Q&A from DCUC Military Lending Act Webinar
Tuesday, January 31, 2017

1) **Can you please cover MLA compliance for indirect auto loans? If the rule excludes purchase money transactions, how would a dealer be responsible?**

Many times an auto purchase transaction at a dealership will include additional cash-out to cover an existing negative equity balance on the vehicle being traded in. In this situation, the purchase transaction would lose its exemption to the MLA.

Question #2 of the DOD's Interpretive Rule issued on August 23, 2016 states that "any credit transaction that provides purchase money secured financing along with additional cash-out financing is not eligible for the exception under §232.3." In addition, in its updated examination procedures for the MLA, the Consumer Financial Protection Bureau states "a transaction where a creditor simultaneously extends an additional cash advance beyond the purchase price of the securing personal property or motor vehicle does not fall under these exceptions."

2) **Is an indirect auto loan that includes an advance to cover negative equity on the vehicle being traded in covered by the MLA?**

Yes, the loan would be subject to the requirements of the MLA. See the answer to question #1 above.

3) **If the member takes additional cash out to cover the negative equity amount on their trade in, is the transaction no longer exempt from the MLA?**

Correct. Any loan that provides for additional cash out beyond the purchase price of the securing motor vehicle would not qualify for the exemption to the MLA. See the answer to question #1 above.

4) **Suppose a member has $3,000 in negative equity on their trade in, but the new vehicle has a $3,000 rebate, so there is no advance of money for negative equity. Does the MLA rule apply?**

The MLA final rule and the DOD's Interpretive Rule does not conclusively address this issue; therefore, additional guidance is being sought. As a result, CUNA is unable to provide definitive legal advice on such a fact specific hypothetical scenario.

However, the conservative answer to this question is that the MLA rule would likely apply in this scenario. This is based on the following:

- Question #2 of the DOD's Interpretive Rule which provides that "any credit transaction that provides purchase money secured financing along with additional cash-out financing is not eligible for the exception under §232.3."
- The Consumer Financial Protection Bureau's updated examination procedures which provides "a transaction where a creditor simultaneously extends an additional cash advance beyond the purchase price of the securing personal property or motor vehicle does not fall under these exceptions."

Consider the hypothetical posed: the purchase price of the new motor vehicle is $18,000. However, a $3,000 rebate is offered. If $18,000 is advanced to the member ($15,000 for the new motor vehicle and $3,000 to cover the negative equity balance existing on the vehicle being traded in), it would seem that no new money is being advanced beyond the purchase price. However, the actual purchase price in this scenario is $15,000 ($18,000 sale price less the $3,000 rebate on the new motor vehicle). So $3,000 in additional cash-out financing beyond the purchase price and unrelated to the motor vehicle being purchased is being advanced. This is because the additional $3,000 advanced is related to the motor vehicle being traded in and NOT the motor vehicle being purchased.

As a result, the transaction is not likely to qualify for the purchase money exemption found in §232.3.

5) **What if the dealer discounts the new automobile so that any outstanding negative equity is absorbed in the purchase price and the loan amount is less than the MSRP of the automobile being purchased?**

See the answer to question #4 above.

In the event the dealer discounts the motor vehicle being purchased, the purchase price becomes the sale price less the discount.

Any additional funds advanced beyond the new net purchase price is likely to be considered cash-out financing unrelated to the purchase. As a result, the loan will likely no longer qualify for the purchase money exemption found in §232.3.

6) **Would an extended warranty be considered additional cash out financing on an indirect auto loan purchase?**

Probably not. If the extended warranty sold covers the motor vehicle being purchased, the extended warranty would not likely be considered "cash-out". Thus, the purchase of an extended warranty alone should not cause the transaction to lose its exemption to the MLA.

This is based on the language found in question #2 in the DOD's Interpretive Rule. It states the following: "A hybrid purchase money and cash advance loan is not expressly intended to finance the purchase of the property, because the loan provides additional financing that is *unrelated to the purchase.*" This seems to indicate that additional financing above and beyond the purchase price, *related to the purchase* (e.g. extended warranty, GAP, etc.) would not be considered cash-out. Thus, the purchase of an extended warranty covering the motor vehicle being purchased would alone NOT likely cause the transaction to lose its exemption to the MLA.

7) **In the event a member decides to purchase GAP, credit life and/or disability or an extended warranty, is the transaction no longer exempt from the MLA?**

Additional financing, above and beyond the purchase price but *related to the purchase* (e.g. GAP, extended warranty, etc.) is not likely to be considered "cash-out". As a result, if these products are purchased in connection with the motor vehicle being purchased, the transaction will likely remain exempt from the MLA's requirements under the purchase money exemption provided for in §232.3.

See the answer to question #6 above.

8) **If GAP and an extended warranty are purchased at the dealership, is the loan no longer exempt from the MLA?**

Additional financing, above and beyond the purchase price but related to the purchase (e.g. GAP, extended warranty, etc.) is not likely to be considered "cash-out". As a result, if these products are purchased in connection with the motor vehicle being purchased, the transaction will likely remain exempt from the MLA's requirements under the purchase money exemption provided for in §232.3.

See the answer to question #6 above.

9) **If the member takes out a personal loan to purchase ancillary products which could not be financed along with the vehicle purchase, is this considered a covered loan or is it exempt since it is in conjunction with the purchase of the vehicle?**

The MLA requirements apply to all consumer credit which is credit offered or extended to a covered borrower primarily for personal, family or household purposes. The exemption related to a motor vehicle purchase requires that the transaction be expressly intended to finance the purchase of a motor vehicle and *secured by the motor vehicle* being purchased.

As a result, a separate personal loan to finance the purchase of ancillary products would no longer qualify for the exemption because that loan would not be secured by the motor vehicle being purchased.

10) If the member takes additional cash out to cover sales tax, is the transaction no longer exempt from the MLA?

Additional financing, above and beyond the purchase price but related to the purchase (e.g. sales tax) is not likely to be considered "cash-out". As a result, if sales tax on the motor vehicle being purchased is included in the loan, the transaction will likely remain exempt from the MLA's requirements under the purchase money exemption provided for in §232.3.

See the answer to question #6 above.

11) If a wrong amount was added for an ancillary product when calculating the MAPR for a closed-end loan, what steps may the credit union take to correct this error following consummation?

The MLA rule doesn't provide any guidance on situations like this or on how errors should be corrected.

While your question doesn't indicate the exact nature of the error, if the charge for the ancillary product was overstated, thus resulting in an incorrect MAPR of over 36%, you should document the correct MAPR as being less than the 36% limit. However, if the charge for the ancillary product was understated, and the correct MAPR would actually be over the 36% limit, you should issue a credit to the borrower for the amount necessary to reduce the MAPR to below the 36% limit.

Remember that §232.4(b) provides that a creditor may not impose an MAPR of greater than 36% in connection with the extension of a closed-end consumer credit transaction or during any billing cycle of an open-end consumer credit transaction.

12) Does consummation occur at the time the member signs the loan contract or at the time the credit union disburses loan proceeds?

When consummation occurs is a matter of state law. Some states provide that consummation occurs when the loan documentation is signed. Other states provide that consummation occurs when the loan is funded. Please seek input from local counsel on how consummation is defined in your jurisdiction.

13) Can the credit union send the statement of the MAPR prior to funding?

§232.6 of the MLA provides that required disclosures must be provided "before or at the time the borrower becomes obligated on the transaction or establishes an account for the consumer credit." So yes, the statement of MAPR can and likely *should* be provided to the borrower prior to funding.

14) **Are we not able to exercise our statutory lien right against an account that was existing at the time of consummation of an MLA covered loan if the member defaults on the MLA covered transaction?**

DOD's Interpretive Rule has created further confusion on this subject; however, it is our opinion that you may NOT exercise a statutory lien right against funds that were already on deposit at the time of consummation.

Question #18 of the Interpretive Rule provides that the MLA does not impede a creditor from exercising a statutory right to take a security interest in funds deposited in an account at any time, provided that *the creditor complies with the MLA regulation.* §232.3 of the MLA states that a creditor may only take a security interest in funds deposited *after the extension of credit in an account established in connection with the consumer credit transaction.* Therefore, if the member defaults on the MLA covered loan, this limitation would prevent the attachment of a security interest to funds deposited prior to the extension of credit.

15) **How do you suggest we handle calculating the MAPR on an open-end loan (credit card or LOC) if we cannot calculate an accurate MAPR until the end of the billing cycle; however, any refund of fees would be done after the billing cycle is closed. Would we be considered in violation of the 36% MAPR restriction for a period of time? Would this violation be cured by the refund to the borrower?**

§232.4(b) provides that a creditor may not impose an MAPR of greater than 36% in connection with the extension of a closed-end consumer credit transaction or during any billing cycle of an open-end consumer credit transaction.

Question #3 from the DOD's Interpretive Rule states that creditors are permitted to waive fees or periodic charges *at the end of a billing cycle or earlier* for open-end credit in order to prevent a borrower from being assessed an MAPR in excess of 36%. This language suggests that the credit union should calculate the MAPR earlier in the billing cycle to determine what fees and/or periodic charges must be waived (if applicable) prior to the end of the billing cycle to reduce the MAPR to 36% or below.