

California's new legislation takes aim at GAP waivers

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California Attorney General Rob Bonta has never minced words in expressing his position that consumers should be protected from guaranteed asset protection (GAP) waivers. This trend continued with his sponsorship of [AB 2311](#), authored by California State Assemblyman Brian Maienschein.

Bonta stated that “when Californians walk into a dealership to buy a car, they should feel confident that they’re not getting ripped off. Unfortunately, auto dealers often play off our anxieties around making this big purchase, convincing us to add on unnecessary products for hundreds of additional dollars. Paying off your auto loan is hard enough without these junk products tacked on.”

California bill AB 2311 was signed by California Governor Gavin Newsom on Sept. 13, and is effective Jan. 1, 2023; it regulates GAP waivers sold in connection with conditional sales contracts (CSC), giving holders, sellers and providers of GAP waivers just over 90 days to comply. The bill, which will amend sections 2981-2983.1 of California’s Civil Code, includes requirements on both the origination and servicing/termination side of two-party GAP waivers. It does not apply to GAP insurance.

Origination

The origination requirements are applicable to any GAP waiver originated on or after Jan. 1, 2023. Requirements for necessary disclosures are similar to what we have seen in other state’s GAP waiver laws. These include: separate itemization of the GAP cost financed, a statement that the GAP waiver is optional, that the holder of the CSC is the contracting party to the GAP waiver, and the name and mailing address of the seller and any administrator.

The latter three must appear in a document separate from the CSC, which must also include a bolded, capitalized statement immediately above the contract signature line advising the consumer to “STOP AND READ” and explaining again that purchase of a GAP waiver is optional; it cannot affect the consumer’s finance terms; and that is unlawful for the seller to require its purchase.

Notably, California has gone further than other states in its origination restrictions by prohibiting sales of a GAP waiver when the waiver will not cover or will only partially cover the gap amount, and by controlling the cost of the GAP waivers. The charge for the GAP waiver cannot be more than 4% of the amount the buyer finances under a CSC.

Further, a GAP waiver cannot be sold if: (a) the amount financed exceeds a maximum dollar amount covered by the GAP waiver; (b) the loan-to-value (LTV) ratio at the contracting date exceeds the maximum LTV ratio covered

by the GAP waiver, unless agreed to by consumer after conspicuous disclosure; and (c) the amount financed is less than 70% of the MSRP for a new motor vehicle or the average retail value for a used motor vehicle, as determined by a nationally recognized pricing.

In the California Senate's companion bill [SB 1311](#), section 408.1 of California's Military and Veteran Code was amended to prohibit a security interest in a retail transaction for motor vehicles that includes credit insurance or other credit-related ancillary products — including but not limited to a GAP waiver — from being perfected if the loan was obtained by a "covered member," as defined in the Military Lending Act pursuant to Section 987 of Title 10 of the United States Code.

This is important to note because a holder may collect installments owed on the contract, but it couldn't repossess the collateral — making it effectively an unsecured contract. This will eliminate the option of service members to purchase GAP waivers in California. Holders are also grappling with how to logistically verify which consumers are active members of the armed forces.

Servicing and termination

The servicing and termination requirements are applicable to any GAP waiver still active on or after Jan. 1, 2023, regardless of when they were entered. These requirements are more stringent than what we've seen in most other states.

When communicating in writing an itemized contract balance to the buyer, including a payoff letter, payoff quote or any written notice required after repossession, the holder of a CSC that includes a GAP waiver must individually identify the amount of the pro-rata credit or refund which would be due to the buyer if the GAP waiver were cancelled on a given date.

This requirement may also be accomplished by letting the consumer know to contact the GAP waiver administrator for the amount of such a refund. Within 60 business days from the termination of a GAP waiver, the holder must tender the refund required or cause the refund to be made by instructing the administrator in writing to make the refund. When the GAP waiver is terminated, no cancellation fee, termination fee or similar fee may be charged.

As more states continue to regulate GAP waivers — and particularly GAP waiver refunds — many holders with a national platform are discussing or beginning to adopt a 50-state automatic refund model.

Using some of the most stringent laws as a base, many of the California regulations may end up in holder refunding practices in other states as well. As this will take time and require systems to implement, most in the industry have suggested that to meet California's requirements, they will generally inform the consumer that they may be entitled to a refund of the unearned portion of a GAP waiver on any written itemization of the balance and direct them to contact the administrator for the exact amount.

Further, it has been suggested that the holders will advise administrators in writing that the GAP waiver has been terminated and a refund is due. Best practice for holders is to keep a copy of both the written notice and evidence that the refund has been made to the consumer from the administrator.

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