STATE OF MICHIGAN

DEPARTMENT OF COMMERCE

FINANCIAL INSTITUTIONS BUREAU

IN RE: REQUEST BY LOCAL FINANCE CORPORATION FOR A DECLARATORY RULING ON THE APPLICABILITY OF MCLA 493.15 TO THE PURCHASE OF REGULATORY LOAN CONTRACTS FROM OTHER REGULATORY LOAN LICENSEES

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DECISION

Statement of Facts

Local Finance Corporation (LFC) a licensee under 1939 PA 21 (The Regulatory Loan Act) MCLA 493.1 acquired certain small loan contracts from Barclays American/Financial Corporation. These contracts were acquired in September, 1980, and were initially held by the home office of LFC in Indiana. On April 20, 1981, an examination of an office of LFC located at 806 West Chicago Road, Sturgis, Michigan, was conducted by the Consumer Finance Division (CFD) of the Financial Institutions Bureau (FIB). Examination of the records at the Sturgis office revealed five cases where persons were obligors on two separate contracts. In each case, the second contract resulted from the acquisition of contracts from Barclays American/Financial Corporation. The aggregate indebtedness in each case exceeded the $3,000 ceiling in the Regulatory Loan Act. The examination also showed that the branch office renewed or refinanced loans in each case subsequent to acquisition without combining the two contracts into one loan. LFC continued to charge the five individuals interest rates permitted by the Regulatory Loan Act on each loan contract.

In a letter dated May 21, 1981, Mr. A. J. Trierweiler, Director of the CFD, cited LFC's Sturgis office for violations resulting from its failure to combine loans for each of five individuals in conjunction with the renewal or refinancing of their contracts. Mr. Trierweiler's letter which was addressed to Mr. Frank Iannelli, Manager of LFC in Sturgis, requested that the loans to each of the five persons be combined into one obligation per individual, and the finance charge be reduced to 7% simple interest because the combined obligations would exceed $3,000. Mr. Walter Allen, Jr., Vice President of LFC in Marion, Indiana, postponed any action on the loans until he had a chance to review all the circumstances surrounding the alleged violations. After review,

Mr. Allen reported that he had, under protest, combined the indebtedness for the five individuals and reduced the finance charge to 7% per annum simple interest from the date of the violation.

On Thursday, October 8, 1981, Mr. William J. Perrone of the law firm of McLellan, Schlaybaugh & Whitbeck met with Commissioner Martha R. Seger, Chief Deputy Commissioner Russell S. Kropschot, Deputy Commissioner Murray E. Brown, and Director of Office of Regulation, Gary K. Mielock in the office of FIB. Mr. Perrone indicated that he represented LFC, and took issue with the position taken by Mr. Trierweiler in the alleged violations at the Sturgis office. In that meeting, Mr. Perrone delivered copies of materials representing communications between Mr. Trierweiler and Mr. Allen. Mr. Perrone also gave FIB officials a copy of a letter from Mr. Richard McLellan of the law firm to Mr. Richard Marcus of the Michigan Consumer Finance Association. That letter explained the legal basis for LFC's disagreement with the CFD's interpretation of section 15 of the Regulatory Loan Act, MCLA 493.15. Mr. Perrone declared his intention to request a declaratory ruling from the Bureau on the legality of the position taken by the CFD.

In an October 9, 1981 letter addressed to Commissioner Martha R. Seger, Mr. Perrone requested a declaratory ruling on the applicability of MCLA 493.15 to the purchase of regulatory loan contracts by a licensee under 1939 PA 21, as amended. The request was made pursuant to section 63 of the Administrative Procedures Act, 1969 PA 306, MCLA 24.63. The letter requested an FIB ruling on whether the bona fide purchase of a regulatory loan contract falls within the exemption provided in MCLA 493.15.

Issues

LFC argues that:

1. The making of a loan by a regulatory loan licensee constitutes a service as that term is used in MCLA 493.15.

2. Regulatory loan contracts acquired by a licensee are therefore exempt from the restrictions and limitations set forth in 493.15 by virtue of the exemptive language in that section.

3. Regulatory loan contracts acquired by a licensee need not be aggregated with direct loans made by the licensee.

Statutes

At issue in this request for a declaratory ruling are certain sections of the Regulatory Loan Act. MCLA 493.15 of the act states the following:

> "A licensee shall not directly or indirectly charge, contract for, or receive an interest, discount, or consideration greater than the lender would be permitted by law to charge if the licensee were not licensed under this act upon a part or all of any aggregate indebtedness of the same borrower, or upon the loan, use, or forbearance of money, goods, or things in action, or upon the loan, use, or sale of credit, of the amount or value of more than the regulatory loan ceiling. This prohibition shall also apply to a licensee who permits a person, as borrower or an indorser, guarantor, or surety for a borrower or otherwise, to owe directly or contingently or both to the licensee at any time a sum of more than the regulatory loan ceiling for principal. If a licensee acquires, directly or indirectly, by purchase or discount the bona fide obligation of a purchaser of goods or services from the person selling the goods or rendering the services, then the amount of the purchased or discounted indebtedness to the licensee shall not be included in computing the aggregate indebtedness of the borrower to the licensee for the purposes of this prohibition."

Other statutory language which is relevant to this decision is Subsection (2) of MCLA 493.13 which states that:

> "A licensee shall not induce or permit a borrower to split up or divide a loan. A licensee shall not induce or permit a person to become obligated, directly or contingently, or both, under more than 1 contract of loan at the same time, for the purpose or with the result of obtaining a higher rate of charge than would otherwise be permitted by this section."

Rule R 487.81 of the Commissioner's Rules also has some bearing on the issue. Paragraph (5) of this rule states:—

> "When an additional loan is made to a borrower who has a loan outstanding, the unpaid balance of the existing loan and the additional loan shall be consolidated into the new loan."

Discussion of Law

The FIB does not dispute the right or ability of a licensee to acquire regulatory loan contracts from other licensees. The CFD permits such acquisitions and also allows the licensee to charge interest rates allowed by the Regulatory Loan Act on each contract if the acquisition results in a licensee holding two contracts for one borrower. However, if a borrower having two contracts with a licensee refinances or renews either of the two contracts, the CFD requires that the contracts be combined into one loan, and if the combined loan exceeds $3,000, the finance charge be reduced to 7% per annum. LFC, through its attorney, argues that the acquisition of such contracts would fall within the exemptive language contained in MCLA 493.15, and that under no circumstances should

the CFD require that acquired loans be aggregated with any direct loans to the same obligor.

LFC argues that a regulatory loan made by another licensee constitutes a service and, therefore, should be grouped together with sales finance contracts in the exemption provided by MCLA 493.15. The CFD has interpreted such exemptive language as including only installment contracts purchased from a seller of goods or services. Such contracts would generally be purchased from a dealer or seller operating under the Motor Vehicle Sales Finance Act MCLA 492.101 et seq, the Retail Installment Sales Act MCLA 445.851 et seq, or the Home Improvement Finance Act MCLA 445.1101 et seq.

Prior to 1963, the exemptive language in MCLA 493.15 only made reference to tangible goods. The language was amended in 1963 to include the word 'services' in the exemption. In the State Banking Department analysis of House Bill 85, which brought about the change, the Department states:

> "At present only contracts covering the sale of tangible goods purchased from a dealer are exempt when computing the aggregate indebtedness. In other words, if a person has a direct loan from the licensee in the amount of $500.00, the maximum, and the licensee purchases an installment contract entered into by such person with a bona fide dealer in tangible goods, such contract would not be added to the direct loan resulting in an excessive loan.
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> It is proposed that contracts entered into covering services such as hospital, medical, repair, health, travel, etc., be placed in the same category as contracts covering the purchase of goods, and that contracts covering services purchased from those rendering such services, be also exempt when computing the aggregate indebtedness of a borrower."

After review of this analysis, it is my position that the intent of the Legislature in adopting the amendment was to permit the purchase of installment sale contracts for the sale of services as well as installment contracts for the sale of tangible goods, without the requirement that such contracts be included in determining the aggregate indebtedness of a borrower.

The position of LFC is that purchased regulatory loan contracts are totally exempt from the requirements of MCLA 493.15. If the CFD had adopted this position without restrictions or modifications, a licensee could easily circumvent the provision of the Regulatory Loan Act which limits the indebtedness of one borrower to $3,000. Licensees could acquire contracts from other licensees, and then make new loans to the obligors under the acquired contracts without aggregating the indebtedness as required by MCLA 493.15 and R 487.81(5)

of the Commissioner's Rules. This interpretation would, in effect, defeat one of the main purposes of the Regulatory Loan Act, that being to limit the indebtedness to any one borrower to the regulatory loan ceiling.

For the reasons set forth above, it is my interpretation that the purchase of regulatory loan contracts from other regulatory loan licensees does not fall within the exemption provided in MCLA 493.15.

There is no provision in the Regulatory Loan Act which prohibits a licensee from purchasing regulatory loan contracts from another licensee. Any business entity or natural person whether licensed under the Regulatory Loan Act or not may purchase existing regulatory loan contracts. If acquisition of contracts results in a licensee holding two regulatory loan contracts for one borrower (one acquired and one involving a previously made direct loan), and the acquisition was not made with the intent to evade the Regulatory Loan Act, the licensee need not aggregate the contracts since the acquisition of a regulatory loan contract does not constitute the making of an "additional loan" within the meaning of R 487.81(5), supra. Thus the acquisition of a regulatory loan contract is handled in a manner similar to the acquisition of a sales finance contract. However, if a licensee holds two regulatory loan contracts for a borrower, one of which was acquired, and the licensee wishes to refinance or renew either of the contracts, this would constitute the making of an "additional loan" to a borrower with a "loan outstanding" within the meaning of R 487.81(5) supra. At this point, the unpaid balance of the existing loan and the additional loan must be consolidated. This consolidation would not be required, however, if the acquired contract were a sales finance contract instead of a regulatory loan contract. In this case, if the licensee wished to refinance the regulatory loan contract, it could be achieved without aggregation of the refinanced regulatory loan contract and the sales finance contract. This results from the specific exemption afforded sales finance contracts under MCLA 493.15, supra. A sales finance contract, therefore, would not be regarded as "a loan outstanding" within the meaning of that phrase as it is used in R 487.81(5), supra.

For the reasons set forth above, it is my interpretation that a regulatory loan licensee which acquires a regulatory loan contract can hold the acquired contract separate from any direct loan made prior to the acquisition to the obligor on the acquired contract, and can collect interest permitted by the

Regulatory Loan Act on both contracts. If the licensee renews or refinances either of the two contracts, both contracts must be consolidated, and if the total indebtedness exceeds $3,000, the interest rate on the consolidated contract must be reduced to 7% per annum, the interest ceiling set forth in the general Usury Act, MCLA 438.31. This conclusion stems from the fact that MCLA 493.15 prohibits a licensee from directly or indirectly charging an interest rate greater than the lender would be permitted by law to charge if the licensee were not licensed under the Regulatory Loan Act.

Martha R. Seger

Martha R. Seger, Ph.D., Commissioner
Financial Institutions Bureau
Department of Commerce

DATE:
10-23-81