HOUSE
RESEARCH
ORGANIZATION bill analysis 4/23/2001

HB 2139
Marchant

SUBJECT: Excluding debt cancellation agreement from definition of insurance

COMMITTEE: Financial Institutions — favorable, without amendment

VOTE: 8 ayes — Averitt, Solomons, Denny, Grusendorf, Hopson, Marchant, Menendez, Wise

0 nays

1 absent — Pitts

WITNESSES: For — Gene Fondren, Texas Automobile Dealers Association; Andy Siegel, New Car Dealers Association; *Registered but did not testify:* Kevin Hamby, Texas Credit Union League; Jim Jeter; Dave Rothell, ANCO Insurance

Against — Birny Birnbaum; *Registered but did not testify:* Rob Schneider, Consumers Union

On — *Registered but did not testify:* Leslie Pettijohn, Office of Consumer Credit Commissioner

BACKGROUND: Finance Code, sec. 348.208(b)(4) allows retail installment loans on motor vehicles to include a separate charge for insurance to pay the difference between what the buyer's collision insurance would pay in the event that the vehicle was a total loss and what the buyer owes on the note. This form of insurance, known as gap insurance, is regulated by the Texas Department of Insurance (TDI).

DIGEST: HB 2139 would allow the lender for a vehicle installment loan to include a provision in the loan that would cancel the portion of the loan amount that exceeded the amount that the buyer's collision insurance would pay in the event that the vehicle was a total loss.

Debt cancellation agreements could provide that the lender agreed to cancel the portion of the amount owed on the installment loan that was attributable to the buyer's deductible under the collision insurance. The charge for a debt cancellation provision could be financed with other charges for the vehicle and included in the installment contract.

HB 2139 would provide that a debt cancellation agreement included in an installment contract is not insurance and cannot be regulated by TDI or the insurance commissioner.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2001.

SUPPORTERS SAY:

HB 2139 would guarantee that consumers could contract with automobile lenders to avoid paying for a car that had been destroyed. When a person buys a car, especially a new one, there may be a period in which the buyer is "upside down" on his or her loan, when the car is worth less than what the person owes on it. If the person has an accident and the car is totaled during that period, the person's collision insurance will pay only the value of the car, not the amount left on the loan. Thus, the consumer is left with a car payment but no car. A debt cancellation agreement protects the consumer from this contingency by allowing the consumer to pay a fee to the seller or lender to agree to accept the amount the collision insurance pays and cancel the remainder of the debt in the event the car is destroyed.

A debt cancellation agreement made as part of an installment loan simply would be another contract term, and such agreements should not be regulated by TDI as insurance. It would not transfer risk, but would extinguish an obligation. Other industries, specifically the financial services industry, are permitted to enter debt cancellation agreements with their clients. Auto dealers/lenders also should be able to do so.

The retail automobile industry is very competitive, as evidenced by the fact that when the average retail car price rose by about $10,000 between 1988 and 1998, the average increase to dealers over that period was only $383. Because of such competition, auto dealers would have an incentive to offer debt cancellation agreements at competitive prices or offer gap insurance instead if that product was cheaper and would help keep the monthly payment on the vehicle within the consumer's budget.

OPPONENTS SAY:

HB 2139 would transfer money from consumers to auto dealers and offer consumers no benefit in return. Gap insurance and debt cancellation agreements offer consumers the same basic protection, but gap insurance, which is regulated by TDI, costs about one-third less than debt cancellation agreements and offers auto dealers about one-sixth of the profit. For instance, a gap policy on a $15,000 loan financed for 60 months costs $150, of which $37 goes to the dealer as a commission for selling the insurer's policy. On the same loan, a dealer typically charges around $400 for a debt cancellation provision and nets $250 after the dealer has paid an insurance company to insure the risk.

HB 2139 also would harm consumers by eliminating the option of buying the less expensive gap insurance. Dealers offer gap insurance now and insurers are willing to write the policies. In fact, three new insurers have applied to TDI for permission to offer gap insurance in the past several months. However, because dealers make more money on the debt cancellation agreements, they would like to stop offering gap policies. If that occurred, even informed consumers who know about gap insurance could not buy the policies.

NOTES: The companion bill, SB 567 by Carona, has been referred to the Senate Business and Commerce Committee.