

**SFA**

BILL ANALYSIS

Senate Fiscal Agency

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House Bill 4354 (Substitute H-1 as reported without amendment)

Sponsor: Representative Alma Stallworth

House Committee: Consumers

Senate Committee: Commerce and Technology

Date Completed: 10-26-89

**RATIONALE**

Often a person who has acted as a cosigner on an obligation, such as a loan, is not aware that the primary signer has missed payments or defaulted on the loan until the cosigner is contacted by a collection agency or reported to a credit bureau as having a bad debt. Tarnished credit ratings and heavy legal expenses have resulted, some people contend, because there is no requirement in law to provide for the notification of cosigners when a primary signer has become delinquent or has defaulted on an obligation. Some people believe that creditors should be required to notify a cosigner, who may be unaware of payment problems by the primary signer, before releasing adverse information to consumer reporting or collection agencies.

**CONTENT**

The bill would create a new act to require creditors to notify a cosigner before informing a credit agency that the cosigner had not complied with the contractual provisions of an obligation. Under the bill, "cosigner" would be defined as a natural person (an individual) who rendered himself or herself liable for the obligation of another person without compensation. A person who did not receive goods, services or money in return for a credit obligation would not be considered under the bill as receiving compensation. The term "cosigner" would include a person whose signature had been requested as a condition to granting credit to

another person, or as a condition for forbearance on collection of another person's obligation that was in default. The term would not include a spouse whose signature was required on a credit obligation to perfect a security interest under State law, or a person who had executed a guarantee. A person who met the definition of "cosigner" would be considered a cosigner under the bill whether or not he or she were designated as a cosigner on a credit obligation.

Before reporting information about a cosigner to a consumer reporting agency concerning the obligation that was cosigned, or before providing any information to a collection agency or taking any collection action on the obligation against the cosigner, the bill would require that a creditor--other than orally communicating information on the delinquency--do both of the following:

- Send a notice to the cosigner by first class mail, indicating that the primary obligor had become delinquent, or had defaulted on the obligation, and that the cosigner was responsible for payment.
- Allow the cosigner not less than 30 days from the date the notice was sent to respond either by paying the amount due, or by making other arrangements that were satisfactory to the creditor.

A creditor could not report adverse credit information regarding a cosigner who had

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responded to a notice by paying the amount due or making satisfactory arrangements for payment.

A cosigner who suffered loss as a result of a violation of the bill could bring an action to recover actual damages or \$250, whichever was greater, together with reasonable attorney's fees. At least 30 days before bringing the action, the cosigner would be required to notify the alleged violator and include a statement of the specific evidence of the loss suffered by the violation. If, within 25 days after receiving the notification, the alleged violator compensated the cosigner in an amount equal to the loss or otherwise agreed to resolve the matter to the cosigner's satisfaction, then the cosigner would be barred from further recovery, including recovery of reasonable attorney's fees.

### **FISCAL IMPACT**

The bill would have no fiscal impact on State or local government.

### **ARGUMENTS**

#### **Supporting Argument**

The bill would provide needed protection for cosigners of obligations that have become delinquent or are in default by establishing a notification procedure and a time period in which a cosigner would be allowed to make arrangements with the lender to satisfy the terms of the obligation. As a result, cosigners would have an opportunity to remedy a situation before adverse information was reported to a collection agency or a consumer reporting agency, or before collection action was taken. Thus, people who cosigned for an obligation, often because their good history was needed to make an obligation more secure, could take action to ensure that they would continue to be viewed as "good risks" or as persons with "good credit".

#### **Opposing Argument**

While the bill would require a creditor to mail to a cosigner a notice that indicated that the primary obligor had become delinquent or had defaulted on the obligation, there is no provision in the bill to guarantee that the cosigner received the notification. It is feared that lenders would believe that they had discharged their duties merely by sending a

notice to a cosigner, even though the cosigner may not have received the letter and, thus, was not duly notified.

**Response:** Since it would be in the best financial interest of the lenders to make every effort to contact cosigners in order to receive loan payments, it can be assumed that lenders would take the necessary steps, in addition to notifying the cosigner by first class mail, to reach a cosigner.

#### **Opposing Argument**

While the bill would prevent adverse action against a cosigner for 30 days after the cosigner was notified that a primary obligor had become delinquent, the bill makes no provision regarding actions a creditor could take against the primary obligor. Some people believe the bill could prohibit creditors from taking action when a cosigner caught up on an obligor's past due payments. When an obligor repeatedly has made late payments on a loan, for example, a creditor normally will "accelerate" the debt and demand that the total amount of the loan be paid off. Some people fear that the bill would prevent such action by the creditor.

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