The Commonwealth of Massachusetts

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April 1, 2004

Ms. Kathleen O'Loughlin Dias
Director of Legal & Government Affairs
Massachusetts State Automobile Dealers Association, Inc.
59 Temple Place
Boston, MA 02111

Dear Ms. Dias:

This letter is written in response to your correspondence of November 12, 2003 and in follow-up to the meeting held with representatives of the Massachusetts State Automobile Dealers Association, Inc., the Massachusetts Bankers Association, Universal Underwriters (CCIA), and the Alliance of Automobile Manufacturers and certain staff of the Division of Banks (the "Division") Legal Unit and Compliance Unit on November 5, 2003 relative to the inclusion of charges for debt cancellation coverage in an automobile retail installment contract governed by G.L. c. 255B. The Division has also received and reviewed other correspondence on behalf of credit unions related to this subject matter.

As you know, the Division issued an opinion dated August 4, 2003[1] addressing whether the charges for debt cancellation coverage are permitted on contracts subject to said chapter 255B and whether such charges could be included in the amount financed. Debt cancellation contracts are agreements between lenders and borrowers where a lender agrees to cancel all or part of a customer's obligation to repay an extension of credit upon the occurrence of a specified event. As referenced in the noted opinion, #03-029, the debt cancellation coverage at issue is commonly referred to as "GAP", which generally provides that in the event of a total loss of the financed vehicle, the gap between what is owed on the finance agreement and the value of the car would be waived by the financing entity. In general, debt cancellation products are recognized as permissible products offered by banks and credit unions on a direct or indirect basis. The opinion stated that a charge for debt cancellation coverage may not be included as part of a contract subject to G.L. c. 255B.

G.L. c. 255B, §14 pertaining to finance charges provides that a retail seller may charge, receive and collect for any new or used motor vehicle, a finance charge not in excess of an annual percentage rate of twenty-one percent. In addition, the last paragraph of said section 14 states "[T]he finance charge shall be inclusive of all charges incident to investigating and making the contract, and for the extension of the credit provided for in the contract and *no fee, expense or other charge whatsoever shall be taken, received, reserved or contracted for except as provided in this section[*finance charges*]* and in section 11 and section 17 and for those items expressly provided for in the retail installment contract as set forth in

[1] *See* Division Opinion 03-029.

chapter 140D." *Emphasis supplied.* Section 11 of chapter 255B authorizes the holder of a retail installment contract to collect a delinquency charge on each installment payment not paid within 15 days of its due date, and section 17 authorizes the holder to collect a deferment or extension charge from the borrower for deferring a scheduled payment or extending the term of the contract. The original enactment and historical development of chapter 255B makes clear that charges that were not finance charges or authorized charges under sections 11, 17 or set forth in then section 9, were not permissible for inclusion in a retail installment contract.[2] The Division has interpreted this language consistent with the premise that other charges not authorized in the cited sections were prohibited.[3] Accordingly, it remains the Division's position that no fees or charges may be taken, received or contracted for except those which are finance charges, delinquency charges or deferment or extension charges. In addition, it has been the consistent position of the Division that said chapter 140D is a consumer credit cost disclosure statute and not an enabling statute. Chapter 140D does not authorize a creditor to assess certain charges to a consumer but rather establishes how any authorized charges must be properly disclosed.

Following extensive review and discussion of this matter, the Division has determined that the charges for debt cancellation coverage elected by a borrower may be included as part of the retail installment contract and are deemed to be a "finance charge" and are otherwise authorized for purposes of G.L. c. 255B, §14. Moreover, such charges must be *treated* as a "finance charge" and included in the calculation of the maximum permissible annual percentage rate of twenty-one percent for purposes of demonstrating compliance with G.L. c. 255B, §14. Accordingly, the amount of the debt cancellation premiums or charges must be included in the calculation of the annual percentage rate which rate may not exceed the maximum allowable rate of twenty-one percent.

With respect to the applicable disclosure requirements, the Commonwealth's Truth in Lending Act, G.L. c. 140D and its implementing regulation 209 CMR 32.00 *et seq*., provide that the charges or premiums paid for debt cancellation coverage may be excluded from the finance charge when its sale conforms to certain conditions which include a written disclosure to the borrower that such coverage is not required; written disclosure to the borrower of the fee or premium for the initial term of coverage; and the borrower signs an affirmative written request for coverage.[4] It is the position of the Division that the charges or premiums for debt cancellation coverage included as an item in a retail installment sales contract subject to said chapter 255B should be disclosed in accordance with G.L. c. 140D and 209 CMR 32.00 *et seq*. as those provisions apply to debt cancellation products.

Accordingly, if the retail seller properly excludes the debt cancellation charges from the Truth in Lending finance charge disclosures, then it must do different calculations to determine the Truth in Lending annual percentage rate and the annual percentage rate for purposes of determining compliance with the maximum rate allowed under G.L. c. 255B, §14, currently twenty-one percent. The charges for the debt cancellation coverage must be listed in the itemization of amount financed in accordance with the requirements of 209 CMR 32.18(3). The Division will review the applicable disclosure documentation and calculations in determining compliance with G.L. c. 255B, G.L. c. 140D and 209 CMR 32.00 *et seq*.

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[2] *See* St. 1958 c. 674.
[3] *See*, e.g. Division Opinion 99-114(charge for default or repossession fee by retail seller not authorized under G.L. c. 255B).
[4] *See* 209 CMR 32.04(4)(c).

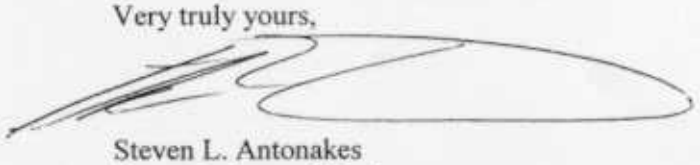
In summary, charges for debt cancellation coverage may be included as part of a retail installment contract subject to G.L. c. 255B. These charges must be included in the calculation of the annual percentage rate and such rate must be within the twenty-one percent maximum allowable rate set forth in G.L. c. 255B. For purposes of disclosure, debt cancellation charges may be disclosed in accordance with G.L. c. 140D and 209 CMR 32.00 *et seq*. as those provisions apply to debt cancellation products.

The position stated herein is the ruling of the Division and negates the determination in Opinion 03-029 which stated that a charge for debt cancellation coverage may not be included as part of a contract subject to G.L. c. 255B.

The Division does not negate a prior opinion lightly and in doing so here acknowledges the difficulty of always being able to reconcile changes in products with statutory language which essentially has in this case been unchanged in over two decades. It becomes more significant when it involves a law with an interest rate cap in a consumer transaction. Accordingly, the Division would encourage all interested parties subject to the provisions of G.L. c. 255B which are at issue to seek a clarifying amendment to the statute. Those parties should prepare to file a petition with the General Court for the next session which will update the allowable charges under G.L. c. 255B, §14. The Division will be reluctant to address additional includable charges by opinion.

The conclusions reached in this letter are based solely on the facts presented and are limited to the inclusion of debt cancellation charges as part of a contract subject to G.L. c. 255B. Fact patterns which vary from those presented may result in a different position statement by the Division.

Very truly yours,



Steven L. Antonakes
Commissioner of Banks

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