoid fraudulent and inappropriate products and sales pitches.

By way of background, First Command Financial Planning Inc. of Fort Worth, Texas, a broker-dealer with many ties to the military, using misleading sales pitches and improper sales tactics, had targeted and sold more than a half-million of complicated and often extremely expensive PPPs to servicepersons, many of whom were young and inexperienced investors. An investor in a PPP makes monthly payments of as little as $50 for a fixed time period, usually 15 years. The payments are invested in mutual funds and the investor is charged a 50 percent sales load or up-front fee on the first year's payments. Payments during the remainder of the 15-year term are not subject to sales loads, so that the effective sales charge decreases if the investor continues to make contributions. However, if the investor stays in the plan for more than 45 days, yet fails to make contributions over the full 15-year term, he or she can pay a sales charge of up to 50 percent of the total amount invested.

After a thorough investigation, including taking testimony from 16 current and former First Command employees, reviewing more than 25,000 pages of documents and over 50,000 email messages, NASD brought disciplinary action against the firm. NASD coordinated its activities with the SEC and both cases against the firm were announced on the same day.

The firm was censured and fined $12 million in December 2004. That amount included restitution to thousands of customers who had terminated PPPs after January 1, 1999, and had paid effective sales charges greater than five percent. By February 2006, more than $4.4 million had been returned to these customers. About $6.8 million was transferred to the NASD Investor Education Foundation to be dedicated to financial education programs for members of the armed services and their families.

First Command has informed NASD that it has ceased selling PPPs. That firm, however, was not the only firm selling PPPs to military servicepersons. NASD has ongoing investigations of additional firms that also sold the plans, although most of them have now stopped. Statistics show that the rate of new PPP account openings at one of the largest sponsors has dropped from about 1,000 per month to about 10 per month.

The First Command case vividly illustrates the need for the education and protection of military servicepersons and family members who invest in securities. Since our settlement with First Command, NASD has devoted a great deal of time, money and attention to developing a far-reaching program for providing financial education to military servicepersons and their families.

NASD Investor Education Foundation

NASD established the NASD Investor Education Foundation in December 2003, inspired in part by survey data, which showed that mainstream investors had a troubling lack of knowledge and understanding of markets and investment products. Since then, we have contributed $31 million to the NASD Foundation. Last year, the SEC filed a motion with the federal court handling the Global Research Analyst Settlement, requesting the transfer to the NASD Foundation of the approximately $55 million in investor education

funds in that settlement. In September 2005, the court approved the SEC's request, and the funds should be transferred in the near future.

Through its grant making, the NASD Foundation funds programs that provide information and resources to audiences typically underserved by financial education programs. More than $4.5 million dollars has been awarded to organizations for educational programs and research projects that reach out to, among others, minorities, young investors, Native American communities and the elderly.

Research grants offer experts a chance to provide insight into how investors make decisions, what information they need to make better-informed decisions and how to create better learning environments. Recent grants include:

- University of Connecticut is conducting experiments that manipulate the visual display of Web-based disclosure information to determine investor preferences, and the effect on comprehension and retention of disclosure information.

- Princeton University is examining psychological biases that play a role in poor investment decisions and developing and testing a set of interventions to promote wise investing by mitigating these biases.

Grants awarded to educational projects aim to create and expand investment resources for populations most in need. Recent educational grants include:

- Collaborating with the University of Florida, Kansas State University and the University of Kentucky, the University of Tennessee will develop a workplace investor education program for young adult workers in Florida, Kansas, Tennessee and Kentucky.

- WISE Senior Services of Santa Monica, in collaboration with the AARP Foundation, is examining the susceptibility of the elderly to fraudulent investment solicitations.

- As part of its successful *Building Native Communities* financial education series, First Nations is producing an educational curriculum called *Investment Skills for Families* and training an initial pool of Native Americans to deliver the new material.

SaveAndInvest.org

As mentioned above, approximately $6.8 million of the First Command settlement funds has been transferred to the NASD Foundation and specifically earmarked for programs designed to help members of the military and their families better understand basic financial concepts, including saving, investing and the markets.

Many servicemembers report having difficulty covering expenses and saving for the future. Research conducted in June 2005 found that only 29 percent of military personnel who currently invest received a passing grade on a quiz about basic financial knowledge. However, 58 percent of survey respondents said that it was very important to them that they become more knowledgeable about saving and investing. Sixty-two percent indicated that they plan to increase their investment levels in the next year.

Working closely with the Department of Defense, the NASD Foundation launched a multifaceted military financial education program early this year. This comprehensive campaign to help servicemembers and their families manage their money with confidence is being implemented on military installations worldwide. It encourages members of the armed forces to take control of their financial futures—by providing them and their spouses with financial information to help them make intelligent saving and investing decisions.

The multifaceted program includes:

- an online resource center, www.SaveAndInvest.org, that serves as a centralized, trusted source for unbiased information on saving and investing, including original content, interactive tools/games, partner resources, frequently asked questions, and more;

- on-the-ground training to support the military's current Personal Financial Management program by establishing a coordinated and uniform financial education program, including the training and continuous certification of personal financial counselors and other volunteers;

- a spousal fellowship program that will train a corps of military spouses to provide financial counseling and education within the military community;

- a print and online publication that helps servicemembers and their families deal with the financial issues surrounding deployment and duty-station changes; and

- partnerships with the Department of Defense, the U.S. Securities and Exchange Commission, the National Military Family Association and other organizations whose expertise in the financial education arena and experience in addressing military audiences complement the NASD Foundation's commitment to providing financial education information and resources to servicemembers and their families.

To ensure that these programs and tools are well exploited by the military community, the NASD Foundation's efforts include a long-term, public awareness campaign that will:

- provide a coordinated, national financial literacy campaign to a military population that is often unable to set and achieve financial goals, unwilling or

unable to save, overextended in debt, vulnerable to fraud and unaware of what can be done to gain control of the situation;

- help military families understand how the financial choices they make can either improve or diminish their ability to achieve goals such as homeownership, a college education, a secure retirement and peace of mind; and
- communicate positive and motivational messages in a variety of ways and through a diversity of media so that everyone in the military has the opportunity to see, understand and act upon them.

Soon after launching SaveAndInvest.org in January 2006, an NASD Investor Education Foundation team traveled around the world to conduct a series of free financial education forums at bases and duty stations in the United States and far beyond our borders. The first of these free forums, a multi-service event, took place in Honolulu, Hawaii; followed quickly by programs at Camp Foster (a U.S. Marine Base), Okinawa, Japan; Yokosuka Naval Base, Yokosuka, Japan; and aboard the San Diego-based USS RONALD REAGAN, now on a tour of duty in the Arabian Gulf.

The Honolulu financial education forum was offered in partnership with Military Family Support Centers serving the Air Force (Hickam Air Force Base), Army (Schofield Barracks), Coast Guard (US Coast Guard-District 14), Marine Corps (MCB Hawaii) and Navy (Pearl Harbor). It was attended by almost 500 members of the military and their families. The event drew attendance from all branches of the U.S. military and Coast Guard. The others programs have drawn almost 1,300 additional members of the military and their families.

At the forums, presenters from NASD covered topics including fundamental principles of saving and investing, how to check the background of your broker or firm, and how to use NASD's mutual fund expense analyzer, a Web-based tool developed by NASD. In addition to this general information, NASD and representatives of the Securities and Exchange Commission and the Hawaii state securities regulators presented financial seminars including:

- Smart Saving and Investing—Avoid the Predatory Loan Trap;
- What to Look for in an Investment Advisor;
- Mutual Funds, 529 Plans and More;
- Bond Investing: the Basics and Beyond;
- Annuities: What You Should Know;
- Stock Trading and the Anatomy of a Stock Scam; and
- Smart Saving for Retirement.

The sessions were well attended and gave attendees an opportunity to receive detailed information and ask specific questions pertaining to their own financial situations.

Aboard the USS RONALD REAGAN, the goal of the three-person NASD team was to integrate itself into the life of the aircraft carrier. Presentations were made virtually around the clock in an effort to reach both day and nightshift personnel. In all,

close to 30 presentations were made during the three days aboard ship, attended by approximately 1000 members of the REAGAN crew. In addition to the core presentations on Predatory Lending, Smart Saving for Retirement and Smart Mutual Fund and 529 Investing, the team provided seminars on Smart Bond Investing, Annuities, Nuts and Bolts of Mutual Fund Share Classes and Expenses, How to Select a Broker or Financial Professional, and Stock Trading and the Anatomy of a Stock Scam.

The NASD Investor Education Foundation continues to schedule on-base events to reach the men and women of the military with this important message. The next scheduled events are two forums at the Naval Submarine Base in Kings Bay, Georgia, on June 13, 2006.

These events give us valuable insight into what issues are important to the members of the military. In both Okinawa and Yokosuka, there was a great deal of interest in predatory lending and how to dig out of debt. There is a clear lack of knowledge about 529 plans, and it was also clear from the audience questions that the Thrift Savings Plan (TSP) was not well understood. NASD plans to create additional content on the SaveAndInvest.org Web Site to clearly and concisely explain the TSP to military personnel.

Our Partners

The NASD Foundation joined forces with the SEC, the National Military Family Association, the Association for Financial Counseling and Planning Education, the InCharge Education Foundation, the National Endowment for Financial Education, the American Savings Education Council, CincHouse.com and the Consumer Federation of America to develop programs, provide training, and distribute information and resources to the military community.

Future Plans and Programming

Through a combination of its own initiatives and partner programs funded by foundation grants, the NASD Foundation will bring the financial education community together with the goals of empowering individuals to learn more in less time, helping organizations work together on new and existing initiatives, and establishing more coordinated and uniform financial education programs. Specific programs will include:

- a financial education e-learning game specifically designed for servicemembers and their families;
- educational toolkits for trainers, offering multiple levels of personal financial information; and
- the expansion of Military Saves, a national program designed by the Consumer Federation of America to encourage servicemembers and their families to save and build wealth.

In order to ensure the Military Financial Education Program's effectiveness, the NASD Foundation plans to conduct a follow-up survey of servicemembers and their families to evaluate the effectiveness of the campaign. In addition, the NASD Foundation will report on changes within DOD, service-specific military command, and other partners to address the importance of financial readiness. We will also measure the demand for financial and investor education materials related to the campaign.

Conclusion

Thank you for giving us the opportunity to testify on these important topics and for your important work on this issue. America's men and women in uniform deserve honesty and integrity from those who sell them financial products. NASD will continue its work to protect all investors, including those in our nation's military.