

States Are Joining the War on Voluntary Protection Products

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When it comes to voluntary protection products, such as guaranteed asset protection, debt cancellation, credit insurance, service contracts, and vehicle protection products, the hottest topic this summer seems to be the Federal Trade Commission's Motor Vehicle Dealers Trade Regulation Rule, which targets "junk fees" and "add-ons" charged in connection with consumer credit transactions. While the FTC's proposed rule is a significant attack, the states also are waging an intensifying war against voluntary protection products. At the state level, battles continue on multiple fronts, with increased focus on voluntary protection products in legislation, regulation, and enforcement. Anyone selling and financing voluntary protection products in connection with consumer credit transactions should be watching the battle lines closely to avoid becoming the next target.

Over the last several years, state legislation has increasingly addressed the sale and financing of voluntary protection products. The most significant trend in state legislation has been the adoption of state laws governing GAP waiver agreements. In 2022, one such bill was introduced in Connecticut (House Bill 5385), although it has not yet been adopted. Additionally, many states have enacted legislation aimed at expanding state law definitions of "service contract" and "vehicle protection product" to include products like road hazard protection, tire and wheel, paint protection, and key fob replacement. The most recent example of this type of legislation is South Dakota Senate Bill 160, effective July 1, 2022, which expressly exempts such products from regulation as insurance. In Alabama, a new law, effective January 1, 2023, provides express authority for motor vehicle protection products, which protect consumers against loss of vehicle value due to theft, damage, obsolescence, depreciation, and other causes. These are examples of legislation that may be favorable to creditors selling and financing products, as the laws provide clarity around how the products are regulated under state law.

However, legislation is also a weapon by which states restrict how and when products are permitted to be offered. For example, legislation currently pending in California (Assembly Bill 1311) would effectively ban installment lenders from financing voluntary protection products in connection with loans to specified servicemembers by providing that a security interest in a motor vehicle is void if the loan funds the purchase of a credit insurance product or credit-related ancillary product. California has also introduced legislation (Assembly Bill 2311) that would impose new GAP refund requirements, cap the amount that can be charged for GAP, and require additional GAP disclosures. Through legislation, many states are undertaking efforts to tighten their controls on GAP requirements. For example, in 2021, Wisconsin (House Bill 8) amended its law to impose new GAP refund requirements. In 2022, Indiana (Senate Bill 383) amended its law to specify that the average retail value for a used motor vehicle that is the subject of a GAP agreement is to be determined by using a third-party valuation service provider customarily relied upon in the used motor vehicle commercial market (versus the

National Automobile Dealers Association average retail value, under current law).

Regulation has also proven to be an effective weapon for the states to use in imposing restrictions on the sale and financing of voluntary protection products. For example, in Massachusetts, the Division of Banks published Opinion Letter 20-005 (February 10, 2022), in which it expressly prohibited GAP waiver administrators from imposing fees for the cancellation of a GAP waiver on consumers under the Retail Instalment Sales of Motor Vehicles chapter. In Virginia, the Bureau of Financial Institutions amended its regulations in 2021 to effectively preclude lenders from financing any ancillary product or service offered in connection with consumer finance loans.

Finally, the deadliest weapon in the states' arsenal is enforcement. At present, Colorado seems to be the most active when it comes to enforcement. In the past two years, the Colorado attorney general has been on an apparent warpath, entering into five settlement agreements with vehicle-secured creditors and GAP administrators that have allegedly failed to provide required GAP refunds. Colorado is not the only active enforcer. Just last week, 18 states joined forces with the FTC to sue a national jewelry retailer, alleging, among other things, that the retailer misrepresented that its protection plan was required to finance purchases and added the plan to purchases without consumers' consent.

The war on voluntary protection products is moving on all fronts, and creditors selling and financing these products are under fire. If you have not done so already, now is the time to build up your defenses. Such defenses may include strong product training to ensure your salespeople understand the products you offer, staying current on recent legal and regulatory developments impacting products, regularly reviewing products for state law compliance, and monitoring product sales practices and customer complaints involving products you have financed. Just as a successful general on the battlefield has a tactical plan, if you sell and finance voluntary protection products in connection with consumer credit transactions, be sure you are at the ready with a strong compliance plan.

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