A nonprofit organization dedicated to making energy improvements easy and affordable.

Overview of the Michigan Municipal Utility Residential Clean Energy Program Act (PA 408 of 2014)

In December of 2014 the Michigan Legislature passed House Bill 5397, which enables municipalities that have municipal electric utilities to establish a residential clean energy program. In the same month, Governor Rick Snyder signed the bill into law as Public Act 408 of 2014 (see Appendix A). Under a residential clean energy program, a municipality may enter into a contract with a residential property owner to finance or refinance one or more energy projects on the property. The law stipulates the way in which the programs can be administered, the improvements that are eligible for financing, the requirements regarding the financial product offered for improvements, and program design requirements and options. A summary of the bill is provided below.

PROGRAM ADMINISTRATION

How the program is established: Following prescribed procedures (adopting a resolution of intent, holding a public hearing, adopting a resolution or ordinance briefly describing the program and its intent, developing and publicly posting a report describing the program and requirements in detail), a municipality whose residents are served by a municipal utility may establish a residential clean energy program.

How the program is administered: A residential clean energy program can be administered by a nonprofit corporation (including the municipal utility or other nonprofit organizations).

Compliance with lending laws: The program administrator must comply with all applicable state and federal lending laws (see Appendix B for applicable laws)

ELIGIBLE IMPROVEMENTS

A residential clean energy program can finance or refinance residential energy projects. Energy projects include the installation or modification of an energy efficiency improvement or the acquisition, installation, or improvement of a renewable energy system. Eligible equipment includes:

- Insulation in walls, roofs, floors, foundations, or heating and cooling distribution systems.
- Storm windows and doors; multi-glazed windows and doors; heat-absorbing or heat-reflecting glazed and coated window and door systems; and additional glazing, reductions in glass area, and other window and door system modifications to reduce energy consumption.
- Automated energy control systems.
- Heating, ventilating, or air-conditioning and distribution system modifications or replacements.
- Air sealing, caulking, and weather-stripping.
- Lighting fixtures that reduce the lighting system's energy use.
- Energy recovery systems.
- Day lighting systems.
- Electrical wiring or outlets to charge a motor vehicle that is fully or partially powered by electricity.
- Measures to reduce water usage or to increase the efficiency of water usage.
- Any other installation or modification of equipment, devices, or materials approved as a utility cost-savings measure by the governing body.

A broad interpretation of the law would suggest that non-energy measures (e.g., asbestos removal, below-code wiring) are eligible for financing, but they would need to be modifications that are necessary to allow for the energy improvement to be made.

FINANCIAL PRODUCT REQUIREMENTS

Who can originate and service the loans: Loans can be originated by the municipal electric utility, a nonprofit corporation, or commercial lenders (directly or through a nonprofit). The loan capital can be provided by the sale of bonds, by funds available to the municipality through any other source, and by owner-arranged financing. Loans can be serviced by the utility or commercial lender.

Financing terms: If a nonprofit (municipal electric utility or other nonprofit) provides the financing, the maximum interest rate that can be charged is prime (currently about 3 percent) plus 4 percent, for a total rate cap of around 7 percent. The maximum loan term is 15 years or the useful life of the energy project, whichever is less.

Loan treatment, consequence for nonpayment, and transferability: The amount financed can be treated as part of the charges for electric service, and paid monthly as a per-meter charge on the utility bill. Consequence for nonpayment is the same as for other electric service charges: the balance owed will be treated as a lien, and service can be shut off for nonpayment. If notice of the loan is recorded with the register of deeds, the payment obligation transfers to subsequent occupants at the time of property transfer.

What can be financed: Financing includes the cost of material and labor necessary to complete the energy project, as well as audit costs, permit fees, inspection fees, application and administration fees, bank fees, and all other fees that may be incurred by the property owner to complete the energy project.

PROGRAM DESIGN ELEMENTS

The law **requires** certain program design elements:

- The only eligible borrowers are private owners of **residential** (4 units or less) properties served by a municipal utility.
- An **audit** is required on every project, which includes an evaluation of energy performance by a qualified person using diagnostic equipment and complying with the standards of the American National Standards Institute. Each audit must include an energy model and cost-benefit analysis for improvements.
- **Quality assurance** must be conducted on every project, which includes verifying that the improvements were installed properly and operate as intended.

Other design elements are left to the discretion of the municipality:

- Program administrator: Programs can be administered by the utility or other nonprofits.
- Eligible improvements: A list of eligible measures is provided in the law, but not all are required. Program goals will dictate which measures will be eligible.
- Loan origination and servicing: Loan origination and servicing can be done by the utility, a nonprofit, or a commercial lender.
- Capital source: The loan capital can be provided by the sale of bonds, by funds available to the municipality through any other source, and by owner-arranged financing.

- Underwriting criteria: The law is not prescriptive about the metrics to be used.
- Disconnection for nonpayment and transferability: The law allows for this, but does not require it.

Appendix A: PA 408 of 2014

Appendix B: Lending laws applicable to on-bill financing programs

Note: This memo was created with investor-owned utilities in mind, but the same laws would apply to municipal utilities.

Memorandum

TO: Council of Michigan Foundations

FROM: Bodman PLC

DATE: May 5, 2014

SUBJECT: Michigan and Federal Consumer Finance Laws

The Council of Michigan Foundations ("Council") has asked what federal and Michigan consumer finance laws apply to a non-municipal utility company ("Company") when it originates an unsecured closed-end loan to an existing consumer customer for the sole purpose of making energy efficient home improvements. The consumer customer would select a third party, unrelated to the Company, to perform the home improvements. The Company would only make loans in Michigan to the Company's existing Michigan consumer customers. The Company would charge interest on the loans. The amounts owed for the loan would not become a lien on the customer's or any consumer's property, including the customer's real property.

In response to the Council's request, this memorandum summarizes the general Michigan and federal consumer finance laws that are likely to apply to the Company's origination of closed-end, unsecured consumer loans in Michigan to Michigan residents. The memorandum only contains a summary of the statutes and regulations. If the Council would like additional information regarding any requirements or prohibitions, including any analysis of cases or other authorities interpreting any statute or regulation, we can provide the additional information upon request. The Council can also find additional details in the statutes and regulations cited in this memorandum.

This memorandum does not include a description of all laws and regulations that could apply to activities related to originating the proposed loans, such as servicing, collection, advertising, certain methods of communication, *etc.* Additionally, the memorandum only summarizes generally applicable Michigan and federal consumer finance laws. It does not include any description of any other laws or regulations. For example, it does not include a description of any laws, regulations or requirements specific to a utility company or address a utility company's general ability to lend or discontinue utility services due to non-payment of the proposed loans.

This memorandum is being provided to the Council for its use only. No other party is entitled to rely on this memorandum.

Equal Credit Opportunity Act

The Equal Credit Opportunity Act ("ECOA"), which is primarily a federal anti-discrimination statute, imposes certain requirements on and prohibits certain conduct by a "creditor." ECOA defines "creditor" as "any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal or continuation of credit; or any assignee of an original creditor who participates in the decision to extend, renew or continue credit." 15 USC 1691a(e). Credit "means the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment or to purchase property or services and defer payment therefor." 15 USC 1691a(d). Regulation B, the regulation that implements ECOA, includes a limited exception for certain transactions. For example, certain provisions of ECOA and Regulation B do not apply to "public utilities credit," which is an extension of credit that involves a "public utility service provided through pipe, wire or other connected facility, or radio or similar transaction if the charges, delayed payment and any discount are filed with or regulated by a government unit." 12 CFR 1002.3. The exception only applies to credit for the purchase of the utility service. Credit provided by a public utility for some other purpose, such as financing insulation or other home improvements, is not within the exception. Comment to 1002.3-1. There is also an exception to some requirements for so-called incidental credit. However, the loans would not be incidental credit because the Company would charge interest.[1] See 12 CFR 1002.3(c).

The exact requirements and prohibitions that apply to a creditor depend on the type of credit that the creditor offers. Below, we summarize the requirements and prohibitions that may apply to the unsecured, closed-end consumer loans that the Company proposes to make.

Generally, ECOA and Regulation B prohibit discrimination[2] on a "prohibited basis" with respect to any aspect of a credit transaction, which can include advertising, originating, administering, or collecting a loan as well as taking a prohibited basis into account in any system of evaluating an applicant[3] for a loan. 12 CFR 1002.4, .6. "Prohibited basis" means race, color, religion, national origin, sex, marital status, age (provided the person has the capacity to contract), the fact that the part of an applicant's income derives from public assistance, or that the applicant has exercised any right under the Consumer Credit Protection Act or certain state laws. 12 CFR 1002.2(z). Except as specifically allowed in Regulation B, the Company cannot require the signature of an applicant's spouse or any other person (other than a joint applicant) on any credit instrument if the applicant qualifies under the creditor's standards of creditworthiness. 12 CFR 1002.7.

In order to limit unlawful discrimination, ECOA and Regulation B would prohibit the Company from asking certain questions or obtaining certain information. The Company would not be able to request information or ask questions regarding the race, color, religion, national origin, or sex of an applicant or any other person in connection with the loans. 12 CFR 1002.5. The Company would be prohibited from asking whether income is derived from alimony, child support, or separate maintenance unless the Company

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[1] Even if the Company did not charge interest, the loans would not be incidental credit if the loan agreement would allow the customer to repay the loan in more than four installments.

[2] Regulators and some courts recognize both disparate impact and disparate treatment claims under ECOA. Therefore, even if a policy is facially neutral, it might be considered discriminatory. Additionally, under Regulation B, a creditor cannot discourage applicants on a prohibited basis.

[3] An applicant includes any person who requests or who has received an extension of credit, and can include a guarantor. 12 CFR 1002.2(f).

disclosed to the applicant that such income does not need to be revealed if the applicant does not want it considered in determining creditworthiness. The Company would be prohibited from asking questions about childbearing or the applicant's spouse. However, the Company could ask whether the spouse will be contractually liable on the loan, whether the applicant is relying on the spouse's income for repayment, or if the applicant is relying on alimony, child support, or maintenance payments from a spouse or former spouse as a basis for repayment. Additionally, if the applicant applied for the unsecured loan in his or her sole name, the Company could not ask about marital status. Otherwise, the Company could only ask if the applicant is married, unmarried or separated. 12 CFR 1002.5.

ECOA and Regulation B require notification regarding certain actions. They require a creditor to notify an applicant within:

(1) Thirty days after receiving a completed application. The notice must inform the applicant whether the creditor is approving the application, making a counter offer or taking an adverse action, such as denying the application. An "application" is an "oral or written request for an extension of credit that is made in accordance with procedures used by a creditor for the type of credit requested." 12 CFR 1002.2(f). A "completed application" is "an application in connection with which a creditor has received all the information that the creditor regularly obtains and considers in evaluating applications for the amount and type of credit requested (including, but not limited to, credit reports, any additional information requested from the applicant, and any approvals or reports by governmental agencies or other persons that are necessary to guarantee, insure, or provide security for the credit or collateral)." *Id.*

(2) Thirty days after taking adverse action on an incomplete application, unless the creditor has notified the applicant (in accordance with Regulation B) that the application is incomplete, specified the information needed to complete the application, designated a reasonable time to provide the information, and notified the applicant that the failure to provide the information will result in the creditor giving the application no further consideration.

(3) Thirty days of taking adverse action on an existing account.

(4) Ninety days after notifying an applicant of a counteroffer if the applicant does not expressly accept the counteroffer. 12 CFR 1002.9.

If the Company takes an adverse action, it would be required to provide written notice of the action taken. The notice would have to include either a statement of the specific reasons for the action taken or a statement of the applicant's right to receive a statement of the specific reasons within thirty days as well as other required information. See 12 CFR 1002.9(a)(2). There are model forms that the Company could use for this purpose.

Regulation B includes additional provisions on allowing the use of certain names, 12 CFR 1002.7, and the furnishing of credit information, including furnishing information to consumer reporting agencies, 12 CFR 1002.10. The Company would also need to comply with these provisions if they are applicable to the Company's activities.

Regulation B requires that the Company retain loan applications, notices of action taken, and other records. See 12 CFR 1002.12 for exact requirements.[4]

Truth in Lending Act

The Truth in Lending Act ("TILA"), which is primarily a federal disclosure statute, and its implementing regulation, Regulation Z, apply to a person who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments, unless the credit is exempted from coverage. 15 USC 1602(g). Potentially relevant exemptions to coverage include exemptions for certain loans over an established dollar amount and public utility credit. If the Company made an unsecured, closed-end home improvement loan and the amount of credit extended exceeded the applicable threshold (currently $53,500), the credit would not be subject to TILA or Regulation Z. However, the proposed loans will not qualify for the public utility credit exemption because the loans are being used to finance home improvements, not for the purpose of providing utility services such as electricity. 12 CFR 1026.3(c).

TILA and Regulation Z include different requirements for open-end and closed-end consumer credit transactions. They also include different requirements for transactions that are secured by real property or a dwelling and transactions that are not and special provisions for educational loans. Because the proposed loans would be unsecured, closed-end consumer credit transactions and would not be educational loans, we have only addressed the requirements for unsecured, closed-end consumer credit transactions.

For loans subject to TILA and Regulation Z, the Company would be required to disclose certain information to borrowers prior to consummation of the loans. The disclosures must be clear and conspicuous, written, in a form that the borrowers can keep (unless the Company provided electronic disclosures in compliance with the Electronic Signatures in Global and National Commerce Act), and include the information required under TILA and Regulation Z. The required disclosures would include the name of the Company, amount financed, finance charge, annual percentage rate, whether or not a variable rate applies and if so certain additional information related to the variable rate, a payment schedule, total of payments, whether or not the loan includes a demand feature, any prepayment penalty, any late payment charge, information on insurance and debt cancellation (as applicable), a contract reference, assumption policy, and whether or not a deposit is required. 12 CFR 1026.18.

TILA and Regulation Z also require that any terms included in advertisements be terms that are actually available. Certain disclosures may also be required in advertisements. See 12 CFR 1026.24.

TILA and Regulation Z include record retention requirements. Generally, the Company would need to maintain evidence of compliance for two years after the disclosures are required to be made. Special record retention requirements apply to advertising. See 12 CFR 1026.25.

Gramm-Leach-Bliley Act

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[4] Even if we have not noted a specific record retention requirement in relation to a specific law or regulation, we recommend that the Company maintain records of compliance with each law and regulation mentioned in this memorandum for a reasonable time, which is generally going to be the time during which a consumer could bring a claim against the Company for violation of the law or regulation.

The Gramm-Leach-Bliley Act ("GLBA") is a federal statute with various implementing regulations. 15 USC 6801-6809. For purposes of this memorandum, it includes both privacy and information security standards and is implemented by the privacy rule and information safeguards rule. 12 CFR Part 1016, 16 CFR Part 314.

The GLBA and its implementing regulations apply to financial institutions. However, the definition of "financial institutions" is not limited to depository financial institutions. The term includes other entities that are in the business of engaging in financial activities under the Bank Holding Company Act. 15 USC 6809(3). Lending is a financial activity under the Bank Holding Company Act. See 12 USC 1843(k). An entity that is not "significantly engaged" in a financial activity is not "in the business of engaging" in that activity. An entity would be covered if it regularly engages in the activity or if the financial activity was one of the entity's lines of business. For example, a retailer that issues its own credit cards directly to consumers is a covered financial institution. 12 CFR 1016.3(l). Unless the Company's lending activity is extremely limited, we believe it would be a financial institution under GLBA and its implementing regulations.

An entity that is subject to the GLBA must provide an individual who obtains a financial product or service for personal, family or household purposes with notice of the entity's privacy policies and practices. In some situations, the entity also must provide the notice to individuals who provide non-public personal information to the entity, but do not obtain a financial product or service. Non-public personal information is any information: (i) a consumer provides on an application to obtain a financial product or service; (ii) about a consumer resulting from any transaction involving a financial product or service between the entity and consumer; or (iii) that the entity otherwise obtains about a consumer in connection with providing a financial product or service to that consumer. It includes any list, description, or other grouping of consumers (and publicly available information pertaining to them) that is derived using the above information if that information is not publicly available. 12 CFR 1016.3(p)(1), (q)(1). Examples of non-public personal information include information on an application, an account balance, a payment history, and the fact that an individual has obtained a financial product or service. 12 CFR 1016.3(q)(1). The notice of privacy policies and practices must meet the content and format requirements of the privacy rule. 12 CFR 1016.6. The Consumer Financial Protection Bureau has provided a model form that, when completed correctly, meets the content and formatting requirements of the privacy rule.

Unless an exception applies, an entity that shares non-public personal information to unaffiliated third parties must also allow an individual the opportunity to opt out of such sharing. The entity must provide a notice of opportunity to opt out and give the individual a reasonable opportunity to opt out prior to sharing non-public personal information with an unaffiliated third party. Additionally, an entity must comply with an individual's decision to opt out as soon as reasonably practicable after receiving the individual's request to opt out. The Consumer Financial Protection Bureau has provided a model form that, when completed correctly, meets the content and formatting requirements for the opt out notice. 12 CFR 1016.7.

If the Company is subject to the GLBA, the Company would be required to provide an initial privacy notice no later than the time that the Company originates a loan and an annual privacy notice each year until the loan relationship is terminated. 12 CFR 1016.4, .5. If the Company will disclose non-public personal information about applicants to unaffiliated third parties, the Company would also need to provide an initial notice to applicants. 12 CFR 1016.4(a)(2). If the Company shares information with an unaffiliated third party outside of an exception, the borrower or applicant must be given the option to opt-out of the sharing. 12 CFR 1016.7. The Company would also need to comply with the limits on using and disclosing non-

public personal information set forth in the Company's privacy notice and the privacy rule. See 12 CFR 1016.10-.15 for the limits on using and disclosing non-public personal information.

An entity that is subject to GLBA must also develop, implement and maintain a written information security program that contains administrative, technical and physical safeguards to insure the security and confidentiality of non-public personal information (*i.e.*, customer information), protect against anticipated threats or hazards to the security or integrity of such information and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any consumer. 15 USC 6801(b). If the Company is subject to GLBA, it would need to develop, implement and maintain a written information security program and as part of that program: (1) designate one or more employees to coordinate the information security program; (2) identify reasonably foreseeable risks to customer information and assess the sufficiency of the current safeguards for controlling the risks; (3) design and implement a program and regularly monitor and test it; (4) select service providers that can maintain appropriate safeguards, contractually require them to do so, and oversee their handling of customer information; and (5) evaluate and adjust the program as required in the information safeguards rule. 16 CFR 314.4.

Unfair or Deceptive Acts and Practices

The Federal Trade Commission Act is a federal statute that contains a provision prohibiting unfair or deceptive acts or practices in or affecting commerce. 15 USC 45. This section of the Federal Trade Commission Act is commonly called Section 5 or the UDAP law. The Credit Practices Rule enumerates some specific prohibited practices under Section 5, but courts and regulators have used Section 5 more generally to prohibit practices that they deem to be unfair or deceptive. Therefore, in addition to complying with the Credit Practices Rule,[5] the Company would need to review its lending practices, including its advertising, origination, servicing and collection practices, to determine whether any of them may be deemed unfair or deceptive.

Generally, an act or practice will be deemed "unfair" if it causes substantial consumer injury, the injury is not outweighed by benefits to consumers or competition, and the injury is not the type that the consumer could reasonably avoid. Public policy may be considered, but cannot be the sole basis for a determination. An act or practice will be "deceptive" it involves a material misrepresentation or omission, it is likely to mislead, and is deceptive from the perspective of a reasonable consumer. Federal and state regulators have published guidance on particular acts and practices that they believe violate or are likely to violate Section 5, and there have been many enforcement actions and court decisions that identify UDAP issues. We can provide additional information about these specific acts and practices upon request.

We have not been provided with a list of acts or practices to review for possible UDAP violations. However, we have been told that the Company intends to use "on bill financing," meaning that the Company will include the amounts due for the loan on the same periodic statement that includes amounts due for utility services. We believe that "on bill financing" could be a potential source of UDAP risk. In order to mitigate UDAP risk, the Company should clearly explain the concept of "on bill financing" to loan applicants, and any periodic statement that the consumer receives should clearly differentiate between the amounts due

[5] The Credit Practices Rule prohibits the following terms in a loan agreement: confessions of judgment, waivers of exemptions, wage assignments, and non-possessory security interests in household goods. It also requires notices to guarantors and other co-signers and prohibits pyramiding late charges.

for utility services and amounts due pursuant to the loan agreement. Consumers should understand the consequences for failing to pay each amount. If the Company may terminate utility services for the failure to pay an amount due on the loan, we believe that the Company should clearly disclose this fact to the consumer. We have not been asked to and are not opining on whether such a practice would be permissible under any law or regulation, including any law or regulation specific to the Company or utility companies generally. If the Council would like additional information on UDAP risks or any analysis regarding "on bill financing" generally, we can provide additional information or analysis upon request.

Fair Credit Reporting Act

The Fair Credit Reporting Act ("FCRA") is a federal statute that governs the use of consumer reports and the furnishing of information to consumer reporting agencies. It also contains provisions related to identity theft and the use of certain information. 15 USC 1681 et seq. A "consumer report" is any written, oral, or other communication of any information by a consumer reporting agency that bears on a consumer's creditworthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected, in whole or in part, for the purpose of serving as a factor in establishing the consumer's eligibility for: 1) credit or insurance to be used primarily for personal, family, or household purposes; 2) employment purposes; or 3) any other purpose authorized under section 604 of FCRA. 15 USC 1681a(d). It would not include a report that contains information regarding experiences between the consumer and the Company. A "consumer reporting agency" is "any person which, for monetary fees, dues, or on a cooperative nonprofit basis, regularly engages in whole or in part in the practice of assembling or evaluating consumer credit information for the purpose of furnishing consumer reports to third parties, and which uses any means or facility of interstate commerce for the purpose of preparing or furnishing consumer reports." 15 USC 1681a(f).

The Company would need to have a permissible purpose under FCRA to obtain a consumer report. Generally, a permissible purpose would include obtaining a report in connection with an extension of credit involving the consumer named in the report or for review or collection of an account of that consumer. In order to ensure that it had a permissible purpose, the Company could also obtain written consent from the consumer before obtaining the consumer report. 15 USC 1681b(a).

The Company would need to provide certain disclosures in connection with any adverse action it takes based in whole or in part on a consumer report. It would also need to provide a special notice if it used a consumer report as the basis, in whole or in part, to grant credit on terms that are materially less favorable than the most favorable terms available to a substantial portion of consumers. 15 USC 1681m. The Company would also be prohibited from using certain information and would be required to take certain actions regarding information, such as fraud and active military duty alerts, in consumer reports.[6] The Company would be required to dispose of any consumer reports as well as any information derived from a consumer report in compliance with FCRA and its implementing regulations. 15 USC 1681w.

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[6] Certain actions are required for address discrepancies between the consumer's address in the Company's file and in the consumer report, for fraud alerts and active duty alerts in consumer reports, and victim reports of identity theft. 15 USC 1681c(h), 1681c-1, 1681g(e). No person is allowed to sell, transfer or place for collection a debt that such person has been notified resulted from identity theft in accordance with FCRA. 15 USC 1681m(f). A creditor cannot obtain or use medical information in connection with a determination of a consumer's eligibility for credit. 15 USC 1681b(g).

If the Company furnished to consumer reporting agencies information about loans that the Company originated, the Company would need to comply with additional requirements. See 15 USC 1681s-2.

FCRA also imposes explicit and implicit limits on sharing consumer reports and information obtained from consumer reports. The Company would need to comply with such limits. In some cases, the sharing of such information could cause the Company to become a consumer reporting agency subject to additional requirements under FCRA.

Finally, the Company would need to determine whether it has a "covered account" under the Red Flags Rules promulgated pursuant FCRA and, if it does, comply with the Red Flags Rules. Generally, a creditor that is subject to ECOA is subject to the Red Flags Rules. 15 USC 1681a(r), 1681m(e). See also 16 CFR 681.1(a), (b)(5). A creditor that is subject to the Red Flags Rules must periodically determine whether it offers or maintains any covered accounts, which are accounts offered primarily for personal, family or household purposes that are designed to permit multiple payments or transactions and any other account for which there is a reasonably foreseeable risk from identity theft. 16 CFR 681.1(b)(3), (c). If a creditor offers or maintains one or more covered accounts, it must develop and implement a written identity theft prevention program designed to detect, prevent, and mitigate identity theft in connection with covered accounts. The written program must comply with the content and administration requirements in the Red Flags Rules. 16 CFR 681.2(d), (e). Because the Company is a creditor under ECOA, it will need to periodically determine whether it offers or maintains any covered accounts. Because the Red Flags Rules include loans such as automobile loans and mortgage loans within the scope of covered accounts, it appears that the loans would likely be covered accounts and the Company would need to develop a written identity theft prevention program even though the loans do not involve multiple advances.

Electronic Fund Transfer Act

Under the Electronic Fund Transfer Act and its implementing regulation, Regulation E, authorizations for electronic fund transfers authorized in advance to recur at substantially regular intervals from a consumer deposit account must meet certain requirements. If the Company intends to obtain such authorizations, such as for auto-payments, the authorizations would need to be in writing and signed or similarly authenticated by the consumers, and the Company would need to provide a copies of the authorizations to the consumers. 12 CFR 1005.10. The Company could not condition the loan on the consumer's repayment by preauthorized electronic fund transfer. 12 CFR 1005.10(e). Additional requirements could apply depending on the payment amounts and the method of processing the transfers.

Office of Foreign Asset Control

All United States persons must comply with the Office of Foreign Asset Control ("OFAC") regulations. OFAC is an office of the United States Treasury Department that administers and enforces the economic and trade sanctions set forth in various executive orders, related regulations, *etc*. Generally, all United States persons are required to block accounts and other property of specified countries, entities and individuals and prohibit or reject unlicensed transactions with specified countries, entities and individuals. Although the executive orders and regulations do not set forth a specific method to comply with these general requirements, most lenders have OFAC compliance programs designed to ensure that they are not lending money to any country, entity or person in violation of the OFAC requirements. These programs include a process for comparing the names of applicants to certain OFAC lists and reporting blocked or rejected transactions.

Bank Secrecy Act

The Bank Secrecy Act, which is a federal law designed to prevent money laundering and other federal crimes, imposes certain reporting and other requirements on “financial institutions.” The statute defines the term “financial institution” broadly to include not only depository institutions but also several different types of entities, including loan and finance companies. 31 USC 5312(a)(2). Although the Financial Crimes Enforcement Network has informally stated that the term “loan and finance company” could be reasonably construed to extend to any business entity that makes loans to or finances the purchases on behalf of consumers or businesses, the implementing regulations limit the definition. Pursuant to the regulation, a “loan and finance company” is a residential mortgage lender or originator that accepts applications for, offers, negotiates, originates or takes assignments of loans that are secured by a mortgage, deed of trust of other equivalent consensual security interest on residential real estate or structures. 31 CFR 1010.100(lll). Because the proposed loans are unsecured, the Company does not currently have any reporting or other obligations under the Bank Secrecy Act.

Michigan Licensing and Usury

In Michigan, the laws governing the collection of interest[7] allow parties to agree in writing that a borrower will pay a “rate of interest” of up to 7% on an unsecured loan. If the agreement is not written, the borrower can only be required to pay an interest rate of up to 5%.[8] MCL 438.31. Certain lenders can charge higher rates if, for example, they are licensed under specific laws or are depository institutions, such as banks or credit unions. In Michigan, these lenders are often described as regulated lenders. For example, a regulated lender can charge up to 25% on most loans under the Michigan Credit Reform Act. See MCL 445.1851 *et seq*. Michigan also has a law that includes an absolute cap on the interest that any lender can charge a borrower. It prohibits charging a simple interest rate of more than 25%. MCL 438.41.

There is no specific Michigan requirement to obtain a license to make unsecured loans in Michigan. However, generally “a person shall not engage in the business of making loans of money, credit, goods or things in action and charge, contract for, or receive on the loan a greater rate of interest, discount or consideration than the lender would be permitted to charge if the lender were not a licensee under [the Regulatory Loan Act] and without first obtaining a license from the commissioner, or by obtaining a license under the consumer financial services act….” MCL 493.2(1). In other words, if the Company wishes to charge an interest rate of more than 7% on an unsecured loan, it must obtain a license under the Regulatory Loan Act or the Consumer Financial Services Act. Although obtaining a license would allow the Company to charge an interest rate above 7% and to charge certain fees, it would subject the Company to examination and supervision by Michigan’s Department of Insurance and Financial Services and to other requirements.

Michigan Social Security Privacy Act

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7 Interest may include fees and other charges that are not called interest. If the Company intends to charge any fees in connection with the loans, it should determine whether they would be considered interest under Michigan law.

8 The Company may be permitted to charge a higher rate of interest if specifically authorized by the Public Service Commission. See MCL 438.31.

The Michigan Social Security Number Privacy Act prohibits publicly displaying or using as an account number more than four sequential digits of an individual's social security number. MCL 445.83. There are additional limits on the use of more than four sequential digits of a social security number, mailing documents that include more than four sequential digits of a social security number, and requiring transmission of more than four sequential digits of a social security number unless the connection is secure or the transmission is encrypted. *Id.* Unless a person only possesses social security number in the ordinary course of business and in compliance with FCRA and GLBA, a person who obtains one or more social security numbers in the ordinary course of business must have a privacy policy to ensure the confidentiality of, limit disclosure of, limit access to, and properly dispose of social security numbers. If the Company only obtains, uses, and disposes of social security numbers in compliance with FCRA and GLBA, it would not need a separate privacy policy under Michigan law. However, the Company would need to have and implement a written information security program under GLBA.

Michigan Fair Lending Provision

Michigan's Penal Code, MCL 750.147a, prohibits discrimination in extending credit or rating creditworthiness on the basis of race, color, religion, national origin, marital status, sex, or physical disability. The Company could not extend credit or rate creditworthiness in violation of the Michigan Penal Code.

Michigan Consumer Protection Act

The Michigan Consumer Protection Act prohibits certain unfair, unconscionable, or deceptive acts or practices in the conduct or trade or commerce. Trade or commerce means the conduct of a business providing goods, property or services primarily for personal, family or household purposes. MCL 445.902(1)(g). A transaction or conduct specifically authorized under laws administered by a regulatory board or officer acting under statutory authority are exempt. However, it is doubtful that this exemption would apply to the Company's lending activities. A complete list of the prohibited acts and practices can be found at MCL 445.903-.903i, but they include a prohibition on causing a probability of confusion or misunderstanding as to the terms or conditions of credit, failing to reveal a material fact that the consumer could not reasonably know, and entering into a consumer transaction in which the consumer waives or purports to waive a right, benefit or immunity provided by law (such a jury waiver) unless the waiver is clearly stated and the consumer has specifically consented.

Identify Theft Protection Act

The Michigan Identity Theft Protection Act prohibits a person from denying credit to a consumer or reducing the consumer's credit limit solely because the consumer was a victim of identity theft or extending credit to a consumer without exercising reasonable procedures to verify the identity of the consumer. MCL 445.71(1)(a),(d). It also prohibits soliciting an extension of credit through use of an unsolicited check or credit card if the check or card contains certain information. MCL 445.71(1)(b),(c).

The Identity Theft Protection Act also requires persons, other than designated financial institutions,[9] to provide notices of certain data security breaches.[10] Under the Act, a public utility that sends monthly billing or account statements to the postal addresses of its customers is allowed to provide notice to its customers by an alternative means. However, it is not clear that the Company could use the alternative means if the breach related to the loan information. See MCL 445.72(11).

A person must also shred, erase, or otherwise destroy data concerning individuals when the data is removed from a database. The data must be destroyed in manner that keeps it from being read, deciphered, or reconstructed through generally available means. However, compliance with an applicable federal requirement regarding the disposal of personal identifying information is deemed compliance with the destruction requirement in the Michigan Identity Theft Protection Act. MCL 445.72a.

Michigan Co-signer Act

Although we have not generally included laws and regulations that apply specifically to servicing or collection and have assumed, given the nature of the loans, that the loans will not have guarantors or co-signers, we note that there is a Michigan law that requires a party to take certain steps before reporting adverse information about a co-signer to a consumer reporting agency or taking collection action against a co-signer. MCL 445.271-273. For this purpose, a co-signer is a natural person who renders himself or herself liable for the obligation of another without compensation. MCL 445.271(c).

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[9] A person subject to the GLBA's privacy and information security requirements would be a financial institution under the Michigan law. MCL 445.63(i). However, the data breach notice requirements apply unless the financial institution has notification procedures in place that are subject to examination by a regulator for compliance with the banking agencies' guidance on unauthorized access. Because it does not appear that the Company would be subject to examination for compliance with the guidance, it would need to comply with the Michigan data breach notice requirements.

[10] A security breach is the unauthorized access and acquisition of computerized personal information that comprises the security or confidentiality of the personal information maintained as part of a database of personal information. In limited situations, it does not include unauthorized access by an employee. See MCL 445.63(b). Generally, notice is required when a security breach may cause substantial loss or injury to or result in identity theft to one or more Michigan residents. MCL 445.72.

Michigan Collection Practices Act

Although we have not generally included laws and regulations that apply specifically to servicing or collection, we note that Michigan does have a law regulating the collection activities of a person whose collection activities are confined to and directly related to the operation of a business other than that of a collection agency. MCL 445.251 *et seq.* The list of prohibited acts is set forth in MCL 445.252.