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Federal Agencies Take Another Shot at GAP Coverage for Buyers Covered by the Military Lending Act

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I have always been a fan of suspenseful entertainment. I really like television shows where it looks like the protagonist is doomed, but then escapes, lands back in trouble, and gets out ... again! So fun.

But this kind of whipsaw action is not so fun when applied to real life. A case in point is *Davidson v. United Auto Credit*, a 2021 case decided by the U.S. District Court for the Eastern District of Virginia. This case involved a motor vehicle retail installment sale in which the plaintiff buyer, who was at that time an active member of the U.S. military, purchased and financed GAP coverage at a cost of $350. The plaintiff's chief complaint was that United Auto Credit Corporation violated the federal Military Lending Act and Department of Defense regulations promulgated thereunder because the RIC failed to disclose the military annual percentage rate and had other features prohibited by the MLA.

Right now, you might be thinking, "Why was this case brought? Didn't we finally determine that GAP can be offered without triggering the MLA disclosure requirements?" That's a great question! And the answer is ... not exactly.

The MLA applies to "consumer credit," a term that now applies very broadly to most kinds of consumer finance transactions. But MLA regulations explicitly exclude a credit transaction that is intended to finance the purchase of a motor vehicle or personal property (I'll call this the "Exclusion"). There has been uncertainty as to whether including the cost of GAP in a vehicle financing transaction would cause the entire transaction to be ineligible for the Exclusion. The DoD has provided guidance on this question. First, in 2016, it issued guidance indicating that the Exclusion was not necessarily lost if the amount financed exceeded the cost of the financed property, but the Exclusion would be lost if the financing was a "hybrid" that included financing for the purchased property and a "cash advance" to the buyer. This guidance didn't directly address GAP, but it was still reasonable to conclude that GAP could be included in transactions with MLA-covered persons (generally, active-duty military and their spouses/dependents).

But, in 2017, the DoD created a crisis when it issued more guidance, this time stating that a credit transaction that includes financing for GAP would not qualify for the Exclusion. This pronouncement caused quite a stir in the auto finance industry. Dealers and lenders generally stopped offering GAP to MLA-covered persons, in part because some were not equipped to provide the MAPR disclosures. But the bigger issue may have been that the MLA arguably does not permit a vehicle financing to be secured by the vehicle's title.

Then, the DoD appeared to reverse itself. In 2020, the DoD withdrew the portion of its 2017 interpretation that included GAP, and there was much rejoicing by the auto industry. But was the GAP question really resolved? When it announced its decision, the DoD noted that it was withdrawing its answer because of "unforeseen technical issues" and, "absent additional analysis, takes no position on any of the arguments or assertions advanced as a basis for withdrawing" its 2017 guidance.

Despite the cryptic nature of the withdrawal, a lot of people reasonably inferred that the DoD's withdrawal of the 2017 guidance meant that GAP could be offered to MLA-covered persons without jeopardizing the Exclusion.

Now let's come back to *Davidson*. The trial court ruled that adding GAP to the RIC now held by United Auto Credit did not make the transaction ineligible for the Exclusion. The judge felt that she was bound to follow the text of the Exclusion, which provided "clear language" that the buyer's transaction was excluded from the MLA. The buyer had argued that the 2016 interpretation (which was unaffected by withdrawal of the 2017 interpretation) would still cause the transaction to be ineligible for the Exclusion because the GAP coverage was unrelated to the purchase of the motor vehicle. The judge found this argument unpersuasive, stating that the GAP coverage was "inextricably" tied to the purchase of the vehicle. Crisis is averted with a well-reasoned opinion from the trial court!

But the next twist in this drama is unfolding now. The *Davidson* case has been appealed to the U.S. Court of Appeals for the Fourth Circuit. And, in January 2022, the Consumer Financial Protection Bureau filed an amicus brief in support of the buyer.

The CFPB takes the position advanced by the buyer, saying that including GAP in vehicle financing provided to an MLA-covered person makes that financing ineligible for the Exclusion. The CFPB makes a number of arguments in support of this position, none of which can be summarized succinctly. One might charitably characterize the CFPB's arguments as "creative." My own view is that the CFPB faces an uphill battle in its effort to get the Fourth Circuit to overturn the trial court on this one.

One area of concern, though, is the fact that the DoD has signed on to the CFPB's amicus brief. In fact, the brief states that the DoD "strongly concurs" with the position taken by the CFPB. So, even if United Auto Credit wins the appeal (as it should), the CFPB's amicus brief has just told us that the DoD does not want GAP offered to MLA-covered persons. It seems unlikely that the DoD would reissue the 2017 guidance that it withdrew in 2020, but the DoD has authority to issue regulations to implement the MLA. Will the DoD draft new rules that take aim at GAP coverage? That, too, seems unlikely. But we thought this MLA drama ended in 2020. Perhaps there is another season left in this series.

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