

Part 8. JOINT FINANCIAL REGULATORY AGENCIES

Chapter 153. HOME EQUITY LENDING

7 TAC §§153.82, 153.84 - 153.88

The Joint Financial Regulatory Agencies comprised of the Finance Commission of Texas and the Texas Credit Union Commission (the “Commissions”) adopt new 7 TAC, Chapter 153, §153.82 and §§153.84 - 153.88, administrative interpretations of subsection (t), Section 50, Article XVI, Texas Constitution, (the “Home Equity Lines of Credit” Laws or “HELOC”). The rules are adopted with non-substantive changes to the proposal as published in the January 2, 2004, issue of the *Texas Register* (29 Tex. Reg. 33).

The Commissions made non-substantive changes to clarify and simplify the addressed provisions as the result of comments. The Commissions also made editing and clerical corrections.

At the February 20, 2004, concurrent meeting of the Finance Commission and Credit Union Commission, one commenter, Robert Doggett, testified. The commenter expressed concern over the absence of specific authorization allowing for any borrower to unilaterally close a HELOC to new advances in §153.82. The commenter stated that the interpretation impermissibly allows a borrower to take advances on a HELOC against the wishes and to the detriment of other borrowers. The Commissions considered this comment and disagree. Parties may contract to allow any borrower to close a HELOC account to new advances. However, the constitution does not require such a limitation. The Commissions decline to modify the interpretation.

The commenter also expressed concern over the failure of the interpretation to restrict the use of convenience and solicitation checks that are not preprinted solicitation checks and do not meet the criteria under §153.84(4). The commenter stated that any check received by a borrower for the purpose of enticing the borrower to request additional advances and that the borrower did not request immediately preceding the receipt of the check should be a prohibited device. The Commissions considered this comment and disagree. The constitution did not exclusively use the term “check,” but modified it with the words “preprinted” and “solicitation.” The Commissions believe that the interpretation accurately reflects the intent of the constitution and decline to modify the interpretation.

The Commissions received written comments. The following commenters generally supported adoption:

Andrea Johnson of Neches Federal Credit Union; Karen M. Neeley of Independent Bankers Association of Texas; Alan J. Pohlmeier of Santa Fe Federal Credit Union-Amarillo; Lorena Rush of Wells Fargo; Karen Wilkerson of United Heritage Credit Union; Robert Zearfoss of Randolph Brooks Federal Credit Union; Suzanne Yashewski of the Texas Credit Union League; Larry Young of Hughes, Watters & Askanase, LLP; Connie Shoemaker of San Antonio City Employees Federal Credit Union; Jeffery Farver of San Antonio Federal Credit Union; and Lori W. Hall of American Airlines Federal Credit Union. The following commenters generally supported adoption, but also requested clarifications or recommended modifications: Greg Storch of USE Credit Union; Sharon Gaugler of Austin Area Teachers Federal Credit Union; Chet Kimmell of Neighborhood Credit Union; and Mark D. Morris of JP Morgan Chase. The following commenters requested clarifications or recommended modifications: Joseph M. Dixon, III of SouthTrust Bank; and David Dulock of Black, Mann & Graham, LLP. Robert W. Doggett of Texas Rio Grande Legal Aid, Inc. commented that the interpretations improperly modified certain sections.

Section 50, Article XVI, Texas Constitution (“Section 50”), sets out the only permissible encumbrances on a homestead. Prior to 1998, Section 50 permitted liens on homestead property for the purposes of purchase money, taxes, an owelty of partition, the refinance of a lien, including tax liens, and home improvements. The 75th Legislature, 1997, passed House Joint Resolution 31 (“HJR 31”), which was adopted by the voters on November 4, 1997. Effective January 1, 1998, HJR 31 created two additional categories of authorized liens: a loan secured by the equity an owner has in a homestead and a reverse mortgage on a homestead. House Joint Resolution 31 also modified the existing provisions regarding liens on a homestead for home improvement purposes. During the 78th Legislature, 2003, Regular Session, the legislature passed Senate Joint Resolution 42 (SJR 42), which was adopted by the voters on September 13, 2003, and amended the constitution effective September 29, 2003. This amendment added Section 50(t) allowing homeowners to contract for home equity lines of credit for the first time in Texas history.

The constitutional provisions do not detail every aspect of home equity lending. Compliance with Section 50 along with other Texas and federal statutes and Texas constitutional provisions is required in making a home equity loan. These interpretations construe the language of Section 50(t) and provide the required practical framework for home equity lending that reflects the con-

stitutional language and the intent of the legislature and the voters. For example, Section 50(t) contains terms that are not defined, even though definitions are necessary for clear meaning and consistent application. Additionally, the constitutional provisions are silent as to the effect of other laws on home equity lending.

Each section of Chapter 153 corresponds with an identified provision of the Texas constitution. The first portion of each section is typically a restatement of the constitutional provision.

The Commissions have applied Chapter 311, Government Code (Code Construction Act) in the use of language in Chapter 153. For example, in Chapter 153, words used in the singular include the plural and the plural includes the singular, the heading of a title, subtitle, chapter, subchapter, or section does not limit or expand the meaning of an interpretation, and the use of the word “include” means “including but not limited to.”

The initial interpretations of Section 50(t) in Chapter 153 do not preclude future consideration by the Commissions of additional HELOC issues that may or may not be addressed at this time. Issues raised in comments to the proposed interpretations have been addressed in this preamble regardless of whether a change was made to the interpretation in response to the comments. Constitutional provisions not interpreted at this time may be addressed either at the request of an interested party or on the motion of the Commissions.

Section 153.82 interprets Section 50(t)(1) clarifying that any owner who is also a borrower may request an advance. The interpretation also recognizes that a lender and a borrower may contractually require specific borrowers or all borrowers to consent to a request for an advance.

Two commenters expressed agreement with §153.82. One commenter stated that “all owners who have any ownership interest in the home should have the ability, individually, to request an advance under a HELOC.” The commenter agreed that additional safeguards could be established by the lender and the borrower to the loan.

Another commenter stated, “We believe the language in proposed §153.82 is the only legally defensible reading of the constitutional phrase ‘the owner requests advances’ in Section 50(t)(1). Indeed, a construction of this phrase that would require *all owners* to request advances . . . would be absurd when read in the context of the complete phrase, because it would require all

owners to repay money--even if they were not borrowers!” The commenter went on to say, “the role of the Commissions in promulgating the proposed interpretations is not to decide what the constitutional provision ought to say; it is to interpret what it actually does say. We believe the language of the Constitution is clear and that proposed §153.82 accurately reflects that language.”

One commenter disagreed with the portion of §153.82 that states: “a HELOC agreement may contain provisions that restrict who may request an advance or require all borrowers to consent to the request.” The commenter suggested removing the language from the interpretation and adding new language that a HELOC agreement may contain provisions that “allow any borrower to close the account to new advances and may require that all borrowers consent to reactivation of the HELOC.” The Commissions have considered this comment and disagree. Consequently, the Commissions decline to modify the interpretation. The Constitution does not prohibit a lender and a borrower from freely negotiating a contract with additional restrictions on who may access a HELOC. The Commissions also believe that the lender and a borrower may contract to allow any borrower to close an account to new advances.

Another commenter stated that “if there is more than one owner then both owners must consent to the advance” and that the Commissions’ “interpretation will benefit predatory lenders.” The Commissions reviewed this comment and believe that the interpretation is correct. Lenders are constitutionally required by Section 50(a)(6)(A) to obtain consent from all owners and all owners spouses to originate a HELOC. The original loan documents determine who is authorized to initiate advances within constitutional limits. The Commissions decline to modify this interpretation.

Section 153.84 interprets Section 50(t)(3), explaining the restrictions on methods of obtaining a HELOC advance. A preprinted solicitation check is a constitutionally prohibited method of obtaining a HELOC advance. This section defines the constitutional phrase “preprinted solicitation check;” this section does not prohibit convenience checks, prearranged drafts, and transfer instructions as methods of obtaining advances. The Commissions believe that if the legislature had intended a prohibition on all checks, it would have prohibited “checks” rather than prohibiting “preprinted solicitation check,” which is a type of check. Checks used to obtain advances must be written for a minimum amount of \$4,000 and comply with the limitations contained in Section 50(t)(5) and (6). The Commissions believe that

adequate procedures should be in place to ensure that checks used to obtain advances do not result in a violation of any constitutional provisions.

The constitution specifically prohibits the use of credit cards, debit cards, preprinted solicitation checks, and “similar devices.” The Commissions believe that the phrase “similar devices” refers to unnamed devices, whether they now exist or are produced in the future, and that the term was used by the drafters in lieu of a list of devices that may not be exhaustive.

Seven commenters specifically expressed support for convenience checks to access HELOC advances. One of these commenters stated, “the clarification of §153.84 concerning usage of checks for draws will be very advantageous to the credit union and its members.”

Another commenter stated, “We strongly support proposed §153.84. It is abundantly clear that the relevant constitutional provision, Section 50(t)(3), does not prohibit check access. The discussion section of the proposed interpretation is absolutely correct....” The commenter stated, “we also believe that the definition of ‘preprinted solicitation check’ in proposed §153.84(3) is a sensible, reasonable definition, which gives effect to all three words in that phrase.”

One commenter recommended that the term “convenience check” be excluded from the definition of “credit card” contained in §346.001(2), Texas Finance Code. The Commissions evaluated this recommendation and determined to modify the interpretation to include a definition of “credit card transaction” as defined in §301.001(1), Texas Finance Code. A credit card is a prohibited device for obtaining a HELOC advance under the constitution. The Commissions believe that a definition is helpful to ensure that parties understand which devices would fall under the definition of credit card and thus be prohibited.

One commenter was concerned that convenience checks could cause lenders procedural problems because of the other constitutional restrictions on advances. All constitutional requirements in connection with advances must be satisfied. If a lender cannot institute appropriate procedural safeguards in connection with the use of a nonprohibited method or device, then they should not use that method or device.

One commenter expressed that §153.84 improperly modifies Section 50(t)(3). The commenter stated that, “The constitutional provision does provide for acceptable methods to obtain an advance, it only prohibits

certain types of advances meant to protect consumers.” The commenter also expressed that the interpretation, “provides more loopholes that are not defined at all; prearranged draft, convenience check, and transfer instructions.” The omission of a definition of “similar devices” by the drafters of the Constitution necessitates an interpretation. Without interpretation, the term “similar device” would cause uncertainty for borrowers and lenders. The Commissions do not believe that loopholes are created by listing examples of permissible devices. The devices would be permissible even if the Commissions did not list them; however, they are listed to offer clarity to borrowers and lenders.

Section 50(t)(3) prohibits preprinted solicitation checks. Because the drafters of the constitution deliberately used the phrase “preprinted solicitation check,” the Commissions carefully considered each word. The Commissions determined that a check is “preprinted” if the lender inserts at least one key payment term, such as the amount or payee on the face of the check. The Commissions determined that “solicitation” occurs when a lender initiates contact to either entice an owner to originate a HELOC or influence a borrower to request additional advances on an existing HELOC. The Commissions determined that §153.84(4) as proposed, limiting preprinted solicitation checks to “negotiable instruments,” was too narrow and amended it to include all checks, whether or not they are negotiable instruments. Check is a statutorily defined term in the Texas Business and Commerce Code and the Commissions believe that definition applies in this context. The Commissions reconsidered §153.84(4) and determined that it adequately gives effect to all three words in the phrase “preprinted solicitation check.” Except for the amendment explained in this paragraph, the Commissions otherwise respectfully decline to modify the interpretation.

One commenter asserted that §153.84 does not address or clarify the use of a HELOC established for overdraft protection (ODP). An ODP account would be activated if the checking account is overdrawn, then an advance of a minimum of \$4,000 from the HELOC will cover the overdraft amount. The commenter asked, “If the owner overdraws his checking account, due to a transaction with his debit card, and the ODP feature of the checking account is used, is the debit card considered to be the access device that created the advance from the HELOC?” The Commissions have considered this issue and believe that this will constitute the use of a debit card or similar device which is prohibited. Therefore, the Commissions decline to modify the interpretation to allow HELOC use for ODP.

Two commenters requested an interpretation that an advance on a HELOC at the time of closing is not subject to the \$4,000 minimum advance requirements. The Commissions decided to study this issue for future consideration. However, absent a constitutional amendment, a court ruling, or a future interpretation by the Commissions to the contrary, the Commissions believe that the \$4,000 limitation applies to advances at closing.

Section 153.85 interprets Section 50(t)(4), defining the time the extension of credit is made. In relation to the allowable fees and charges associated with the loan, the time the extension of credit is made is the date on which the loan is closed.

One commenter stated, “We agree that the loan closing date should be used when determining the allowable fees and charges associated with the loan. A clear interpretation can prevent misunderstandings that could lead to costly and unnecessary litigation.”

Another commenter stated, “Proposed §153.85, interpreting the phrase ‘the date the extension of credit is established’ to mean the closing date, is consistent with Section 50(t)(4). It is also consistent with the recently adopted interpretation of comparable constitutional language in Section 50(a)(6), 7 TAC §153.1(6), defining the ‘date the extension of credit is made’ as the closing date. There is no logical reason that the ‘date the extension of credit is *established*’ should be any later than the closing date, especially since, in a line of credit, the commitment to lend exists after execution of loan documents, regardless of when funding may occur. We support §153.85 as proposed.”

Section 153.86 interprets Section 50(t)(5), clarifying that a HELOC may not violate the 80 percent fair market value limitation in Section 50(a)(6)(B). The interpretation also clarifies that the maximum principal balance of a HELOC is determined on the date of closing and does not change during the term of the HELOC.

One commenter expressed concern over the fact that the maximum principal balance of a HELOC does not increase as the value of the homestead increases over the life of the HELOC. The commenter suggested that the Commissions examine the intent of the law to see if a more liberal interpretation could be allowed. Section 50(t)(5) states in pertinent part that, “the maximum principal amount that may be extended under the account, when added to the aggregate total of the outstanding balance principal of all indebtedness secured by the homestead on the date the extension of credit is established ...” (Emphasis added) The Commissions

have reviewed the intent and plain language of the constitution and have determined that a more liberal interpretation is not allowed.

Section 153.87 interprets the application of the fair market value limitation contained in Section 50(t)(6). The constitution allows for the principal amount of a HELOC to exceed the 50 percent fair market value limitation contained in Section 50(t)(6) but not the 80 percent fair market value limitation contained in Section 50(t)(5). The 50 percent fair market value limitation, however, is a restriction on additional advances if the aggregated amount of the HELOC exceeds 50 percent of the fair market value of the homestead. It is not the maximum loan to value amount of a HELOC. Under Section 50(t)(6), advances are prohibited until the principal balance of the HELOC is repaid to an amount equal to or less than 50 percent of the fair market value of the homestead. Each time a HELOC is paid down to 50 percent or less of the fair market value of the homestead, additional advances may be made by the lender, up to the limitation set forth in Section 50(t)(5). Paying a HELOC balance to zero does not prohibit further advances, unless the parties contract otherwise.

Two commenters expressed general support of §153.87. One of these commenters stated, “the plain language of the Constitution allows a HELOC up to 80% of the fair market value of the home. The fair market value limitation restricts additional advances if the amount of the HELOC exceeds 50% of the fair market value of the home at the time of loan closing. This interpretation seems appropriate and is supported by us.”

One commenter requested that the language “equal to or” be added to §153.87(3) immediately preceding the word “below.” The Commissions considered this request and added the phrase “equal to or” to more closely follow the plain language of the constitution.

One commenter disagreed with the “restriction of advances when the outstanding balance exceeds 50% of the fair market value.” The commenter argues that this restriction does nothing to protect a consumer and makes it more costly and difficult for a consumer to use the equity in their home. The Commissions considered this argument, but have determined that the constitution requires this limitation, and the Commissions have no authority to adopt an interpretation that contradicts Section 50(t)(6).

Section 153.88 interprets Section 50(t)(8), explaining the repayment schedule. Section 153.88(a) allows for semi-monthly scheduled payments not more often than

every 14 days. In computing a period of days, the first day is excluded, and the last day is included. Section 153.88(b) provides that the first repayment is not required to occur until two months after the first advance; if no advance is taken at the time the extension of credit is made, then the initial regular periodic payment must be scheduled to be paid no later than 60 days after the date of the first advance.

One commenter stated, "payment flexibility is important to consumers so we believe offering payments on the 15th and final day of the month will offer great benefits to credit union members." The commenter further expressed, "payments that coincide with pay dates would appeal to many consumers as well." Another commenter requested that language explaining that February is an anomaly and an exception to the requirement that payments not be made more often than once every 14 days be included in the interpretation and not just the preamble. The Commissions declined to modify the interpretation or address the issue in this preamble, but will further study the impact of February semi-monthly payment schedules.

One commenter expressed concern that §153.88 could be interpreted to prevent a borrower from electing a repayment schedule more frequently or otherwise different from the HELOC requirements of the constitution. The commenter requested that the following language be added: "Nothing in this section prohibits an owner from electing to voluntarily make payments on a schedule that is different from the repayment terms required by this section, so long as an election is not imposed or required by the lender." The Commissions considered this suggestion and clarified the interpretation by adding a subsection (c) which specifically allows a borrower to voluntarily prepay a HELOC on a more frequent schedule than is required by the lender.

One commenter said that there is a potential for confusion over the wording of §153.88(b) because it could be read to mean that a payment cannot be due until two months after the first advance. The commenter stated that "if the first advance is made on the next to last day of a statement cycle, the first interest payment may be due 30 days or less after the first advance." In order to make this language clearer, the commenter suggested rewriting §153.88(b) as: "Section 50(t)(8) does not require repayment of a HELOC to begin until two months after the initial advance. For example, if an advance is not made at the time of closing, repayment is not required to begin until after the first advance. If at any time there is no outstanding balance, then Section 50(t)(8) does not require a payment." The Commissions have considered this comment and disagree with the

commenter's analysis of the constitution and the Commissions' interpretation. Section 153.88(b) specifically states that "Repayment of a HELOC *is not required* to begin until two months after..." (Emphasis added). The language "is not required" only provides the latest date when repayment must begin. It does not mean that repayment must begin on a date two months following the advance. The Commissions decline to make the suggested changes.

The Finance Commission and the Credit Union Commission are working together to achieve the interpretive consistency required by §11.308 and §15.413, of the Texas Finance Code (as added by Chapter 1207 Acts of the 78th Legislature, Regular Session, 2003).

The interpretations are adopted under the provisions of Section 50(u), Article XVI, Texas Constitution and §11.308 and §15.413, Texas Finance Code as added by Chapter 1207 (Acts of the 78th Legislature, Regular Session, 2003), which authorize the Finance Commission and the Credit Union Commission to adopt interpretations of Sections 50(a)(5)-(7), (e) - (p), and (t), Article XVI, Texas Constitution.

§153.82.Owner Requests for HELOC Advance: Section 50(t)(1).

A home equity line of credit (HELOC) is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which the owner requests advances, repays money, and reborrows money. Any owner who is also a named borrower on the HELOC may request an advance. A HELOC agreement may contain provisions that restrict which borrowers may request an advance or require all borrowers to consent to the request.

§153.84.Restrictions on Devices and Methods to Obtain a HELOC Advance: Section 50(t)(3).

A HELOC is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which an owner is prohibited from using a credit card, debit card, preprinted solicitation check, or similar device to obtain a HELOC advance.

(1) A lender may offer one or more non-prohibited devices or methods for use by the owner to request an advance. Permissible methods include contacting the lender directly for an advance, telephonic fund transfers, and electronic fund transfers. Examples of devices that are not prohibited similar devices include prearranged drafts, convenience checks, or written transfer

instructions. Regardless of the permissible method or device used to obtain a HELOC advance, the amount of the advance must comply with:

- (A) the advance requirements in Section 50(t)(2);
- (B) the loan to value limits in Section 50(t)(5); and
- (C) the debit or advance limits in Section 50(t)(6).

(2) An owner may, but is not required to, make in-person contact with the lender to obtain a HELOC advance.

(3) A credit card, which is a prohibited device under Section 50(t)(3), is a card that may be used for personal, family, or household use to debit an open-end account.

(4) A preprinted solicitation check, which is a prohibited device under Section 50(t)(3), is a check that:

(A) is provided to an owner for the purpose of originating a HELOC or to a borrower for the purpose of soliciting additional advances on an existing HELOC;

(B) contains at least one preprinted key payment term, such as the amount or payee; and

(C) is not requested by the borrower or owner.

§153.85. Time the Extension of Credit is Established: Section 50(t)(4).

(a) A HELOC is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which fees described in Section 50(a)(6)(E) are charged and collected only at the time the extension of credit is established and no fee is charged or collected in connection with any debit or advance.

(b) For the purpose of this section, the time the extension of credit is established for a HELOC refers to the date of closing.

§153.86. Maximum Principal Amount Extended under a HELOC: Section 50(t)(5).

A HELOC is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which the maximum principal amount that may be extended under the account, when added to the aggregated total of the outstanding principal balances of all indebtedness secured by the homestead on the date the extension of

credit is established, cannot exceed 80 percent of the fair market value of the homestead on the date the extension of credit is made.

(1) At the time the initial or subsequent advance is made, the principal amount of the advance must comply with Section 50(t)(5). The following amounts when added together must be equal to or less than 80 percent of the fair market value:

(A) the amount of the advance;

(B) the amount of the principal balance of the HELOC at the time of the advance; and

(C) the principal balance outstanding of all other debts secured by the homestead on the date of the closing of the HELOC.

(2) An advance under Section 50(t)(5) must meet the requirements of Section 50(t)(2).

(3) The maximum principal balance of the HELOC that may be outstanding at any time must be determined on the date of closing and will not change through the term of the HELOC.

(4) For purposes of calculating the limits and thresholds under Section 50(t)(5) and (6), the outstanding principal balance of all other debts secured by the homestead is the principal balance outstanding of all other debts secured by the homestead on the date of the closing of the HELOC.

§153.87. Maximum Principal Amount of Additional Advances under a HELOC: Section 50(t)(6).

A HELOC is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which no additional debits or advances can be made if the total principal amount outstanding exceeds an amount equal to 50 percent of the fair market value of the homestead as determined on the date the account is established.

(1) A subsequent advance may be made only when the outstanding principal amount of the HELOC is 50 percent or less of the fair market value.

(2) A subsequent advance is prohibited if the outstanding principal amount of the HELOC exceeds 50 percent of the fair market value.

(3) If the outstanding principal amount exceeds 50 percent of the fair market value and then is repaid to an amount equal to or below the 50 percent of the fair

market value, subsequent advances are permitted subject to the requirements of Section 50(t)(2) and (5).

§153.88.Repayment Terms of a HELOC: Section 50(t)(8).

(a) A HELOC is a form of an open-end account that may be debited from time to time, under which credit may be extended from time to time and under which repayment is to be made in regular periodic installments, not more often than every 14 days and not less often than monthly, beginning not later than two months from the date the extension of credit is established, and during the period during which the owner may request advances, each installment equals or exceeds the amount of accrued interest; and after the period during which the owner may request advances, installments are substantially equal.

(b) Repayment of a HELOC is not required to begin until two months after the initial advance. For example, if an advance is not made at the time of closing, the repayment period is not required to begin until after the first advance. If there is no outstanding balance, then a payment is not required.

(c) Nothing in this section prohibits a borrower from voluntarily making payments on a schedule that is more frequent or earlier than is required by a lender.

This agency hereby certifies that the adoption has been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority.

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Commissioner

Joint Financial Regulatory Agencies

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