STATE OF MICHIGAN
DEPARTMENT OF LABOR AND ECONOMIC GROWTH
OFFICE OF FINANCIAL AND INSURANCE REGULATION

Bulletin 2008-08-BT

In the Matter of:

The sale of Debt Cancellation Contracts and Debt Suspension Agreements by Depository Institutions

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Issued and entered
this 11 day of July 2008
by Ken Ross
Commissioner

This bulletin supersedes Bulletin 2004-01.

On June 18, 2004, the Commissioner issued a declaratory ruling in the matter of the sale of debt cancellation contracts (DCC) and debt suspension agreements (DSA) by depository institutions. The Commissioner ruled that these institutions may sell these contracts and agreements and may do so without being subject to the Insurance Code of 1956, as amended ("the Code"), MCL 500.100 et seq. The ruling was based upon the application of the principal object and purpose test. Loan agreements of depository institutions do not become subject to the Code due to the sale of related DCCs and DSAs. The principal object and purpose of a loan agreement is the loan itself, not insurance.

The declaratory ruling (No. 04-053-M) may be seen in its entirety at the Office of Financial and Insurance Regulation (OFIR) website:

http://www.michigan.gov/documents/DCCDecRul5_94839_7.pdf

The declaratory ruling prospectively changed and superseded Declaratory Ruling No. 98-105-M.

Nationally chartered banks, credit unions, and thrifts are authorized to sell DCCs and DSAs. The Comptroller of the Currency (OCC) issued rules that took effect in June, 2003 that regulate national banks in their sale of DCCs and DSAs (See 12 CFR Part 37).

When Declaratory Ruling No. 04-053-M was issued, the Commissioner also scrutinized the OCC rules and concluded that DCCs and DSAs offered by state-chartered depository institutions in connection with extensions of credit that conform with the standards identified in the OCC rules would be deemed by OFIR to be provided in a safe and sound manner.

Bulletin 2004-01 was issued to reflect that decision. Regarding the sale of DCCs and DSAs, the Commissioner concurs with the Comptroller of the Currency:

> A...bank must manage the risks associated with debt cancellation contracts and debt suspension agreements in accordance with safe and sound banking principles. Accordingly, a...bank must establish and maintain effective risk management and control processes over its debt cancellation and debt suspension agreements. Such processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with the products. A bank also should assess the adequacy of its internal control and risk mitigation activities in view of the nature and scope of its debt cancellation contract and debt suspension agreement programs (12 CFR 37.8).

An inquiry from an interested party prompted the Commissioner to review OCC rule § 37.5, which says in pertinent part:

> Except as provided in § 37.3(c)(2) [which prohibits a single or lump sum payment for a DCC or DSA where the debt is a residential mortgage loan], a bank may offer a customer the option of paying the fee for a contract in a single payment, provided the bank also offers the customer a *bona fide* option of paying the fee for that contract in monthly or other periodic payments.

The Commissioner has concluded that state-chartered depository institutions do not have to offer a customer the option of paying the fee for a DCC in monthly or other periodic payments when the product offered is what is commonly known as GAP ("guarantee auto" or "guaranteed asset" protection) coverage or waiver. As used in this Bulletin, GAP is a type of DCC where the underlying loan is for a motor vehicle and is intended to cover any difference between the insurance settlement and the balance remaining on the loan if the motor vehicle is stolen, damaged beyond repair, or otherwise declared a total loss. For GAP products only, it is not considered an unsafe or unsound practice for a state-chartered depository institution to offer customers only a single-payment debt cancellation agreement.

Other than this exception, state-chartered depository institutions seeking to sell DCCs and DSAs should continue to look to the standards in 12 CFR Part 37 as a model for the safe and sound provision of these products. They should continue to:

1. Conduct preliminary and ongoing due diligence reviews of program vendors.

2. Evaluate the substance of a program as well as the form in which it is presented.

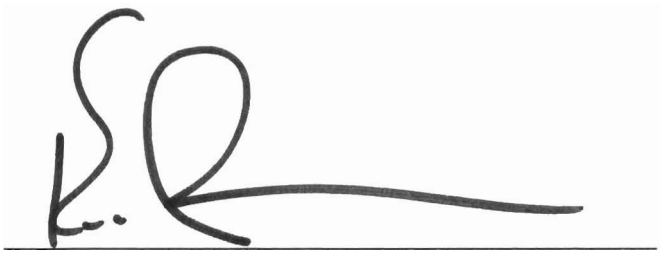
3. Thoroughly analyze the legal, supervisory, and public policy issues set forth in 12 CFR Part 37 and this Bulletin in determining whether to offer or continue to offer debt cancellation contracts and debt suspension agreements.

4. Obtain guidance from competent legal counsel.

Any questions regarding this bulletin should be directed to:

Office of Financial and Insurance Regulation
Office of General Counsel
611 West Ottawa Street
P.O. Box 30220
Lansing, Michigan 48909-7720

Phone: (517) 373-0435
Toll Free: (877) 999-6442



Ken Ross
Commissioner
Office of Financial and Insurance Regulation