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MEMORANDUM

TO: CLIENTS AND FRIENDS OF THE FIRM

FROM: Al Alsup

DATE: January 13, 2004

SUBJECT: HOME EQUITY LENDING UPDATE

I. INTRODUCTION: PROPOSITION 16 SIGNALS A NEW ERA IN TEXAS HOME EQUITY LENDING

Significant home equity reform measures approved by Texas voters effective September 29, 2003 should ease mortgage lenders' concerns about compliance with Texas constitutional homestead law and the threat of a Draconian forfeiture provision that had daunted many equity lenders and investors who considered Texas home equity loans too risky. Texas homeowners should benefit from a broader choice of equity loan product offerings, lower rates and overall borrowing costs, and secondary market efficiencies ultimately brought about by these home equity reforms.

The new amendments to Section 50, Article XVI of the Texas Constitution recast the dreaded constitutional "forfeiture provision" as a definitive "cure provision" that should virtually eliminate the risk to lenders that unintended deficiencies in documentation or closing procedures could have the consequence of forfeiture of loan principal and interest. Texas homeowners were thought to pay a premium interest rate because of this perceived risk and the reluctance of many risk-adverse mortgage lenders to originate and mortgage investors to make an efficient secondary market in Texas home equity loans. In addition to defusing the forfeiture risk, the Texas Finance Commission and Texas Credit Union Commission have now been delegated the power to interpret the complex and often ambiguous constitutional home equity provisions and adopt rules that provide compliance protections to mortgage lenders who in good faith rely on those interpretations.

The new home equity amendments were proposed by SJR 42, a joint resolution earlier passed by a required super-majority (2/3) vote of both houses of the 78th Texas Legislature, a copy of which is attached to this memorandum as Exhibit A. The proposed amendments appeared on the ballot as Proposition 16, which was approved by a simple majority of qualified voters at a special election on September 13 and was effective on the date of the official canvass of the election returns and certification of the vote by the Secretary of State on September 29, 2003. This brief memorandum summarizes those key home equity amendments and reports on related rulemaking activity of the Texas Finance Commission and Texas Credit Union Commission in adopting home equity interpretive rules, the Texas Department of Insurance in adopting procedural rules amending the form and coverage of the T-42.1 home equity endorsement to the mortgagee form of title insurance policy,

and actions by Fannie Mae revising its uniform instruments, including its forms of home equity notes, security instrument, and compliance affidavit, and issuing its related policy Announcement 03-10.

II. SUMMARY OF KEY HOME EQUITY AMENDMENTS

A. "FORFEITURE" PROVISION NOW PROVIDES CLEAR GUIDELINES FOR LENDERS TO CURE (a)(6) ERRORS AND DEFICIENCIES

Section 50(a)(6)(Q)(x) formerly provided for a Draconian forfeiture of all principal and interest of an equity loan "if the lender or holder fails to comply with the lender's or holder's obligations under the extension of credit within a reasonable time after the lender or holder is notified by the borrower of the lender's failure to comply."

This express forfeiture provision and the *strict compliance* standard traditionally applied by Texas courts when determining the validity and enforceability of homestead lien claims had been particular troubling to many traditional mortgage lenders because of the perceived risk that even unintended deficiencies in home equity documentation or procedures when making an (a)(6) equity loan could result in an unconscionable forfeiture of all principal and interest. Texas homeowners were thought to pay a premium interest rate because of this perceived risk and the consequent reluctance of many traditional mortgage lenders to originate, and secondary mortgage investors to make an efficient market in, Texas home equity loans.

The Texas Supreme Court in a 2001 landmark decision construing subsection (Q)(x), however, found that the legislature through enactment of this provision intended for lenders to have the right and opportunity to cure unintended deficiencies without the risk of forfeiture if acting promptly after being notified of any failure to comply with the constitution. The high court in *Doody v. Ameriquest Mortgage Co.*, 49 S.W.3d 342 (Tex. 2001), departed from the traditional *strict compliance* standard and generally characterized subsection (Q)(x) as a "cure provision" that permits lenders to cure mistakes. SJR 42 took its cue from the *Doody* decision and proposed to amend Subsection (Q)(x) to provide clear guidelines regarding the timing and procedural requirements that lenders must follow to invoke the protections of the (Q)(x) cure provision.

As amended, subsection (Q)(x) now provides a lender or holder of a home equity loan a 60-day period in which to cure any failure on its part to comply with its constitutional obligations after receiving notification from the borrower of a violation. Specifically, subsection (Q)(x) provides that a lender or any holder of a promissory note made in connection with a home equity loan is subject to forfeiture of all principal and interest of the loan for a failure to comply with its obligations under the loan *only* if the lender or holder "fails to correct the failure to comply not later than the 60th day after the date that the lender or holder is notified by the borrower" . . . of the violation. To correct the violation, the lender or holder must take one or more of the specific actions set out in subdivisions (Q)(x)(a) – (f), as applicable:

(a) ***Refund of Overcharges.*** If the borrower/owner has paid an amount to the lender or holder that exceeds the *3% fee cap* under Subsection (a)(6)(E) or another amount controlled by the Texas Constitution under Subsections (a)(6)(G) prohibiting *prepayment penalties* or (a)(6)(O) regulating *interest* charges, the lender or holder must pay to the borrower/owner an amount of money equal to any such overcharge.

(b) ***Acknowledgment of Partial Lien Invalidity***. If the principal amount of the loan at closing exceeds the limitations under Subsection (a)(6)(B) of *80% of the fair market value* of the homestead property (when added to the aggregate balances of all other valid encumbrances of record), the lender or holder must send the borrower/owner a written acknowledgment that the lien securing the home equity loan is valid only in the amount and to the extent that the amount does not exceed the 80% loan-to-value limitation.

If the loan purports to be secured by any real or personal property other than the homestead property as *additional collateral* prohibited by Subsection (a)(6)(H), the lender or holder must send the borrower/owner a written acknowledgment that the loan is not secured by any such additional real or personal property.

Finally, if the loan purports to be secured by any homestead property designated for *agricultural use* prohibited by Subsection (a)(6)(I), the lender or holder must send the borrower/owner a written acknowledgment that the loan is not secured by any such agricultural property. [*Note:* While avoiding a forfeiture (which arguably would require that fees, charges, and interest paid to date be disgorged), this curative action would appear to leave the hapless lender as holder of a non-recourse, unsecured loan.]

(c) ***Modification of Prohibited Terms.*** If the home equity loan contains any other amount, percentage, term, or other provision prohibited by Section 50, the lender or holder must (i) send the borrower/owner a written notice modifying the loan to conform to an amount, percentage, term, or other provision permitted by Section 50, and (ii) adjust the account of the borrower/owner to ensure that the borrower is not required to pay more than an amount permitted by the constitution and is not subject to any other term or provision prohibited by Section 50.

(d) ***Delivery of Signed Documents***. If the lender has (i) failed to provide the borrower/owner a copy of all documents signed by the borrower/owner related to the home equity loan at the time of closing as required by Subsection (Q)(v) or (ii) failed to obtain the required signatures of the owner and/or the lender on the written acknowledgment of fair market value as required by Subsection (Q)(ix), the lender or holder must deliver the required documents to the borrower.

(e) ***Acknowledgment of Abatement of Interest and Obligations***. If the lender has made a home equity loan on a homestead property that already has a home equity debt secured on the same property made under Subsection (a)(6) or a reverse mortgage debt secured on the same property made under Subsection (a)(7) in violation of Subsection (a)(6)(K), the lender or holder must send the borrower/owner a written acknowledgment that the accrual of interest and all of the owner's obligations under the loan are abated while any such prior (a)(6) or (a)(7) lien remains secured by the same homestead property.

(f) ***Payment of $1,000 Penalty and Offer of "No Cost" Refinancing***. If the lender when making a home equity loan has failed to comply with any constitutional obligation that cannot be cured under any of the foregoing subdivisions (a) – (e), the lender or holder may cure the failure to comply by (i) a refund or credit to the borrower/owner of the sum of $1,000 *and* (ii) an offer to the borrower/owner of the right to refinance the home equity loan with the lender or holder for the remaining term of the loan at no cost to the borrower/owner on the same terms, including interest, as the original home equity loan (with any modifications in terms necessary for the loan to comply with Section 50 requirements or on such terms as the lender or holder and the borrower otherwise may agree upon). [*Note*: Such a refinancing made under

the cure provisions of subdivision (Q)(x)(f) is excepted from the seasoning limitations of amended Subsection (a)(6)(M)(iii), which otherwise would prohibit the refinance of an (a)(6) equity loan before the first anniversary of the closing date of the loan.]

Although subdivisions (a) – (e) seem to provide clear guidelines for a lender to cure the more common constitutional deficiencies and subdivision (f) is designed to provide a means of curing violations that otherwise do not lend themselves to such easy cure (including, for example, the failure of the lender to have deferred the loan closing for a 12-day "cooling off" period under Subsection (a)(6)(M)), all risks of forfeiture are not eliminated by the revamped (Q)(x) cure provision. Two violations particularly are excepted from the cure provision under Subsection (Q)(xi), and the lender or holder of a home equity loan expressly would forfeit all principal and interest of the loan:

- *If* the loan is made by a lender that is not authorized by Subsection (a)(6)(P) to make home equity loans [Note: Licensed Texas mortgage brokers were added as a new category of authorized lenders under new subdivision (P)(vi).]; or

- *If* the lien securing the loan was not created under a written agreement with the consent of each owner *and* each owner's spouse as required by Subsection (a)(6)(A) (*unless* the lender subsequently obtains the written consent of each owner and each owner's spouse who did not initially consent).

Furthermore, uncertainties persist regarding the precise procedures that lenders must follow to invoke the protections of the (Q)(x) cure provisions. For example, although the borrower/owner is required to first give notice of a violation to the lender to start the running of the 60-day period in which the lender or holder must act to cure the violation, the form and the manner of delivery of such a notice is not specified. The notice is not expressly required by the constitution to be in writing or delivered to the lender or holder at any particular address or by any particular means. Arguably, an unrecorded complaint made orally by telephone call to the holder's loan servicing department or even to the lender's branch production office might suffice as notice that initiates the running of 60-day cure period. Lenders may need to redraft notice provisions set out in their standard forms of promissory notes and security instruments documenting home equity loans for that reason to require that the borrower make any notice required under the loan documents or the constitution or statutes of the State of Texas in writing and deliver or mail the notice to a particular centralized address where trained personnel may log them in and process the notices appropriately (although such a provision might not be enforced by the courts as an effective waiver of vested constitutional rights of the owner under (Q)(x) to provide notice by any means). Moreover, the 60-day period appears to be an absolute, and no *mailbox rule* has been provided in the amendment that would deem the lender's notice or other required curative action to be timely if mailed properly stamped and postmarked by midnight of the 60th day. Similarly, no provision has been made for curative efforts that are begun within the 60-day period and diligently pursued, but not completed by midnight of the 60th day.

B. THE LEGISLATURE IS NOW AUTHORIZED TO DELEGATE TO ONE OR MORE STATE AGENCIES THE POWER TO INTERPRET SUBSECTIONS (a)(5) HOME IMPROVEMENT, (a)(6) HOME EQUITY, AND (a)(7) REVERSE MORTGAGE PROVISIONS AND THEREBY PROVIDE LENDERS "RELIANCE ON RULE" PROTECTIONS.

One of the criticisms of the 1997 legislation amending the Texas Constitution to first authorize home equity lending in Texas was that no implementing legislation accompanied the amendment and no state agency was delegated rulemaking authority to provide interpretive guidance to mortgage lenders and homeowners seeking to comply with the complex and often ambiguous requirements of

Section 50. The Office of the Attorney General refrained from responding to numerous requests for interpretations of the new constitutional provisions by calling on the legislature in a May 29, 1998 letter to revisit Section 50 and to provide a mechanism for giving lenders and consumers interpretive guidance:

> "Furthermore, we believe that the legislature should be given the opportunity to revisit section 50 in the next legislative session. As we have said, no state agency was given regulatory authority to construe or enforce the amendments, nor was any enabling legislation passed or mandated in conjunction with the changes. The five opinion requests submitted to this office are a strong indication of the number of questions raised by the amendments and the uncertainty facing lenders, builders, insurers, consumers, and others in creating enforceable loans pursuant to the new law. The legislature may wish to remedy the state of uncertainty by giving express regulatory power to an agency, by enabling legislation, or by proposing further amendments to section 50."

Months later on December 21, 1998, the Office of the Attorney General issued its Opinion No. DM-495 addressing whether the legislature may legally authorize and empower a state agency to construe and interpret the provisions of Section 50, Article XVI, Texas Constitution, regarding home equity loans absent a constitutional amendment. The answer, strictly read, was that "the legislature has no authority to interpret or declare a matter of constitutional construction, nor may it delegate such authority to an administrative agency" absent express constitutional authority. Although the legislature may not infringe upon the power of the judiciary to construe and interpret the constitution, the Attorney General nevertheless clarified that under its plenary powers the legislature may authorize a state agency to adopt rules implementing the home equity amendment that are subject to review but that may be given weight in the discretion of the courts, unless clearly wrong.

In recognition of the need for interpretive guidance, the Office of the Consumer Credit Commissioner (in conjunction with the state's Department of Banking, Savings & Loan Department, and Credit Union Department) undertook to issue a *Regulatory Commentary on Equity Lending Procedures*, which was last revised and issued October 7, 1998, in an attempt to provide unofficial interpretive guidance to lenders and consumers regarding the meaning and effect of the provisions of the amendment — while acknowledging that Texas courts may not defer to the agencies' interpretations. In fact, the Texas Supreme Court did show passing deference to the *Regulatory Commentary on Equity Lending Procedures* in *Stringer v. Cendant Mortgage Corporation*, 23 S.W.3d 353 (Tex. 2000) when construing Subsection (a)(6)(Q)(i), which prohibits a lender from requiring that the borrower/owner use home equity loan proceeds to repay another debt to the lender that is not already secured on the homestead property. The Supreme Court cited the commentary in support of its own conclusions and showed it particular credence, considering that no constitutional or statutory authority then existed for these agencies to interpret the Texas Constitution and that no protections from liability were afforded lenders who in good faith rely on those interpretations. The court signaled its willingness to look to the commentary in future cases with the following praise:

> "Although the commentary is advisory and not authoritative, it represents four Texas administrative agencies' interpretation of the Home Equity Constitutional Amendment. These agencies are responsible for regulating the entities that make home equity loans. The Commentary's purpose is to provide guidance to lenders and consumers about the regulatory views on the meaning and effect of article XVI, section 50." "Furthermore, we believe that the legislature should be given the opportunity to revisit section 50 in the next legislative session. As we have said, no state agency was given regulatory authority to construe or enforce the amendments, nor was any enabling legislation passed or mandated in conjunction with the changes. The five opinion requests submitted to this office are a strong indication of the number of questions raised by the amendments and the uncertainty facing lenders, builders, insurers, consumers, and others in creating enforceable loans pursuant to the new law. The legislature may

wish to remedy the state of uncertainty by giving express regulatory power to an agency, by enabling legislation, or by proposing further amendments to section 50."

SJR 42 seemed to take its cue from the Supreme Court in providing the express constitutional authority for the legislature to delegate interpretive power to one or more state agencies. Specifically, new Subsection 50(u) provides that the legislature by statute may delegate one or more state agencies the power to interpret Subsections (a)(5) – (a)(7), (e) – (p), and (t) pertaining to home improvement loans, home equity loans, and reverse mortgage loans. Furthermore, new Subsection 50(u) provides constitutional "reliance on rule" protections to lenders relying on interpretations of state agencies that are delegated interpretive authority. Specifically, the constitution provide that any act or omission by a lender does not constitute a violation of any provision of those subsections if the act or omission conforms to an interpretation of the provision that is in effect at the time of the act or omission and made by a state agency to which the power of interpretation is delegated or an interpretation made by a Texas or federal appellate court.

C. CONSTITUTIONAL PROHIBITION AGAINST OPEN-END ACCOUNTS WAS AMENDED TO AUTHORIZE A TYPE OF HOME EQUITY LINE OF CREDIT (HELOC)

Subsection (a)(6)(F) formerly prohibited home equity line of credit loans, or HELOCs, popular in other states by defining a Texas home equity loan in part as an extension of credit that "is not a form of open-end account that may be debited from time to time or under which credit may be extended from time to time." SJR 42 amended Subsection (a)(6)(F) to provide that open-end accounts are prohibited "unless the open-end account is a home equity line of credit" as defined by new Subsection (t). This reform measure authorizes for the first time in Texas a form of home equity line of credit that permits homeowners, subject to limitations, to borrow against the built-up equity in their homes in requested advances from time to time when the homeowner has a specific use or need for the money. Homeowners should be able to minimize their costs of borrowings under line of credit terms by fixing the amount and timing of their borrowings to coincide with their needs, such as when college tuitions or property taxes are due.

As amended, new Subsection (t) defines an authorized Texas home equity line of credit as "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 . . .":

(1) ***Revolving Line of Credit.*** The borrower/owner requests advances, repays money, and "reborrows" money;

(2) ***$4,000 Minimum Advance.*** Any single debit or advance is not less than $4,000;

(3) ***No Credit Card.*** The borrower/owner does not use a credit card, debit card, preprinted solicitation check, or similar device to obtain an advance;

(4) ***No Advance Fees.*** Any fees charged by the lender are charged and collected only at loan closing (subject to the 3% fee cap provisions) and no fee is charged or collected in connection with any debit or advance;

(5) ***80% Loan to Value Limitation.*** The maximum principal amount that may be extended under the account (when added to the aggregate total of all other indebtedness secured by the homestead property as of the date of closing) does not exceed 80% of the fair market value of the homestead as provided under Subsection (a)(6)(B);

(6) ***50% Outstanding Balance to Value Limitation.*** No additional debits or advances are made if the total principal amount outstanding exceeds an amount equal to 50% of the fair market value of the homestead property determined as of the date of closing;

(7) ***No Unilateral Amendment***. The lender or holder may not unilaterally amend the terms of the loan; and

(8) ***Regular Periodic Repayment Installments.*** Repayment is made in regular periodic installments that are not more frequent than every 14 days and not less frequent than monthly and that commence not later than two months from the date the extension of credit is established; and

- during the draw period in which the borrower/owner may request advances, each such installment equals or exceeds the amount of accrued interest; and

- after the draw period in which the borrower/owner may request advances, installments are made in substantially equal amounts.

A Texas home equity line of credit loan, of course, may be made only under, and subject to, the 25 or more conditions of Section 50(a)(6) applicable to other Texas home equity loans, except as modified by subsection (t). A Texas HELOC conforming to these constitutional requirements differs from typical HELOC loan programs in other jurisdictions where borrowers are permitted to draw any amount up to a maximum limit unilaterally established by the lender from time to time and to repay the loan in minimum monthly payments of only 1.5% of the unpaid principal balance — with a resulting large balloon payment at the end of a 5-10 year term that often must be refinanced. Moreover, an annual fee and transaction fees in connection with each draw requested and the release or reconveyance of the security upon satisfaction of the loan typically are charged the borrower in addition to interest.

Texas law in contrast only permits lenders to charge homeowners fees, other than interest, at loan closing and restricts their borrowings with respect to (i) a minimum amount of each advance (i.e., not less than $4,000), (ii) a maximum loan limit (i.e., not exceeding, when combined with other homestead debt, 80% of the homestead property's fair market value as of the date of closing), and,(iii) after closing and the initial loan disbursement, a prohibition on subsequent advances if, and so long as, the principal balance of the loan exceeds 50% of the homestead property's fair market value as of the date of closing. Furthermore, the terms of repayment (after an initial draw period in which interest only may be charged) require that bi-weekly or monthly payments be fixed in substantially equal amounts (i.e., presumably in equal amount adequate to amortize the unpaid balance over the remaining term of the loan) and thereby prohibits a balloon payment at maturity. These constitutional limitations are thought to be consumer protection provisions designed to assure that Texas homeowners will not over-extend their borrowings and risk losing their homesteads through foreclosure.

D. LENDERS ARE NOW REQUIRED TO PROVIDE HOMEOWNERS A NEW ITEMIZED DISCLOSURE OF ACTUAL FEES AND CHARGES AT LEAST ONE DAY BEFORE LOAN CLOSING.

Texas home equity loans are conditioned on certain consumer notice and timing requirements intended to provide homeowners the protections before closing of a substantial "cooling off" period during which the homeowner may reflect on the decision before undertaking an indebtedness that places the family homestead at risk and a "seasoning" requirement to discourage "flipping" practices in which equity in the homestead could be stripped through a series of refinancings initiated by the same lender in which front-end fees are loaded into the principal debt and total indebtedness is incrementally increased. Subsection 50(a)(6)(M)(i) in that regard defines a Texas home equity loan in part as an extension of credit that is not closed before the 12th day after the later of the date that

the homeowner submits a loan application to the lender for an equity loan or the date that the lender delivers to the homeowner a promulgated form of Notice Concerning Extensions of Credit Defined by Section 50(a)(6), Article XVI, Texas Constitution (the "12-Day Notice") as set out in full in Section 50(g). Furthermore, if the loan is to refinance another home equity loan secured on the same homestead property, Subsection 50(a)(6)(M)(ii) provides that the loan may not be closed before the first anniversary of the closing date of the preexisting equity loan to be refinanced.

New Subsection 50(a)(6)(M)(ii) now further provides that a home equity loan may not be closed before one business day after the homeowner receives a final itemized disclosure of the actual fees, points, interest, costs, and charges that will be charged to the borrower at closing:

> "(M) is closed not before:
>
> . . .
>
> (ii) one business day after the date that the owner of the homestead receives a final itemized disclosure of the actual fees, points, interest, costs, and charges that will be charged at closing. If a bona fide emergency or another good cause exists and the lender obtains the written consent of the owner, the lender may provided the documentation to the owner or the lender may modify previously provided documentation on the date of closing; and . . .
>
> [*Note*: Former Subsection 50(a)(6)(M)(ii) containing the one-year equity loan seasoning requirement has been renumbered as Subsection 50(a)(6)(M)(iii) and is otherwise unchanged.]

This requirement for delivery of yet another written disclosure to the homeowner as a constitutional condition of closing was a late floor amendment to SJR 42 penned by Rep. Steve Wolens (Dem.-Dallas) before the bill was laid before the Senate for concurrence in the 11th hour of the Regular Session. Of course, the federal Real Estate Settlement Procedures Act (RESPA) already requires that a Good Faith Estimate of all such fees and charges be provided loan applicants within three business days after loan application and that actual fees and charges be itemized and given to borrowers at loan closing in the form of the HUD-1 Settlement Statement. RESPA also requires that the settlement agent permit borrowers to inspect the HUD-1 Settlement Statement, completed to set forth those items then known to the settlement agent, during the business day immediately preceding the date of closing. Courts have construed this provision as not requiring that the HUD-1 be completed and delivered to the borrower on the business day preceding a scheduled closing, but instead merely requiring that the HUD-1 be made available for the borrower's inspection at the offices of the title company or other settlement agent during regular business hours on the preceding business day.

But the provisions of new Subsection 50(a)(6)(M)(ii) are more restrictive than the RESPA requirements in that the new constitutional disclosure must be delivered to the homeowner at least one day before the date of loan closing and it must contain an itemization of "*actual* fees, points, interest, costs, and charges." In practice, actual fees and charges often are not known until the lender's closing instructions and invoices from third-party settlement service providers are received by the settlement agent responsible for preparing the settlement statement — often only minutes before a scheduled closing. Presumably, because the requirement for the advance disclosure of actual charges is now embedded as a constitutional condition to the creation of a valid lien, equity loan closings sometimes may have to be deferred and rescheduled at least one day should any fee be altered or amended after deliver of the disclosure. Because no particular form of the disclosure is prescribed, a completed HUD-1 Settlement Statement delivered to the homeowner one business day preceding the date of closing satisfies this notice requirement. Although closings of home equity loans theoretically could still be accomplished on the 12th day following the date of loan application

and delivery of the 12-Day Notice by providing the Subsection 50(a)(6)(M)(ii) notice on the 11th such day, title agents serving as settlement agents must significantly alter their former practices and procedures in order to determine final, unalterable figures and provide a written itemization of all such amounts one day prior to a scheduled loan closing.

One exception to the timing requirement for delivery of the new disclosure arises if "a bona fide emergency or other good cause exists" and the lender obtains the written consent of the owner. In that event only, the lender may satisfy the disclosure requirements of new Subsection 50(a)(6)(M)(ii) by providing the written itemization of actual charges to the homeowner (or modifying a previously provided itemization) on the date of closing. Significantly, key terms as "business day," "bona fide emergency," and "good cause," which were used but undefined in the constitutional amendments, have now been defined by an interpretive rule adopted by the Finance Commission and the Credit Union Commission discussed in Section III. A. of this memorandum.

E. LENDERS ARE NOW AUTHORIZED TO REFINANCE AND REPLACE A HOME EQUITY LIEN WITH THE PROCEEDS OF A REVERSE MORTGAGE (AS AN EXCEPTION TO THE "ONCE A HOME EQUITY, ALWAYS A HOME EQUITY" RULE) BUT ARE STILL PROHIBITED FROM AFFIXING A REVERSE MORTGAGE LIEN ON THE SAME HOMESTEAD PROPERTY ENCUMBERED WITH A HOME EQUITY LIEN.

Many senior homeowners who had voted for the 1997 constitutional amendment authorizing Texas home equity and reverse mortgage loans for the first time had been denied eligibility for a reverse mortgage because they unwittingly took out a home equity loan to tide them over until reverse mortgages were actually available in the marketplace some three years later. These seniors were unaware that under the provisions of Section 50(f) proceeds from a reverse mortgage could not be used to refinance a home equity loan. The initial funding of a reverse mortgage loan is routinely used in part to pay-off and discharge any existing liens in order to attain first-priority lien status on the homestead.

Section 50(f), sometimes referred to as the "Once a home equity, always a home equity" provision, was generally construed to prohibit the refinance of any home equity loan with any loan other than another home equity loan (presumably to prevent a lender from evading the extensive (a)(6) consumer protections once the equity loan is refinanced and replaced by a traditional mortgage loan).

But Section 50(f), as amended, now authorizes an (a)(6) home equity loan to be refinanced *either* by another (a)(6) home equity loan *or* an (a)(7) reverse mortgage, and reads as follows:

> (f) A refinance of debt secured by the homestead, any portion of which is an extension of credit described by Subsection (a)(6) of this section, may not be secured by a valid lien against the homestead unless the refinance of the debt is an extension of credit described by Subsection (a)(6) **or (a)(7)** of this section. [emphasis added]

This amendment to Section 50(f) restores the promise to Texas's senior homeowners that was intended by the Texas Legislature and Texas citizens when voting to establish a constitutional right for senior Texas homeowners to use their own home equity as a resource for borrowings needed to live out their "Golden Years" in the comfort and security of their own homes, if they so choose. Importantly, these reforms preserve many of the extensive consumer protections of the 1997 and 1999 home equity amendments. Constitutional safeguards such as non-recourse liability, restrictions on events of default, and judicial process foreclosures in certain instances are preserved intact under this amendment.

Although lenders may replace an (a)(6) equity loan secured on a homestead property with a reverse mortgage loan, Subsection(a)(6)(K) still prohibits making a reverse mortgage loan to a homeowner that is secured on the same homestead property already securing an (a)(6) home equity loan. That is to say a homestead may not be encumbered with both an (a)(6) home equity lien and an (a)(7) reverse mortgage lien at the same time. Subsection(a)(6)(K) defines a home equity loan in part as "the only debt secured by the homestead at the time the extension of credit is made unless the other debt was made for a purpose described by Subsections (a)(1) – (a)(5) *or Subsection (a)(8)* of this section." This provision has the effect of prohibiting more than one home equity loan to be secured on the same homestead property at any one time or any home equity loan to be secured on the same homestead property at the same time as a reverse mortgage loan.

F. FORM OF "12-DAY NOTICE" HAS BEEN AMENDED TO INCORPORATE NEW DISCLOSURES ABOUT HELOC TERMS AND CURE PROVISIONS AND TO CORRECT DEFECTIVE DISCLOSURE LANGUAGE ABOUT APPLYING LOAN PROCEEDS TO PAY DEBTS TO THE SAME LENDER

A promulgated written form of Notice Concerning Extensions of Credit Defined by Section 50(a)(6), Article XVI, Texas Constitution is set out in full in Section 50(g). The lender must provide this so-called 12-Day Notice to the homeowner to commence a 12-day "cooling off" period before a Texas home equity loan may be closed. In an effort to simplify the explanations of the more complex provisions contained in the constitutional language, the 12-Day Notice lapsed into inaccuracies in several instances. One of the more pronounced of these inaccuracies involved the explanation of the provisions of Subsection (a)(6)(Q)(i) that "the owner of the homestead is not required to apply the proceeds of the [home equity loan] to repay another debt except debt secured by the homestead or debt to another lender." Under this provision, an equity loan cannot be conditioned on a requirement that the loan proceeds be used wholly, or in part, to discharge or repay another indebtedness owed the same lender, *except* a debt that is already validly secured by the homestead property. An apparent purpose of this provision is to prevent an unsecured creditor from demanding that the creditor be granted a security interest in the debtor's homestead as a condition for granting a forbearance, rearrangement or recasting of the unsecured indebtedness. While the language clearly would permit the lender to require that loan proceeds be used in part to repay an indebtedness already secured on the homestead (even if owed the same lender) or an unsecured debt owed another lender or creditor, the promulgated form of the 12-Day Notice conflicts with that clear meaning. Paragraph Q of the form of notice read in pertinent part as follows:

> (Q) LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MUST:
>
> (1) NOT REQUIRE YOU TO APPLY THE PROCEEDS TO ANOTHER DEBT THAT IS NOT SECURED BY YOUR HOME OR TO ANOTHER DEBT TO THE SAME LENDER;
>
> . . .

The issue whether homestead owners may be required to use loan proceeds in part to pay other creditors as a condition to a home equity loan was raised squarely in a certified question to the Texas Supreme Court by the federal Fifth Circuit Court of Appeals in *Stringer v. Cendant Mortgage Corporation*, 23 S.W.3d 353 (Tex. 2000). The circuit court had under review a claim by plaintiffs that they were unlawfully required to use a portion of their loan proceeds to pay off debts to creditors other than Cendant in contravention to the prohibition set out in paragraph Q of the 12-Day Notice. Although the notice provision conflicted in that regard with the constitutional language itself, plaintiffs contended that

any ambiguity between the provisions of the notice and the constitutional provision of Section 50(a)(6)(Q) should be resolved in favor of the notice, which Stringer contended "clearly and concisely" reflected the intent of the Texas Legislature. The question certified to the Texas Supreme Court by the circuit court at 199 F.3d 190, 192 (5th Cir. 1999) read as follows:

> Under the Texas Constitution, may a home-equity lender require the borrower to pay off third-party debt that is not secured by the homestead with the proceeds of the loan?

The Supreme Court answered the certified question *yes* and held "that under the Texas Constitution, a home equity lender may require a borrower to use loan proceeds to pay a third-party debt that is not secured by the homestead." The Supreme Court agreed with the Fifth Circuit court that the plain language of the constitutional provision and that of the notice conflict, but reasoned that the constitutional provisions of Section 50(a)(6)(Q)(i) establish the substantive rights and obligations of lenders and borrowers in this regard. The notice provisions set out in Section 50(g)(Q)(1) provide only the language of the mandatory notice to borrowers, the court held, and do not independently establish rights or obligations for the extension of the home equity credit. Based on this finding of state law, the Fifth Circuit thereupon affirmed the judgment of the trial court dismissing the case. In an unusual quasi-legislative initiative, the Supreme Court also sought to resolve the conflict between the substantive provisions of the constitution and the flawed notice summarizing those provisions that can mislead prospective home equity borrowers through the invention of an additional notice that the court stated lenders *should* provide in addition to the 50(g)(Q)(1) notice to identify the conflict between the two sections and explain the Section 50(a)(6)(Q)(i) substantive effect. This notice according to the Supreme Court should state:

> The notice above states that your home-equity lender may not require you to apply the loan proceeds to another debt that is not secured by your home. Although the Texas Constitution requires that the notice include this statement, the statement conflicts with another provision of the Texas Constitution. That provision permits your home-equity lender to require you to apply the loan proceeds to a debt to another lender that is not secured by your home. This provision is controlling, and you should disregard the contrary statement in the notice.

Section 50(g), as amended, now corrects the defective explanation in the 12-Day Notice that the *Stringer* decision struck down to read in pertinent part as follows (corrections indicated and emphasized):

> "(Q) LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MUST:
>
> "(1) NOT REQUIRE YOU TO APPLY THE PROCEEDS TO ANOTHER DEBT **EXCEPT A DEBT** THAT IS [~~**NOT**~~] SECURED BY YOUR HOME OR **OWED** TO ANOTHER [~~**DEBT TO THE SAME**~~] LENDER;

Although the amendments to the form of 12-Day Notice do not address other disclosures contained in the notice that arguably are similarly defective, including specifically subdivisions (E), (H), (L), and (M), the amended form does in effect codify the findings in *Stringer* that only the express provisions of the constitution itself may be relied upon to support a claim that a lender has failed to comply with its constitutional obligations. The amendments in that regard supercede the advice of the Texas Supreme Court in *Stringer* that an additional notice be provided to homeowners to disregard the defective notice, and substitutes for that additional notice the following legend:

THIS NOTICE IS ONLY A SUMMARY OF YOUR RIGHTS UNDER THE TEXAS CONSTITUTION. YOUR RIGHTS ARE GOVERNED BY SECTION 50, ARTICLE XVI, OF THE TEXAS CONSTITUTION, AND NOT BY THIS NOTICE.

These and other amendments to the promulgated form of 12-Day Notice, including those pertaining to the newly authorized home equity line of credit terms, are illustrated in Exhibit B to this memorandum. Ironically, the amended form of 12-Day Notice, which was intended to clear up the ambiguities left by prior legislatures, itself failed to take into account and disclose the requirements of new Subsection 50(a)(6)(M)(ii) for a one-day advance disclosure of actual fees, points, interest, costs, and charges that will be charged to the borrower at closing. The authority for lenders to supplement the form of the 12-Day Notice to incorporate this disclosure is discussed in section III.B of this memorandum.

G. Licensed Texas Mortgage Brokers are now Authorized to Make Home Equity Loans for the First Time.

Section 50(a)(6)(P) enumerates the only categories of lenders that are authorized to make a first- or second-lien home equity loan, which prior to the 2003 home equity reform amendment included only:

> "(i) a bank, savings and loan association, savings bank, or credit union doing business under the laws of this state or the United States;
> (ii) a federally chartered lending instrumentality or a person approved as a mortgagee by the United States government to make federally insured loans;
> (iii) a person licensed to make regulated loans, as provided by statute of this state;
> (iv) a person who sold the homestead property to the current owner and who provided all or part of the financing for the purchase; or
> (v) a person who is related to the homestead property owner within the second degree of affinity or consanguinity."

Strictly construed, it has been assumed by legal practitioners that a purported equity loan made by a lender not expressly authorized by this constitutional provision would be void, at least for purposes of creating an effective lien on a homestead property. That has meant that the presumed but ambiguous authority of some traditional mortgage originators who make or arrange equity loans but who do not clearly fit within any of these other enumerated categories of authorized lenders, such as mortgage brokers, FHA correspondents, VA lenders, and foreign state-chartered banks, could be the grounds for a claim of lien invalidity under Section 50(a)(6)(P).

Mortgage brokers, who were unlicensed under Texas law until the 1999 enactment of the Texas Mortgage Broker License Act and fit none of the categories of authorized lenders, seized on the distinction between the act of "making" and that of "arranging" a loan to justify their home equity loan origination activities. Because only the "making" of an equity loan appears to be regulated by Section 50(a)(6)(P), mortgage brokers argued that their activity of "negotiating," or "arranging" a home equity loan is not prohibited. Mortgage brokers contended that so long as the equity loan were closed in the name of an authorized lender (i.e., the constitutionally authorized lender is the named payee in the note evidencing the loan) and closed with funds advanced by the authorized lender from its own resources or a banking warehouse line of credit for which the lender is liable, the equity loan would have been "made" by the authorized lender within the meaning of this constitutional provision — notwithstanding that the mortgage broker performed various loan origination, processing, and related services in connection with the loan for which it will be compensated. The joint agencies' *Regulatory Commentary*

on Equity Lending Procedures of October 7, 1998, supported this rationale that a mortgage broker only "negotiating or arranging" a first-lien equity loan or a secondary lien equity loan providing for annual interest of 10%, or less, would *not* be required to be licensed to carry on these activities.

> [*Note*: If an equity loan in any case is secured by a secondary, or subordinate, mortgage subject to Chapter 342, Texas Finance Code, the mortgage broker more clearly would be required to be a Consumer Loan licensee under new Chapter 342 because the regulated activity under the Secondary Mortgage Loans provisions of that chapter expressly includes engaging in "the business of making, transacting, or *negotiating*, [secondary mortgage loans] … ."]

Section 50(a)(6)(P), as amended, now removes the necessity for such hairsplitting distinctions between "making" and "arranging" home equity loans by adding licensed Texas mortgage brokers as a category of lenders authorized to make home equity loans. As amended, new subdivision (P)(vi) defines an equity loan in part as an extension of credit that:

> "(P) is made by one of the following that has not been found by a federal regulatory agency to have engaged in the practice of refusing to make loans because the applicants for the loans reside or the property proposed to secure the loans is located in a certain area:
> . . .
> **(vi) a person regulated by this state as a mortgage broker; and"** [emphasis added]

This express authority of Texas licensed mortgage brokers to make home equity loans is particularly important in light of the amendment to Section 50(a)(6)(Q), which adds a new subdivision (xi) to read as follows:

> "(xi) the lender or any holder of the note for the extension of credit shall **forfeit all principal and interest of the extension of credit if the extension of credit is made by a person other than a person described under Paragraph (P) of this subdivision** [emphasis added] or if the lien was not created under a written agreement with the consent of each owner and each owner's spouse, unless each owner and each owner's spouse who did not initially consent subsequently consents;"

By enacting new subdivision (xi), the legislature apparently intends that home equity loans made by any person or entity not expressly authorized by Section 50(a)(6)(P) to make home equity loans will be void and subject to immediate forfeiture of all principal and interest. Moreover, when made by an unauthorized lender, home equity loans will not have the protections of the Section 50(a)(6)(Q)(x) cure provisions or require any notice or other action on the part of a homeowner as a condition of forfeiture. The possibility of forfeiture in this limited circumstance suggests that wholesale mortgage lenders and their assignees must have in place reliable screening procedures to verify that originators of home equity loans are authorized lenders under the provisions of Section 50(a)(6)(P) as either (i) a federal- or state-chartered depository institution, including expressly either a bank, savings and loan association, savings bank, or credit union; (ii) a HUD-approved mortgagee (i.e., a "a person approved as a mortgagee by the United States government to make federally insured loans); (iii) a licensed regulated lender under Chapter 342, Texas Finance Code (regarding consumer and secondary mortgage loans); or (vi) a licensed mortgage broker under Chapter 156, Texas Finance Code.

III. OFFICIAL RULES INTERPRETING HOME EQUITY PROVISIONS OF THE TEXAS CONSTITUTION ADOPTED BY THE JOINT FINANCIAL REGULATORY AGENCIES

A. THE FINANCE COMMISSION AND CREDIT UNION COMMISSION ADOPT OFFICIAL HOME EQUITY LENDING INTERPRETATIONS EFFECTIVE JANUARY 8, 2004 THAT PROVIDE "SAFE HARBOR" PROTECTIONS TO MORTGAGE LENDERS.

As one of their first official acts under their new delegated rulemaking authority discussed in section II B. of this memorandum, The Texas Finance Commission and the Texas Credit Union Commission (the "Commissions") adopted official home equity lending interpretations at a joint agency meeting held December 18, 2003. The interpretations are codified in the Texas Administrative Code as 7 TAC Chapter 153 and were published in the Texas Register on January 2, 2004 (29 Tex.Reg. 1) to be effective January 8, 2004 (the "Home Equity Lending Interpretations"). The power to interpret constitutional home equity lending provisions was expressly delegated to the Texas Finance Commission (with respect to constitutionally authorized home equity lenders) and to the Credit Union Commission (with respect to the credit union lenders regulated by that commission) by SB 1067, which amended Chapters 11 and 15 of the Texas Finance Code to that effect as of September 29, 2003.

The Commissions also adopted home equity lending procedures codified in 7 TAC §§151.1-151.8, inclusive, to regulate the process by which future interpretations are to be undertaken and issued. The Texas Finance Commission or Credit Union Commission are authorized on request of an interested person or on its own motion to issue interpretations of Subsections 50(a)(5)–(7), inclusive, 50(e)–(p), inclusive, and 50(t) and (u).The Finance Commission and Credit Union Commission are required to attempt to adopt interpretations that are as consistent as feasible (or they must state the justification for any inconsistency). Interpretations of these agencies are subject to the uniform policies and procedures of the Administrative Procedures Act, Chapter 2001, Texas Government Code.

The Final Rule of the Commissions is significant not only for the general interpretive guidance it provides the mortgage lending industry, but also because it provides "safe harbor" protections to mortgage lenders who perform acts or omissions in good faith reliance on the Commissions' official interpretations that may later be determined by a court or other authority to violate the Texas Constitution. Subsection 50(u) in that regard provides that any act or omission by a lender does not constitute a violation of any provision of those subsections if the act or omission conforms to an official interpretation of the provision that is in effect at the time of the act or omission and made by a state agency to which the power of interpretation is delegated or an interpretation made by a Texas or federal appellate court. Appellate courts generally defer to a regulatory agency's interpretations of statutes when the agency has been delegated interpretive authority by Congress or a state's legislature unless the agency's interpretation is found by the reviewing court to conflict with the "plain meaning" of the statute. Even in those cases, however, no provision of the constitution otherwise imposing liability on a mortgage lender for a violation would be found to apply to any act done or omitted in good faith conformity with an official interpretation of that provision by the Commissions even if after the act or omission the interpretation were amended, rescinded, or determined by a court or other authority to violate the Texas Constitution.

B. OVERVIEW OF HOME EQUITY LENDING INTERPRETATIONS ADOPTED BY THE COMMISSIONS EFFECTIVE JANUARY 8, 2004

The Home Equity Lending Interpretations are codified in the Texas Administrative Code (TAC) at 7 TAC Chapter 153, §§153.1-153.5, inclusive, 153.7-153.18, inclusive, 153.18, 153.20, 153.22, 153.24, 153.24, 153.41, and 153.51, which may be viewed in their entirety at http://wwwfc.state.tx.us/home%20equity/ch153adop.htm. The interpretations are based upon and

replace the informal *Regulatory Commentary on Equity Lending Procedures* by the Joint Financial Regulatory Agencies dated and issued October 7, 1998, as described in section I.B. of this memorandum, with few substantive revisions.

Although a comprehensive analysis of the Home Equity Lending Interpretations is beyond the scope of this brief memorandum, the following provisions are noteworthy for the additional guidance provided the mortgage lending industry and the affirmation in some instances of established industry practices. Section references are to subsections of 7 TAC Chapter 153.

§153.1 Definitions

(2) *Business Day*. The Commissions adopted the identical definition used in Regulation Z for federal right of rescission purposes to mean "all calendar days except Sundays and these federal legal public holidays: New Year's Day, Martin Luther King's Birthday, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veterans Day, Thanksgiving Day, and Christmas Day."

(6) *Date the Extension of Credit is Made*. The Commissions clarified that this frequently used term in the constitution means the date of closing and not the later date of funding. *Closing* in turn is defined as the date on which the owner and spouse (if any) sign the *equity loan agreement* or the date of signing the *equity loan agreement* on their behalf.

(13) *Owner*. The Commissions defined this frequently used term in the constitution broadly as "a person who has the right to possess, use, and convey, individually or with the joinder of another person, all or part of the homestead." As defined, *owner* would appear to include a non-titled, non-borrowing spouse of any record title owner. This is significant in determining the parties that must be provided the various consumer notices and must sign various documents to comply with constitutional requirements for creation of a lien under Section 50(a)(6).

§153.5 *Three Percent Fee Limitation.* The Commissions clarified through example the types of charges it regards as interest that are not subject to the 3% fee cap established by Section 50(a)(6)(E):

> (3) *Charges that are Interest*. Charges an owner or owner's spouse is required to pay that constitute interest under the law, for example per diem interest and points, are not fees subject to the three percent limitation.

This interpretation does not address the more controversial issue whether a lender's origination fee, which has been held by Texas courts to constitute interest for usury purposes, is deemed interest not subject to the 3% fee cap. In that regard, the Commissions beg the issue by stating only that charges "to originate an equity loan that are not interest are fees subject to the three percent limitation."

§153.8 *Security of the Equity Loan*. The Commissions clarified that taking a security interest in "easements necessary or beneficial to the use of the homestead, including access easements for egress and ingress" do not violate the Section 50(a)(6)(H) prohibitions against additional collateral. The Commissions did not address whether the acreage contained within an access easement appurtenant to

the homestead property would be included within the 10-acre limitation of an urban homestead. This interpretation has not yet addressed other additional collateral issues that arise, such as whether taking a security interest in a rented duplex dwelling unit or garage apartment making up a part of the homestead property recognized under Texas law constitutes impermissible additional collateral. The Commissions did clarify that a guaranty or surety of an equity loan would constitute impermissible additional collateral under this provision but did not address specifically whether co-signing of an equity note by a person cohabiting the homestead property but without an ownership interest would constitute such a prohibited surety. Consistent with that interpretation, the Commissions further stated that a lender is prohibited by Section 50(a)(6)(H) from contracting for a right of offset against an owners escrow funds maintained by the lender for payment of property taxes and insurance.

§153.9 *Acceleration.* The Commissions clarified that a cross-default clause allowing the lender to declare default in a subordinate home equity lien in the event of a default in a superior lien on the same homestead property does not violate Section 50(a)(6)(J) prohibitions against accelerating home equity indebtedness "because of the owner's default under other indebtedness not secured by a prior valid encumbrance against the homestead."

§153.10 *Number of Loans.* The Commissions clarified that if the homestead property encumbered with a home equity lien ceases to be a homestead under Texas law, that the lender may treat what was originally a home equity lien as a non-homestead loan. This suggests that if the owner of a property encumbered with a homestead lien were to acquire and establish occupancy in another Texas property that the erstwhile home equity lien may be refinanced without regard to constitutional limitations on the refinance of a home equity lien.

§153.12 *Closing Date*. The Commissions clarified the manner in which the 12-day "cooling off" period that must run before closing of a home equity loan is determined. Specifically, the next succeeding day after the day on which the homeowner is provided the 12-Day Notice is counted as the first day of the 12-day period and the loan closing may then occur at any time on or after the 12th calendar day.

§153.13 *Preclosing Disclosure*. The Commissions adopted extensive interpretations of new Section 50(a)(6)(M)(ii) requiring a one-day Preclosing Disclosure of actual fees and charges that will be charged at closing discussed in section II.D. of this memorandum, which read in their entirety as follow:

§153.13.Preclosing Disclosures: Section 50(a)(6)(M)(ii).

An equity loan may not be closed before one business day after the date that the owner of the homestead receives a final itemized disclosure of the actual fees, points, interest, costs, and charges that will be charged at closing. If a bona fide emergency or another good cause exists and the lender obtains the written consent of the owner, the lender may provide the documentation to the owner or the lender may modify previously provided documentation on the date of closing.

(1) A lender may satisfy the disclosure requirement of this section by delivery to the borrower of a properly completed Department of Housing and Urban Development (HUD) disclosure Form HUD-1 or HUD-1A.

(2) An owner may consent to receive the preclosing disclosure on the date of closing in the case of a bona fide emergency occurring before the date of the extension of credit. An equity loan secured by a homestead in an area designated by Federal Emergency Management Agency (FEMA) as a disaster area is an example of a bona fide emergency if the homestead was damaged during FEMA's declared incident period.

(3) To modify timing of the disclosure, the lender should obtain written consent from the owner that:

(A) describes the emergency;

(B) specifically states that the owner consents to receive the preclosing disclosure on the date of closing; and

(C) bears the signature of all of the owners entitled to receive the preclosing disclosure.

(4) A de minimus variance can be good cause at the owner's option. An owner who has received a preclosing disclosure may consent to receive a subsequent or modified preclosing disclosure on the date of closing under the good cause standard if:

(A) the actual disclosed fees, costs, points and charges on the date of closing do not vary from the initial preclosing disclosure by more than the greater of:

(i) $100 of the amount charged at closing or

(ii) 0.125 percent of the principal amount of the equity loan at closing; or

(B) one or more items in subparagraph (A) of this paragraph is less than the disclosed rate or amount on the initial preclosing disclosure.

(5) An owner may consent to receive the preclosing disclosure or a modification of the preclosing disclosure on the date of closing if another good cause exists. A condition that would cause the owner substantial financial hardship if the equity loan were not allowed to close on the scheduled date of closing is an example of other good cause.

(6) An equity loan may be closed at any time during normal business hours on the next business day following the calendar day on which the owner receives the preclosing disclosure or any calendar day thereafter.

The Commissions clarified through this interpretation that a home equity loan may be closed during normal business hours on the first business day after the calendar day on which the required Preclosing Disclosure is provided the owner or on any calendar day thereafter. The requirement that the closing occur during normal business hours seems to apply only if the loan is closed on the first business day, which under the adopted definition of *business day* may be a Saturday. If closed on any calendar day after the first business day, closing is not restricted to normal business hours. Presumably, *normal business hours* refers to the usual and customary hours of the title company, mortgage lender, or attorney at law acting as settlement agent and conducting the loan closing. The timing of delivery of the Preclosing Disclosure under this interpretation is not restricted and may occur at any hour on any calendar day.

The Commissions also set standards for the circumstances that may constitute a bona fide emergency or another good cause under Section 50(a)(6)(M)(ii) and thereby permit the lender, with the written consent of the owner, to provide the Preclosing Disclosure to the owner, or to modify a previously provided Preclosing Disclosure, on the scheduled date of closing so that the closing is not unnecessarily delayed. In that

regard, the Commissions determined that a de minimis variance in the fees and charges can be a good cause at the owner's option. The Commissions in §153.13(4) adopted a de minimis variance test under which very minor variances that occur between actual fees and charges disclosed on the final HUD-1 Settlement Statement at loan closing and the same fees and charges disclosed in the Preclosing Disclosure may be permitted. A closing could proceed at the owner's option on the scheduled closing date under this de minimis variance test *if* (i) any actual fee or charge at closing is less than the amount disclosed in the Preclosing Disclosure, and (ii) no one fee or charge, or all fees and charges in total, do not exceed the greater of $100 or .125 percent (1/8 %) of the principal loan amount. Accordingly, by way of example, a final HUD-1 Settlement Statement for a $150,000 home equity loan disclosing actual fees and charges at closing would satisfy the de minimis test if (i) no single fee or charge disclosed in the Preclosing Disclosure and (ii) the total of all fees and charges disclosed in the Preclosing Disclosure do not exceed the sum of $187.50 (or 1/8 % of $150,000).

§153.14 *One Year Prohibition*. The Commissions clarified that Section 50(a)(6)(M)(iii) prohibitions against closing a home equity loan before the first anniversary of the closing date of any other equity loan on the same homestead property does not apply to a *modification* in which terms of the loan are amended but the debt is not satisfied and replaced with a new debt note and security instrument. Modifications may not call for the advance of additional funds to a borrower and may not provide for new terms that would not have been permitted by applicable law at the date of loan closing. Furthermore, modifications of an equity loan must be made in writing and signed by both the borrower and lender except in any case in which applicable law may require a lender's unilateral modification of terms, such as to lower rates or suspend enforcement of terms under the Soldier's and Sailor's Civil Relief Act for borrowers who are in active military service.

[*Note:* This interpretation is consistent with a joint opinion letter dated December 20, 2001, (the "Joint Agency Letter") issued by the four Texas financial regulators, Texas Department of Banking, Texas Savings and Loan Department, Office of the Consumer Credit Commissioner, and the Texas Credit Union Department opining that (i) a lender may modify a home equity loan by reducing its interest rate and changing the amounts and/or the number of monthly payments without going through all the steps required by the Texas Constitution for a loan refinance and (ii) a modification may be undertaken by agreement of the lender and borrower at any time, even if before the first anniversary of the loan]

§153.15 *Location of Closing*. The Commissions clarified that Section 5(a)(6)(N) requiring that the closing of a home equity loan be conducted only at the office of the lender, attorney at law, or a title company does not prohibit the use of a power of attorney that authorizes a named attorney-in-fact to appear at the office and sign documents on behalf of the homeowner. Although this section would appear to prohibit "mail out" closings, §153.15(3) seems to permit presumably a non-borrowing spouse to provide the written consent to the home equity loan required in Section 50(a)(6)(A) by mail or delivery to the authorized physical location of the closing.

§153.16 *Rate of Interest*. The Commissions harmonized Section 50(a)(6)(O), which expressly permits a lender to contract for a variable rate of interest, with the provisions of Section 50(a)(6)(L) that require a home equity loan to be scheduled to repay the loan in fully amortizing, substantially equal successive monthly installments of principal and interest. Consistent with industry practices, the Commissions clarified that an equity loan with variable rate terms simply must

satisfy the requirement that scheduled payments be in substantially equal, successive monthly installments between each interest rate adjustment. Thus, on each change date the requirements of Section 50(a)(6)(L) are met if payments are calculated to fully amortize the outstanding principal balance over the remaining term of months in substantially equal, successive monthly payments. The Commissions also clarified that Section 50(a)(6)(O) permits a variable rate loan with an initial discounted rate or a fixed-rate loan in which interest is increased periodically in accordance with a schedule of stepped up rates.

§153.17 *Authorized Lenders*. The Commissions clarified that HUD-approved correspondents to HUD-approved mortgagees are not authorized lenders under provisions of Section 50(a)(6)(P) that authorize a person "approved as a mortgagee to make federally insured loans" unless qualifying under another category of authorized lenders under that section. Although not addressed by the Commissions, lenders approved only to make VA-Guaranty loans presumably would not qualify as an authorized lender under this provision either, unless qualifying under another category.

§153.22 *Copies of Documents.* The Commissions clarified that lenders are not required by the provisions of Section 50(a)(6)(Q)(v) at closing to provide owners copies of documents that were signed by the owner prior to closings, such as the loan application or other application documents. But copies of documents that are signed by the owner after closing, such as a confirmation of non-cancellation given after the running of the three day right of rescission, must be provided to the owner within three business days after signing.

§153.24 *Release of Lien.* The Commissions determined that thirty (30) days is a reasonable time for the lender to satisfy its Section 50(a)(6)(Q)(vii) requirements to cancel and return the note and release of lien after full payment of a home equity loan. The Commissions clarified a lender must perform these services without charge to the owner but is not required to record or pay for the recordation of the lien release instrument.

The Commissions emphasize that the Home Equity Lending Interpretations adopted in Chapter 153 are derived from its informal *Regulatory Commentary on Equity Lending Procedures* adopted by the Office of the Consumer Credit Commissioner in conjunction with the other state regulatory agencies as of October 7, 1998, with few substantive changes except to the extent the Commissions considered it necessary to clarify or expound upon that commentary. Furthermore, these interpretations are a beginning and will not preclude future consideration of other issues that may be raised on the request of an interested party or on the motion of the Commissions themselves. These interpretations are intended not only to construe the actual language of the constitutional provisions, but also to provide a practical framework for home equity lending that implements the constitutional language consistent with legislative intent.

C. Overview of Proposed Interpretations by The Finance Commission and Credit Union Commission of New Section 50(t) Authorizing Home Equity Line of Credit Loans (HELOCs)

The Commissions also have proposed for adoption new 7 TAC §§153.82, 153.84-153.88 interpreting new Section 50(t), Article XVI, Texas Constitution, which effective September 29, 2003, authorized

for the first time, home equity line of credit (HELOC) terms discussed in section II.C. of this memorandum. The proposed interpretations were published for public comment in the Texas Register (29 Tex. Reg. 1) on January 2, 2004, and the earliest possible date of adoption under applicable administrative rules is February 1, 2004. The proposed interpretations address a number of threshold questions raised by Section 50(t) provisions, such as who can request an advance under a HELOC, how may an advance be requested and obtained, when is the extension of credit established, what is the maximum principal amount that may be obtained for the initial and subsequent advances, and what restrictions apply to the terms of repayment. The following overview is excerpted from the commentary of the proposed interpretive rule:

Section 153.82 interprets Section 50(t)(1), clarifying that any owner who is also a borrower may request an advance, but allows for the parties to contract to require specific borrowers or all borrowers to consent to the request.

Section 153.84 interprets Section 50(t)(3), explaining the restrictions on methods of obtaining a HELOC advance. This section defines a preprinted solicitation check as an instrument not requested by an owner or borrower that is used to solicit an owner to obtain a HELOC or to solicit a HELOC borrower to get an advance, and one or more of the key payment terms is completed by the lender. The Commissions believe that if the legislature had intended all checks to be prohibited as methods of obtaining an advance, it would have used the general term "check" as opposed to the more specific "preprinted solicitation check." Accordingly, the interpretation provides that it is permissible to use convenience checks to obtain HELOC advances. Checks used to obtain advances must be written for a minimum amount of $4,000. Any advance must comply with both limitations contained in (t)(5) and (6). The Commissions believe that adequate procedures should be in place to ensure that checks used to obtain advances do not violate 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" is primarily intended to refer to unknown devices.

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.

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

Section 153.87 interprets the application of the fair market value limitation contained in Section 50(t)(6). The plain language of the constitution allows a HELOC to exceed 50 percent of the fair market value of the homestead.

The constitution allows for the principal amount of a HELOC to exceed the fair market value limitation contained in Section 50(t)(6). That fair market value limitation, however, restricts additional advances if the aggregated amount of the HELOC exceeds 50 percent of the fair market value of the homestead. No further advances may be made 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. At no time may a HELOC advance violate subsection (t)(2) or (5).

Section 153.88 interprets Section 50(t)(8), explaining the repayment schedule. 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 no payment is due until 60 days after the date of the first advance.

The interpretation 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. A payment schedule requiring payment the fifteenth and final day of the month will have a scheduled payment

period of less than every 14 days in the month of February in a year that is not a leap year. This is an anomaly and does not negate semi-monthly scheduled payments on the 15th and the last day of the month.

IV. TEXAS DEPARTMENT OF INSURANCE PROPOSES TO ADOPT AMENDMENTS TO PROCEDURAL RULES AND MODIFICATIONS OF FORMS OF T-42 AND T-42.1 ENDORSEMENTS TO ADDRESS INSURING ISSUES RAISED BY NEW HOME EQUITY REFORM MEASURES

The Texas Department of Insurance, acting upon the October 3, 2003, petition of James L. Gosdin, Senior Vice President and Senior Underwriting Counsel for Stewart Title Guaranty Company, is considering adopting conforming title insurance amendments to Procedural Rule P-47 and to the insuring forms of the Equity Loan Mortgage Endorsement (T-42) and the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1). The amendments would make technical corrections to references to applicable law, conform these documents to insure future advances under home equity lines of credit (HELOCs), and insure compliance with new requirements for a one-day advance disclosure of actual fees and charges by title insurance companies or title insurance agents who close home equity loans. The promised benefit to mortgagees is insurance protection against the risk of claimed lien invalidity arising out of the failure of the title company or title agent to timely and accurately provide a preclosing disclosure of actual fees and charges as required by new Section 50(a)(6)(M)(ii) in accordance with the lender's written closing instructions. As amended, the form of T-42.1 Endorsement would add a new subdivision (l) that insures the mortgagee of against:

> **(l) Failure of the Company or its Title Insurance Agent to provide the owner a copy of the final settlement statement prepared by the Company or its Title Insurance Agent itemizing the actual fees, points, interest, costs and charges collected or disbursed by the Company or its Title Insurance Agent at least one business day before the business day that the owner executed the insured mortgage and the promissory note secured thereby. As used in this paragraph (l), the term business day shall have the meaning assigned to such term by the Texas Finance Commission and/or the Texas Credit Union Commission pursuant to the authority granted such agencies by sections 11.308 and 15.413 of the Texas Finance Code, respectively.**

However, proposed paragraph 12 to Procedural Rule P-47 would require the title company or agent to delete subdivision (l) as an insured risk if in fact it fails for any reason to actually provide the preclosing disclosure:

> **12. Final Disclosure of Fees**
>
> **The Company must delete subparagraph (l) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the Company or its Title Insurance Agent does not provide each owner with a copy of the final settlement statement at least one business day before the business day that the owner executes the insured mortgage and the promissory note secured thereby. As used in this item 12, the term business day shall have the meaning assigned to such term by the Texas Finance Commission and/or the Texas Credit Union Commission pursuant to the authority granted such agencies by sections 11.308 and 15.413 of the Texas Finance Code, respectively.**

Lenders, therefore, should include in their written closing instructions the specific instruction that a home equity loan may not be closed by the company or agent unless it is prepared to issue the T-42.1 endorsement without striking subdivision (l). This practice should either provide lenders the insuring protections of the T-42.1, as amended by new subdivision (l) or alert the lender that a new

or modified one-day disclosure of actual fees and charges must be provided to the owner and the loan reset for closing on the next business day thereafter or another day thereafter.

Similar amendments are under consideration to Procedural Rule P-46 and insuring forms of the Junior Mortgagee Policy Variable Rate Endorsement (T-46), the Junior Mortgagee Down Date Endorsement (T-45), and the Texas Residential Limited Coverage Junior Mortgagee Policy (T-44) to conform the new amendments to the constitutional provisions for home equity loans, including home equity lines of credit. The Department expects to publish these proposed rules for public comment in the Texas Register on January 16, 2004, and under applicable administrative rules the amendments could be effective as early as February 5, 2004. Copies of proposed amendments to Procedural Rule P-47 and endorsement forms T-42 and T-42.1 with modifications indicated are attached as Exhibit C to this memorandum.

V. FANNIE MAE REVISES ITS FORMS OF TEXAS HOME EQUITY DOCUMENTS AND ISSUES ITS POLICY ANNOUNCEMENT 03-10

Fannie Mae made revisions on October 10, 2003, to six of its Texas Home Equity uniform instruments in connection with the new home equity amendments, including the forms of:

• Texas Home Equity Security Instrument	Form 3044.1
• Texas Home Equity Affidavit and Agreement	Form 3185
• Texas Home Equity Fixed-Rate Note	Form 3244.1
• Texas Home Equity Fixed/Adjustable Rate Notes:	Form 3263.44
	Form 3522.44
	Form 3523.44

Immediate use of the revised forms is encouraged and use is mandatory as of January 15, 2004. The forms may be obtained by print-out of the electronic version of the revised forms at www.efanniemae.com/singlefamily/forms.

Fannie Mae announced the revisions to its forms in its Announcement 03-10: Texas Section 50(a)(6) Mortgages, which also describes the changes it is making to its servicing policies, closing procedures, and mortgage documentation requirements as a result of the home equity constitutional amendments. Fannie Mae's policy announcement was issued prior to the effective date of the Joint Financial Agencies adoption of the Home Equity Lending Interpretations and conflicts with those interpretations with respect to the definition of "business day" and the determination of the first date on which an equity loan may be closed after the lender provides the preclosing disclosure required by new Section 50(a)(6)(M)(ii). Fannie Mae sources suggest that those policies were temporary pending the publication of the official interpretive rule and that all loans made in compliance with those interpretations will satisfy Fannie Mae seller-servicer requirements.

Exhibits Attached:

EXHIBIT A Senate Joint Resolution 42

EXHIBIT B Amended Form of 12-Day Notice

EXHIBIT C Proposed Amendments to Equity Loan Title Endorsements T-42 and T-42.1 and Procedural Rule P-47

EXHIBIT D Fannie Mae Announcement Ann. 03-10: Texas Section 50(a)(6) Mortgages

EXHIBIT A

S.J.R. No. 42

SENATE JOINT RESOLUTION

proposing a constitutional amendment authorizing a home equity line of credit, providing for administrative interpretation of home equity lending law, and otherwise relating to the making, refinancing, repayment, and enforcement of home equity loans.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. Subsection (a), Section 50, Article XVI, Texas Constitution, is amended to read as follows:

(a) The homestead of a family, or of a single adult person, shall be, and is hereby protected from forced sale, for the payment of all debts except for:

(1) the purchase money thereof, or a part of such purchase money;

(2) the taxes due thereon;

(3) an owelty of partition imposed against the entirety of the property by a court order or by a written agreement of the parties to the partition, including a debt of one spouse in favor of the other spouse resulting from a division or an award of a family homestead in a divorce proceeding;

(4) the refinance of a lien against a homestead, including a federal tax lien resulting from the tax debt of both spouses, if the homestead is a family homestead, or from the tax debt of the owner;

(5) work and material used in constructing new improvements thereon, if contracted for in writing, or work and material used to repair or renovate existing improvements thereon if:

(A) the work and material are contracted for in writing, with the consent of both spouses, in the case of a family homestead, given in the same manner as is required in making a sale and conveyance of the homestead;

(B) the contract for the work and material is not executed by the owner or the owner's spouse before the fifth day after the owner makes written application for any extension of credit for the work and material, unless the work and material are necessary to complete immediate repairs to conditions on the homestead property that materially affect the health or safety of the owner or person residing in the homestead and the owner of the homestead acknowledges such in writing;

(C) the contract for the work and material expressly provides that the owner may rescind the contract without penalty or charge within three days after the execution of the contract by all parties, unless the work and material are necessary to complete immediate repairs to conditions on the homestead property that materially affect the health or safety of the owner or person residing in the homestead and the owner of the homestead acknowledges such in writing; and

(D) the contract for the work and material is executed by the owner and the owner's spouse only at the office of a third-party lender making an extension of credit for the work and material, an attorney at law, or a title company;

(6) an extension of credit that:

(A) is secured by a voluntary lien on the homestead created under a written agreement with the consent of

each owner and each owner's spouse;

(B) is of a principal amount that when added to the aggregate total of the outstanding principal balances of all other indebtedness secured by valid encumbrances of record against the homestead does not exceed 80 percent of the fair market value of the homestead on the date the extension of credit is made;

(C) is without recourse for personal liability against each owner and the spouse of each owner, unless the owner or spouse obtained the extension of credit by actual fraud;

(D) is secured by a lien that may be foreclosed upon only by a court order;

(E) does not require the owner or the owner's spouse to pay, in addition to any interest, fees to any person that are necessary to originate, evaluate, maintain, record, insure, or service the extension of credit that exceed, in the aggregate, three percent of the original principal amount of the extension of credit;

(F) is not a form of open-end account that may be debited from time to time or under which credit may be extended from time to time unless the open-end account is a home equity line of credit;

(G) is payable in advance without penalty or other charge;

(H) is not secured by any additional real or personal property other than the homestead;

(I) is not secured by homestead property designated for agricultural use as provided by statutes governing property tax, unless such homestead property is used primarily for the production of milk;

(J) may not be accelerated because of a decrease in the market value of the homestead or because of the owner's default under other indebtedness not secured by a prior valid encumbrance against the homestead;

(K) is the only debt secured by the homestead at the time the extension of credit is made unless the other debt was made for a purpose described by Subsections (a)(1)-(a)(5) or Subsection (a)(8) of this section;

(L) is scheduled to be repaid:

(i) in substantially equal successive periodic [~~monthly~~] installments, not more often than every 14 days and not less often than monthly, beginning no later than two months from the date the extension of credit is made, each of which equals or exceeds the amount of accrued interest as of the date of the scheduled installment; or

(ii) if the extension of credit is a home equity line of credit, in periodic payments described under Subsection (t)(8) of this section;

(M) is closed not before:

(i) the 12th day after the later of the date that the owner of the homestead submits an application to the lender for the extension of credit or the date that the lender provides the owner a copy of the notice prescribed by Subsection (g) of this section; [~~and~~]

(ii) one business day after the date that the owner of the homestead receives a final itemized disclosure of the actual fees, points, interest, costs, and charges that will be charged at closing. If a bona fide emergency or another good cause exists and the lender obtains the written consent of the owner, the lender may provide the documentation to the owner or the lender may modify previously provided documentation on the date of closing; and

(iii) the first anniversary of the closing date of any other extension of credit described by Subsection (a)(6) of this section secured by the same homestead property, except a refinance described by Paragraph (Q)(x)(f) of this subdivision;

(N) is closed only at the office of the lender, an

attorney at law, or a title company;

(O) permits a lender to contract for and receive any fixed or variable rate of interest authorized under statute;

(P) is made by one of the following that has not been found by a federal regulatory agency to have engaged in the practice of refusing to make loans because the applicants for the loans reside or the property proposed to secure the loans is located in a certain area:

(i) a bank, savings and loan association, savings bank, or credit union doing business under the laws of this state or the United States;

(ii) a federally chartered lending instrumentality or a person approved as a mortgagee by the United States government to make federally insured loans;

(iii) a person licensed to make regulated loans, as provided by statute of this state;

(iv) a person who sold the homestead property to the current owner and who provided all or part of the financing for the purchase; [~~or~~]

(v) a person who is related to the homestead property owner within the second degree of affinity or consanguinity; or

(vi) a person regulated by this state as a mortgage broker; and

(Q) is made on the condition that:

(i) the owner of the homestead is not required to apply the proceeds of the extension of credit to repay another debt except debt secured by the homestead or debt to another lender;

(ii) the owner of the homestead not assign wages as security for the extension of credit;

(iii) the owner of the homestead not sign any instrument in which blanks are left to be filled in;

(iv) the owner of the homestead not sign a confession of judgment or power of attorney to the lender or to a third person to confess judgment or to appear for the owner in a judicial proceeding;

(v) the lender, at the time the extension of credit is made, provide the owner of the homestead a copy of all documents signed by the owner related to the extension of credit;

(vi) the security instruments securing the extension of credit contain a disclosure that the extension of credit is the type of credit defined by Section 50(a)(6), Article XVI, Texas Constitution;

(vii) within a reasonable time after termination and full payment of the extension of credit, the lender cancel and return the promissory note to the owner of the homestead and give the owner, in recordable form, a release of the lien securing the extension of credit or a copy of an endorsement and assignment of the lien to a lender that is refinancing the extension of credit;

(viii) the owner of the homestead and any spouse of the owner may, within three days after the extension of credit is made, rescind the extension of credit without penalty or charge;

(ix) the owner of the homestead and the lender sign a written acknowledgment as to the fair market value of the homestead property on the date the extension of credit is made; [~~and~~]

(x) except as provided by Subparagraph (xi) of this paragraph, the lender or any holder of the note for the extension of credit shall forfeit all principal and interest of the extension of credit if the lender or holder fails to comply with the lender's or holder's obligations under the extension of credit and fails to correct the failure to comply not later than the 60th day after the date [~~within a reasonable time after~~] the lender or holder is notified by the borrower of the lender's failure to comply by:

(a) paying to the owner an amount equal to any overcharge paid by the owner under or related to the extension of credit if the owner has paid an amount that exceeds an amount stated in the applicable Paragraph (E), (G), or (O) of this subdivision;

(b) sending the owner a written acknowledgement that the lien is valid only in the amount that the extension of credit does not exceed the percentage described by Paragraph (B) of this subdivision, if applicable, or is not secured by property described under Paragraph (H) or (I) of this subdivision, if applicable;

(c) sending the owner a written notice modifying any other amount, percentage, term, or other provision prohibited by this section to a permitted amount, percentage, term, or other provision and adjusting the account of the borrower to ensure that the borrower is not required to pay more than an amount permitted by this section and is not subject to any other term or provision prohibited by this section;

(d) delivering the required documents to the borrower if the lender fails to comply with Subparagraph (v) of this paragraph or obtaining the appropriate signatures if the lender fails to comply with Subparagraph (ix) of this paragraph;

(e) sending the owner a written acknowledgement, if the failure to comply is prohibited by Paragraph (K) of this subdivision, that the accrual of interest and all of the owner's obligations under the extension of credit are abated while any prior lien prohibited under Paragraph (K) remains secured by the homestead; or

(f) if the failure to comply cannot be cured under Subparagraphs (x)(a)-(e) of this paragraph, curing the failure to comply by a refund or credit to the owner of $1,000 and offering the owner the right to refinance the extension of credit with the lender or holder for the remaining term of the loan at no cost to the owner on the same terms, including interest, as the original extension of credit with any modifications necessary to comply with this section or on terms on which the owner and the lender or holder otherwise agree that comply with this section; and

(xi) the lender or any holder of the note for the extension of credit shall forfeit all principal and interest of the extension of credit if the extension of credit is made by a person other than a person described under Paragraph (P) of this subdivision or if the lien was not created under a written agreement with the consent of each owner and each owner's spouse, unless each owner and each owner's spouse who did not initially consent subsequently consents;

(7) a reverse mortgage; or

(8) the conversion and refinance of a personal property lien secured by a manufactured home to a lien on real property, including the refinance of the purchase price of the manufactured home, the cost of installing the manufactured home on the real property, and the refinance of the purchase price of the real property.

SECTION 2. Subsection (f), Section 50, Article XVI, Texas Constitution, is amended to read as follows:

(f) A refinance of debt secured by the homestead, any portion of which is an extension of credit described by Subsection (a)(6) of this section, may not be secured by a valid lien against the homestead unless the refinance of the debt is an extension of credit described by Subsection (a)(6) or (a)(7) of this section.

SECTION 3. Subsection (g), Section 50, Article XVI, Texas Constitution, is amended to read as follows:

(g) An extension of credit described by Subsection (a)(6) of this section may be secured by a valid lien against homestead property if the extension of credit is not closed before the 12th day after the lender provides the owner with the following written notice on a separate instrument:

"NOTICE CONCERNING EXTENSIONS OF CREDIT DEFINED BY SECTION 50(a)(6), ARTICLE XVI, TEXAS CONSTITUTION:

"SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION ALLOWS CERTAIN LOANS TO BE SECURED AGAINST THE EQUITY IN YOUR HOME. SUCH LOANS ARE COMMONLY KNOWN AS EQUITY LOANS. IF YOU DO NOT REPAY THE LOAN OR IF YOU FAIL TO MEET THE TERMS OF THE LOAN, THE LENDER MAY FORECLOSE AND SELL YOUR HOME. THE CONSTITUTION PROVIDES THAT:

"(A) THE LOAN MUST BE VOLUNTARILY CREATED WITH THE CONSENT OF EACH OWNER OF YOUR HOME AND EACH OWNER'S SPOUSE;

"(B) THE PRINCIPAL LOAN AMOUNT AT THE TIME THE LOAN IS MADE MUST NOT EXCEED AN AMOUNT THAT, WHEN ADDED TO THE PRINCIPAL BALANCES OF ALL OTHER LIENS AGAINST YOUR HOME, IS MORE THAN 80 PERCENT OF THE FAIR MARKET VALUE OF YOUR HOME;

"(C) THE LOAN MUST BE WITHOUT RECOURSE FOR PERSONAL LIABILITY AGAINST YOU AND YOUR SPOUSE UNLESS YOU OR YOUR SPOUSE OBTAINED THIS EXTENSION OF CREDIT BY ACTUAL FRAUD;

"(D) THE LIEN SECURING THE LOAN MAY BE FORECLOSED UPON ONLY WITH A COURT ORDER;

"(E) FEES AND CHARGES TO MAKE THE LOAN MAY NOT EXCEED 3 PERCENT OF THE LOAN AMOUNT;

"(F) THE LOAN MAY NOT BE AN OPEN-END ACCOUNT THAT MAY BE DEBITED FROM TIME TO TIME OR UNDER WHICH CREDIT MAY BE EXTENDED FROM TIME TO TIME UNLESS IT IS A HOME EQUITY LINE OF CREDIT;

"(G) YOU MAY PREPAY THE LOAN WITHOUT PENALTY OR CHARGE;

"(H) NO ADDITIONAL COLLATERAL MAY BE SECURITY FOR THE LOAN;

"(I) THE LOAN MAY NOT BE SECURED BY AGRICULTURAL HOMESTEAD PROPERTY, UNLESS THE AGRICULTURAL HOMESTEAD PROPERTY IS USED PRIMARILY FOR THE PRODUCTION OF MILK;

"(J) YOU ARE NOT REQUIRED TO REPAY THE LOAN EARLIER THAN AGREED SOLELY BECAUSE THE FAIR MARKET VALUE OF YOUR HOME DECREASES OR BECAUSE YOU DEFAULT ON ANOTHER LOAN THAT IS NOT SECURED BY YOUR HOME;

"(K) ONLY ONE LOAN DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MAY BE SECURED WITH YOUR HOME AT ANY GIVEN TIME;

"(L) THE LOAN MUST BE SCHEDULED TO BE REPAID IN PAYMENTS THAT EQUAL OR EXCEED THE AMOUNT OF ACCRUED INTEREST FOR EACH PAYMENT PERIOD;

"(M) THE LOAN MAY NOT CLOSE BEFORE 12 DAYS AFTER YOU SUBMIT A WRITTEN APPLICATION TO THE LENDER OR BEFORE 12 DAYS AFTER YOU RECEIVE THIS NOTICE, WHICHEVER DATE IS LATER; AND IF YOUR HOME WAS SECURITY FOR THE SAME TYPE OF LOAN WITHIN THE PAST YEAR, A NEW LOAN SECURED BY THE SAME PROPERTY MAY NOT CLOSE BEFORE ONE YEAR HAS PASSED FROM THE CLOSING DATE OF THE OTHER LOAN;

"(N) THE LOAN MAY CLOSE ONLY AT THE OFFICE OF THE LENDER, TITLE COMPANY, OR AN ATTORNEY AT LAW;

"(O) THE LENDER MAY CHARGE ANY FIXED OR VARIABLE RATE OF INTEREST AUTHORIZED BY STATUTE;

"(P) ONLY A LAWFULLY AUTHORIZED LENDER MAY MAKE LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION; [~~AND~~]

"(Q) LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MUST:

"(1) NOT REQUIRE YOU TO APPLY THE PROCEEDS TO ANOTHER DEBT EXCEPT A DEBT THAT IS [~~NOT~~] SECURED BY YOUR HOME OR OWED TO ANOTHER [~~DEBT TO THE SAME~~] LENDER;

"(2) NOT REQUIRE THAT YOU ASSIGN WAGES AS SECURITY;

"(3) NOT REQUIRE THAT YOU EXECUTE INSTRUMENTS WHICH HAVE BLANKS LEFT TO BE FILLED IN;

"(4) NOT REQUIRE THAT YOU SIGN A CONFESSION OF JUDGMENT OR POWER OF ATTORNEY TO ANOTHER PERSON TO CONFESS JUDGMENT OR APPEAR IN A LEGAL PROCEEDING ON YOUR BEHALF;

"(5) PROVIDE THAT YOU RECEIVE A COPY OF ALL DOCUMENTS YOU SIGN AT CLOSING;

"(6) PROVIDE THAT THE SECURITY INSTRUMENTS CONTAIN A DISCLOSURE THAT THIS LOAN IS A LOAN DEFINED BY SECTION 50(a)(6),

ARTICLE XVI, OF THE TEXAS CONSTITUTION;

"(7) PROVIDE THAT WHEN THE LOAN IS PAID IN FULL, THE LENDER WILL SIGN AND GIVE YOU A RELEASE OF LIEN OR AN ASSIGNMENT OF THE LIEN, WHICHEVER IS APPROPRIATE;

"(8) PROVIDE THAT YOU MAY, WITHIN 3 DAYS AFTER CLOSING, RESCIND THE LOAN WITHOUT PENALTY OR CHARGE;

"(9) PROVIDE THAT YOU AND THE LENDER ACKNOWLEDGE THE FAIR MARKET VALUE OF YOUR HOME ON THE DATE THE LOAN CLOSES; AND

"(10) PROVIDE THAT THE LENDER WILL FORFEIT ALL PRINCIPAL AND INTEREST IF THE LENDER FAILS TO COMPLY WITH THE LENDER'S OBLIGATIONS UNLESS THE LENDER CURES THE FAILURE TO COMPLY AS PROVIDED BY SECTION 50(a)(6)(Q)(x), ARTICLE XVI, OF THE TEXAS CONSTITUTION; AND

"(R) IF THE LOAN IS A HOME EQUITY LINE OF CREDIT:

"(1) YOU MAY REQUEST ADVANCES, REPAY MONEY, AND REBORROW MONEY UNDER THE LINE OF CREDIT;

"(2) EACH ADVANCE UNDER THE LINE OF CREDIT MUST BE IN AN AMOUNT OF AT LEAST $4,000;

"(3) YOU MAY NOT USE A CREDIT CARD, DEBIT CARD, SOLICITATION CHECK, OR SIMILAR DEVICE TO OBTAIN ADVANCES UNDER THE LINE OF CREDIT;

"(4) ANY FEES THE LENDER CHARGES MAY BE CHARGED AND COLLECTED ONLY AT THE TIME THE LINE OF CREDIT IS ESTABLISHED AND THE LENDER MAY NOT CHARGE A FEE IN CONNECTION WITH ANY ADVANCE;

"(5) THE MAXIMUM PRINCIPAL AMOUNT THAT MAY BE EXTENDED, WHEN ADDED TO ALL OTHER DEBTS SECURED BY YOUR HOME, MAY NOT EXCEED 80 PERCENT OF THE FAIR MARKET VALUE OF YOUR HOME ON THE DATE THE LINE OF CREDIT IS ESTABLISHED;

"(6) IF THE PRINCIPAL BALANCE UNDER THE LINE OF CREDIT AT ANY TIME EXCEEDS 50 PERCENT OF THE FAIR MARKET VALUE OF YOUR HOME, AS DETERMINED ON THE DATE THE LINE OF CREDIT IS ESTABLISHED, YOU MAY NOT CONTINUE TO REQUEST ADVANCES UNDER THE LINE OF CREDIT UNTIL THE BALANCE IS LESS THAN 50 PERCENT OF THE FAIR MARKET VALUE; AND

"(7) THE LENDER MAY NOT UNILATERALLY AMEND THE TERMS OF THE LINE OF CREDIT.

"THIS NOTICE IS ONLY A SUMMARY OF YOUR RIGHTS UNDER THE TEXAS CONSTITUTION. YOUR RIGHTS ARE GOVERNED BY SECTION 50, ARTICLE XVI, OF THE TEXAS CONSTITUTION, AND NOT BY THIS NOTICE."

If the discussions with the borrower are conducted primarily in a language other than English, the lender shall, before closing, provide an additional copy of the notice translated into the written language in which the discussions were conducted.

SECTION 4. Section 50, Article XVI, Texas Constitution, is amended by adding Subsections (t) and (u) to read as follows:

(t) A home equity line of credit 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:

(1) the owner requests advances, repays money, and reborrows money;

(2) any single debit or advance is not less than $4,000;

(3) the owner does not use a credit card, debit card, preprinted solicitation check, or similar device to obtain an advance;

(4) any fees described by Subsection (a)(6)(E) of this section 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;

(5) the maximum principal amount that may be extended under the account, when added to the aggregate total of the outstanding principal balances of all indebtedness secured by the homestead on the date the extension of credit is established, does not exceed an amount described under Subsection (a)(6)(B) of this section;

(6) no additional debits or advances are 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;

(7) the lender or holder may not unilaterally amend the extension of credit; and

(8) 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:

(A) during the period during which the owner may request advances, each installment equals or exceeds the amount of accrued interest; and

(B) after the period during which the owner may request advances, installments are substantially equal.

(u) The legislature may by statute delegate one or more state agencies the power to interpret Subsections (a)(5)-(a)(7), (e)-(p), and (t), of this section. An act or omission does not violate a provision included in those subsections if the act or omission conforms to an interpretation of the provision that is:

(1) in effect at the time of the act or omission; and

(2) made by a state agency to which the power of interpretation is delegated as provided by this subsection or by an appellate court of this state or the United States.

SECTION 5. This proposed constitutional amendment shall be submitted to the voters at an election to be held September 13, 2003. The ballot shall be printed to permit voting for or against the proposition: "The constitutional amendment authorizing a home equity line of credit, providing for administrative interpretation of home equity lending law, and otherwise relating to the making, refinancing, repayment, and enforcement of home equity loans."

_____ _____

President of the Senate Speaker of the House

I hereby certify that S.J.R. No. 42 was adopted by the Senate on May 14, 2003, by the following vote: Yeas 26, Nays 5; and that the Senate concurred in House amendments on May 29, 2003, by the following vote: Yeas 28, Nays 3.

_____

Secretary of the Senate

I hereby certify that S.J.R. No. 42 was adopted by the House, with amendments, on May 24, 2003, by the following vote: Yeas 115, Nays 0, one present not voting.

_____

Chief Clerk of the House

EXHIBIT B

NOTICE CONCERNING EXTENSIONS OF CREDIT DEFINED BY SECTION 50(a)(6), ARTICLE XVI, TEXAS CONSTITUTION

SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION ALLOWS CERTAIN LOANS TO BE SECURED AGAINST THE EQUITY IN YOUR HOME. SUCH LOANS ARE COMMONLY KNOWN AS EQUITY LOANS. IF YOU DO NOT REPAY THE LOAN OR IF YOU FAIL TO MEET THE TERMS OF THE LOAN, THE LENDER MAY FORECLOSE AND SELL YOUR HOME. THE CONSTITUTION PROVIDES THAT:

(A) THE LOAN MUST BE VOLUNTARILY CREATED WITH THE CONSENT OF EACH OWNER OF YOUR HOME AND EACH OWNER'S SPOUSE;

(B) THE PRINCIPAL LOAN AMOUNT AT THE TIME THE LOAN IS MADE MUST NOT EXCEED AN AMOUNT THAT, WHEN ADDED TO THE PRINCIPAL BALANCES OF ALL OTHER LIENS AGAINST YOUR HOME, IS MORE THAN 80% OF THE FAIR MARKET VALUE OF YOUR HOME;

(C) THE LOAN MUST BE WITHOUT RECOURSE FOR PERSONAL LIABILITY AGAINST YOU AND YOUR SPOUSE UNLESS YOU OR YOUR SPOUSE OBTAINED THIS EXTENSION OF CREDIT BY ACTUAL FRAUD;

(D) THE LIEN SECURING THE LOAN MAY BE FORECLOSED UPON ONLY WITH A COURT ORDER;

(E) FEES AND CHARGES TO MAKE THE LOAN MAY NOT EXCEED 3% OF THE LOAN AMOUNT;

(F) THE LOAN MAY NOT BE AN OPEN-END ACCOUNT THAT MAY BE DEBITED FROM TIME TO TIME OR UNDER WHICH CREDIT MAY BE EXTENDED FROM TIME TO TIME **UNLESS IT IS A HOME EQUITY LINE OF CREDIT**;

(G) YOU MAY PREPAY THE LOAN WITHOUT PENALTY OR CHARGE;

(H) NO ADDITIONAL COLLATERAL MAY BE SECURITY FOR THE LOAN;

(I) THE LOAN MAY NOT BE SECURED BY AGRICULTURAL HOMESTEAD PROPERTY, UNLESS THE AGRICULTURAL HOMESTEAD PROPERTY IS USED PRIMARILY FOR THE PRODUCTION OF MILK;

(J) YOU ARE NOT REQUIRED TO REPAY THE LOAN EARLIER THAN AGREED SOLELY BECAUSE THE FAIR MARKET VALUE OF YOUR HOME DECREASES OR BECAUSE YOU DEFAULT ON ANOTHER LOAN THAT IS NOT SECURED BY YOUR HOME;

(K) ONLY ONE LOAN DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MAY BE SECURED WITH YOUR HOME AT ANY GIVEN TIME;

(L) THE LOAN MUST BE SCHEDULED TO BE REPAID IN PAYMENTS THAT EQUAL OR EXCEED THE AMOUNT OF ACCRUED INTEREST FOR EACH PAYMENT PERIOD;

(M) THE LOAN MAY NOT CLOSE BEFORE 12 DAYS AFTER YOU SUBMIT A WRITTEN APPLICATION TO THE LENDER OR BEFORE 12 DAYS AFTER YOU RECEIVE THIS NOTICE, WHICHEVER DATE IS LATER; **AND MAY NOT CLOSE BEFORE ONE BUSINESS DAY AFTER THE DATE ON WHICH YOU RECEIVE A FINAL ITEMIZED DISCLOSURE OF THE ACTUAL FEES, POINTS, INTEREST, COSTS, AND CHARGES THAT WILL BE CHARGED AT CLOSING[1];** AND MAY NOT CLOSE AND IF YOUR HOME WAS SECURITY

[1] This underlined portion of (M) was apparently inadvertently omitted from the amendments to the promulgated form on notice set forth Subsection 50(g). Authority to incorporate this constitutional language appears to be granted in 7 TAC §153.51(2) permitting lenders to supplement the form of disclosure "to clarify any discrepancies or inconsistencies."

FOR THE SAME TYPE OF LOAN WITHIN THE PAST YEAR, A NEW LOAN SECURED BY THE SAME PROPERTY MAY NOT CLOSE BEFORE ONE YEAR HAS PASSED FROM THE CLOSING DATE OF THE OTHER LOAN;

(N) THE LOAN MAY CLOSE ONLY AT THE OFFICE OF THE LENDER, TITLE COMPANY, OR AN ATTORNEY AT LAW;

(O) THE LENDER MAY CHARGE ANY FIXED OR VARIABLE RATE OF INTEREST AUTHORIZED BY STATUTE;

(P) ONLY A LAWFULLY AUTHORIZED LENDER MAY MAKE LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION; AND

(Q) LOANS DESCRIBED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION MUST:

(1) NOT REQUIRE YOU TO APPLY THE PROCEEDS TO ANOTHER DEBT **EXCEPT A DEBT** THAT IS ~~**NOT**~~ SECURED BY YOUR HOME OR **OWED** TO ANOTHER ~~**DEBT TO THE SAME**~~ LENDER;

(2) NOT REQUIRE THAT YOU ASSIGN WAGES AS SECURITY;

(3) NOT REQUIRE THAT YOU EXECUTE INSTRUMENTS WHICH HAVE BLANKS LEFT TO BE FILLED IN;

(4) NOT REQUIRE THAT YOU SIGN A CONFESSION OF JUDGMENT OR POWER OF ATTORNEY TO ANOTHER PERSON TO CONFESS JUDGMENT OR APPEAR IN A LEGAL PROCEEDING ON YOUR BEHALF;

(5) PROVIDE THAT YOU RECEIVE A COPY OF ALL DOCUMENTS YOU SIGN AT CLOSING;

(6) PROVIDE THAT THE SECURITY INSTRUMENTS CONTAIN A DISCLOSURE THAT THIS LOAN IS A LOAN DEFINED BY SECTION 50(a)(6), ARTICLE XVI, OF THE TEXAS CONSTITUTION;

(7) PROVIDE THAT WHEN THE LOAN IS PAID IN FULL, THE LENDER WILL SIGN AND GIVE YOU A RELEASE OF LIEN OR AN ASSIGNMENT OF THE LIEN, WHICHEVER IS APPROPRIATE;

(8) PROVIDE THAT YOU MAY, WITHIN 3 DAYS AFTER CLOSING, RESCIND THE LOAN WITHOUT PENALTY OR CHARGE;

(9) PROVIDE THAT YOU AND THE LENDER ACKNOWLEDGE THE FAIR MARKET VALUE OF YOUR HOME ON THE DATE THE LOAN CLOSES; AND

(10) PROVIDE THAT THE LENDER WILL FORFEIT ALL PRINCIPAL AND INTEREST IF THE LENDER FAILS TO COMPLY WITH THE LENDER'S OBLIGATIONS UNLESS THE LENDER CURES THE FAILURE TO COMPLY AS PROVIDED BY SECTION 50 (a)(6)(Q)(x), ARTICLE XVI, OF THE TEXAS CONSTITUTION; AND

® IF THE LOAN IS A HOME EQUITY LINE OF CREDIT;

(1) YOU MAY REQUEST ADVANCES, REPAY MONEY, AND REBORROW MONEY UNDER THE LINE OF CREDIT;

(2) EACH ADVANCE UNDER THE LINE OF CREDIT MUST BE IN AN AMOUNT OF AT LEAST $4,000;

(3) YOU MAY NOT USE A CREDIT CARD, DEBIT CARD, SOLICITATION CHECK, OR SIMILAR DEVICE TO OBTAIN ADVANCES UNDER THE LINE OF CREDIT;

(4) ANY FEES THE LENDER CHARGES MAY BE CHARGED AND COLLECTED ONLY AT THE TIME THE LINE OF CREDIT IS ESTABLISHED AND THE LENDER MAY NOT CHARGE A FEE IN CONNECTION WITH ANY ADVANCE;

(5) THE MAXIMUM PRINCIPAL AMOUNT THAT MAY BE EXTENDED, WHEN ADDED TO ALL OTHER DEBTS SECURED BY YOUR HOME, MAY NOT EXCEED 80 PERCENT OF THE FAIR MARKET VALUE OF YOUR HOME ON THE DATE THE LINE OF CREDIT IS ESTABLISHED;

(6) IF THE PRINCIPAL BALANCE UNDER THE LINE OF CREDIT AT ANY TIME EXCEEDS 50 PERCENT OF THE FAIR MARKET VALUE OF YOUR HOME, AS DETERMINED ON THE DATE THE LINE OF CREDIT IS ESTABLISHED, YOU MAY

NOT CONTINUE TO REQUEST ADVANCES UNDER THE LINE OF CREDIT UNTIL THE BALANCE IS LESS THAN 50 PERCENT OF THE FAIR MARKET VALUE; AND

(7) THE LENDER MAY NOT UNILATERALLY AMEND THE TERMS OF THE LINE OF CREDIT.

THIS NOTICE IS ONLY A SUMMARY OF YOUR RIGHTS UNDER THE TEXAS CONSTITUTION. YOUR RIGHTS ARE GOVERNED BY SECTION 50, ARTICLE XVI, OF THE TEXAS CONSTITUTION, AND NOT BY THIS NOTICE.

THE UNDERSIGNED ACKNOWLEDGE RECEIPT OF THE FOREGOING NOTICE ON _____ ____, 200_.

_____ Owner/Borrower	_____ Owner/Borrower
_____ Owner/Borrower	_____ Owner/Borrower
_____ Owner/Borrower	_____ Owner/Borrower

EXHIBIT C

Proposed Amendments to Equity Loan Mortgage Endorsement T-42 to read as follows:

EQUITY LOAN MORTGAGE ENDORSEMENT T-42

Attached to and made a part of _____ Title Insurance Company

Mortgagee Policy No. _____,

dated the _____ day of _____, 20____.

Issued by

_____ TITLE INSURANCE COMPANY

The policy is hereby amended as follows:

1. The following new Subsection (h) is inserted in Section 1 of the Conditions and Stipulations:

(h) "consumer credit protection law": any applicable federal or state regulation, law or constitutional provision relating to consumer credit protection. For purposes of the policy and paragraph 5 of the Exclusions from Coverage, consumer credit protection law includes, but is not limited to, the provisions of Subsections (a)(6), [~~and~~] (g), and (t) of Section 50, Article XVI, Texas Constitution and any statutory or regulatory requirements for a mortgage made pursuant to Subsection (a)(6)."

2. Notwithstanding the specific provisions of paragraph 5 of the Exclusions from Coverage relating to consumer credit protection laws, the Company insures the insured against loss, if any, sustained by the insured under the terms of the policy because of invalidity or unenforceability of the lien of the insured mortgage by reason of the following:

(a) The failure of the insured mortgage to be created under a written agreement with the consent of each owner of the estate or interest described in Schedule A and each owner's spouse, as set forth in Subsection (a)(6)(A) of Section 50, Article XVI, Texas Constitution.

(b) The land being homestead property designated for agricultural use as provided by statutes governing property tax, as set forth in Subsection (a)(6)(I) of Section 50, Article XVI, Texas Constitution.

(c) The indebtedness secured by the lien of the insured mortgage on the land not being the only debt secured by a valid lien on the land at the time the extension of credit is made pursuant to the insured mortgage unless the other debt was made for a purpose [~~the purpose~~] described by Subsections (a)(1) through (a)(5) or Subsection (a)(8) of Section 50 of Article XVI,

Texas Constitution, as set forth in Subsection (a)(6)(K) of Section 50, Article XVI, Texas Constitution.

(d) The extension of credit secured by the lien of the insured mortgage closing before the first anniversary of the closing date of any other extension of credit described by Subsection (a)(6) of Section 50 of Article XVI, Texas Constitution and secured by a valid lien on the land, as set forth in Subsection (a)(6)(M)(iii) [~~(ii)~~] of Section 50, Article XVI, Texas Constitution.

(e) The failure of the insured mortgage to contain a disclosure that the extension of credit is the type of credit defined by Section 50(a)(6), Article XVI, Texas Constitution, as set forth in Subsection (a)(6)(Q)(vi) of Section 50 (a)(6), Article XVI, Texas Constitution.

3. Provided the insured mortgage secures a home equity line of credit, the Company insures the Insured that any disbursements under the home equity line of credit made subsequent to the date of this policy as provided in the insured mortgage shall be deemed to have been made as of the date of this policy and such disbursements and accrued interest shall have the same priority as any advances made as of the date of this policy, except as to (i) bankruptcies affecting the estate or interest described on Schedule "A" hereof prior to the date of any such advance or disbursement; and (ii) taxes, costs, charges, damages and other obligations to the government secured by statutory liens arising or recorded subsequent to the date of the Policy.

4. [~~3.~~] Except as provided in paragraph 2 above, the Company does not insure against invalidity or unenforceability of the lien of the insured mortgage, which arises out of the transaction evidenced by the insured mortgage and is based on any consumer credit protection law.

5. [~~4.~~] This endorsement does not insure against invalidity or unenforceability of the lien of the insured mortgage, or claim thereof, arising out of usury or truth in lending laws.

This endorsement when countersigned below by an Authorized Countersignature is made a part of said Policy. Except as expressly modified by the provisions hereof, this endorsement is subject to the following policy matters: (i) Insuring provisions; (ii) Exclusions from Coverage; (iii) Schedule "B" Exceptions; (iv) the Conditions and Stipulations; and (v) any prior endorsements. Except as stated herein, this endorsement does not: (i) extend the effective date of the policy and/or any prior endorsements; or (ii) increase the face amount of the policy.

Form T-42 Equity Loan Mortgage Endorsement T-42

PROPOSED

Proposed amendments to Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) to read as follows:

SUPPLEMENTAL COVERAGE EQUITY LOAN MORTGAGE ENDORSEMENT (T-42.1)

Attached to and made a part of _____ Title Insurance Company

Mortgagee Policy No. _____ (herein the "Policy"),

dated the _____ day of _____, 20____.

Issued By

_____ TITLE INSURANCE COMPANY

THIS ENDORSEMENT IS VOID AND OF NO EFFECT UNLESS IT IS ATTACHED TO A MORTGAGEE POLICY OF TITLE INSURANCE (FORM T-2), WHICH CONTAINS AN EQUITY LOAN MORTGAGE ENDORSEMENT (FORM T-42) ATTACHED TO THE MORTGAGEE POLICY.

In this endorsement, the term "owner" shall refer to each owner of the land described in Schedule "A" of this Mortgagee Policy.

Date of Endorsement: _____

1. Notwithstanding the specific provisions of paragraph 5 of the Exclusions from Coverage relating to consumer credit protection laws and the provisions of the Equity Loan Mortgage Endorsement (T-42), the Company insures the insured against loss, if any, sustained by the insured under the terms of the policy because of invalidity or unenforceability of the lien of the insured mortgage pursuant to Section 50(a)(6), Article XVI, Texas Constitution, arising solely by reason of one or more of the following:

(a) The insured mortgage and promissory note secured thereby being executed at an office of the Company or its Title Insurance Agent before the specific calendar date stated in written closing instructions from the insured name in Schedule A delivered to the Company or its Title Insurance Agent prior to the execution of the insured mortgage and promissory note.

(b) Any loan proceeds received by the Company or its Title Insurance Agent in connection with the extension of credit secured by the lien of the insured mortgage being disbursed by the Company or its Title Insurance Agent sooner than the fourth calendar day after the insured mortgage and promissory note secured thereby are executed.

(c) A document expressly purporting to evidence an election not to rescind the extension of credit secured by the lien of the insured mortgage being executed by the owner and spouse, if any, of the owner, in the presence of an escrow officer of the Company or its Title Insurance Agent on or before the date that the insured mortgage and promissory note secured thereby were executed.

(d) Failure of the Company or its Title Insurance Agent to provide the owner with a copy of all documents related to the extension of credit secured by the lien of the insured mortgage that were executed by the owner at the office of the Company or its Title Insurance Agent on the date that the owner executed the insured mortgage and the promissory note secured thereby.

(e) The Company or its Title Insurance Agent collecting or disbursing any fees not shown on the final settlement statement prepared by the Company or its Title Insurance Agent and sent to the lender named on the settlement statement prior to the execution of the insured mortgage and the promissory note secured thereby.

(f) Blanks (other than signature lines, if any, for execution by the lender) in the following instruments left to be filled in when executed by the owner in an office of the Company or its Title Insurance Agent: (i) an instrument prepared by the Company or its Title Insurance Agent, (ii) the purported written acknowledgment as to the fair market value, (iii) the insured mortgage, (iv) the promissory note secured thereby, or (v) affidavits of compliance with Section 50(a)(6), Article XVI, Texas Constitution.

(g) The failure of the written document purporting to be a written acknowledgment as to the fair market value of the land to have attached, at the time of execution of such written document by the owner, a purported appraisal or a purported evaluation of the fair market value of the land. However, the Company does not insure that the purported written acknowledgment or the purported appraisal or purported evaluation complies with Subsection (a)(Q)(ix) or Subsection (h) of Section 50, Article XVI, Texas Constitution or any laws or regulations relating to the subject matter of said subsections.

(h) The failure of the written document purporting to be an acknowledgment as to the fair market value to be executed by the owner on the date that the insured mortgage and promissory note secured thereby are executed by the owner.

(i) Part of the land described in Schedule A not being the homestead of the owner.

(j) Title to other land which, according to the public records, appears to be vested in the name of the owner as shown on Schedule A and which is not described in Schedule A and which is located in the same county in which the land described in Schedule A is located, being subject at Date of Policy to a mortgage executed by the owner, recorded in the public records, which discloses that it secures an extension of credit made pursuant to Subsection (a)(6) of Section 50, Article XVI, Texas Constitution.

(k) Title to other land which, according to the public records, appears to be vested in the name of the owner as shown on Schedule A and which is not described in Schedule A and which is located in the same county in which the

land described in Schedule A is located, having been subject to a mortgage executed by the owner, recorded in the public records, which disclosed that it secured an extension of credit made pursuant to Subsection (a)(6) of Section 50, Article XVI, Texas Constitution, that was closed within one year prior to Date of Policy.

(l) Failure of the Company or its Title Insurance Agent to provide the owner a copy of the final settlement statement prepared by the Company or its Title Insurance Agent itemizing the actual fees, points, interest, costs and charges collected or disbursed by the Company or its Title Insurance Agent at least one business day before the business day that the owner executed the insured mortgage and the promissory note secured thereby. As used in this paragraph (l), the term business day shall have the meaning assigned to such term by the Texas Finance Commission and/or the Texas Credit Union Commission pursuant to the authority granted such agencies by sections 11.308 and 15.413 of the Texas Finance Code, respectively.

2. This Endorsement does not insure against invalidity or unenforceability of the lien of the insured mortgage, or claim thereof, arising out of usury or truth in lending laws.

3. Except as provided in paragraph 1 above and except as provided in the Equity Loan Mortgage Endorsement (T-42), the Company does not insure against invalidity or unenforceability of the lien on the insured mortgage, which arises out of the transaction evidenced by the insured mortgage and is based on any consumer credit protection law.

4. This Endorsement does not represent or insure that a Title Insurance Agent of the Company is the agent of the Company other than for issuance of title insurance policies, as provided by applicable law.

This Endorsement when countersigned below by an Authorized Countersignature is made a part of said Policy. Except as expressly modified by the provisions hereof, this endorsement is subject to the following policy matters: (i) Insuring provisions; (ii) Exclusions from Coverage; (iii) Schedule "B" Exceptions; (iv) the Conditions and Stipulations; (v) the Equity Loan Mortgage Endorsement (T-42) and all of the terms thereof, except as it may be modified by deletion of any subparagraph of paragraph 2 thereof; and (vi) any other prior endorsements. Except as stated herein, this Endorsement does not: (i) extend the effective date of the policy and/or any prior endorsements; or (ii) increase the face amount of the policy.

Authorized Countersignature:

_____

By:_____
(Signature)

Title:_____

Printed Name:_____

PROPOSED Form T-42.1 Supplemental Coverage Equity Loan Mortgage Endorsement

Proposed amendments to Procedural Rule P-47 to read as follows:

P-47 Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1)
A. GENERAL REQUIREMENTS

When a Mortgagee Policy of Title Insurance (T-2) is to be issued insuring the lien securing an extension of credit made pursuant to Subsection (a)(6) of Section 50, Article XVI, Texas Constitution, the Company may attach the Mortgagee Policy of Title Insurance (T-2) and the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the Company considers the risk insurable and the Company complies with this Procedural Rule P-47. The general requirements and limitations for issuance of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) are as follows:

1. The Company shall not attach the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) to the Mortgagee Policy of Title Insurance (T-2) unless:

a. The Equity Loan Mortgage Endorsement (T-42) is attached to said Mortgagee Policy of Title Insurance[~~;~~] and[~~;~~]

b. The Company has complied with the provisions of Procedural Rule P-44 concerning the attachment of the Equity Loan Mortgage Endorsement (T-42) to the Mortgagee Policy of Title Insurance (T-2).

2. The Company may delete any provision of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if it does not consider the additional risk insurable. The following language may be placed along side each lettered sub-paragraph reference contained in paragraph 1 [~~(one)~~] of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) which the Company determines to delete:

"Item_____of paragraph 1 [~~(one)~~] of this Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) is hereby deleted."

The Company shall complete the blank with the appropriate sub-paragraph letter of paragraph 1 [~~(one)~~] of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the above format is utilized.

3. The Company shall not provide Express Insurance (pursuant to P-39) as to matters set forth in the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1), whether or not the Company issues T-42.1.

4. The Company must delete subparagraphs (a) through (h) **and subparagraph (l)** of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if:

a. the insured mortgage and the promissory note secured thereby are not executed at

the office of a title company in accordance with Procedural Rule P-44(c)(1); or,

b. the Company deletes subparagraph 2(f) of the Equity Loan Mortgage Endorsement (T-42).

In order to evidence the deletion required by this subsection of P-47.A.(4), the following language may be stated on the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) in place of sub-paragraphs (a) through (h) **and sub-paragraph (l)** of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1). The following language may be used:

"Sub-paragraphs (a) through (h) **and sub-paragraph (l)** of paragraph 1 [~~(one)~~] of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) are hereby deleted in their entirety."

B.SPECIFIC ENDORSEMENT PARAGRAPH REQUIREMENTS

The requirements and limitations applicable for each numbered insuring provision of Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) are set forth in items 1 [~~(one)~~] through **12** [~~11 (eleven)~~] below:

1. Signature Before Specified Date

The Company must delete subparagraph (a) of paragraph 1 of Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if:

(a) written instructions are not furnished by the insured to the Company or its Title Insurance Agent prior to the execution of the insured mortgage and the promissory note secured thereby;

(b) the written instructions do not state a specific calendar date that constitutes the earliest date for execution of the insured mortgage and the promissory note secured thereby.

2. Loan Proceeds Disbursement Before Fourth Day

The Company must delete subparagraph (b) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if:

a. the Company or its Title Insurance Agent does not disburse all loan proceeds received by the Company or its Title Insurance Agent; or

b. any of the loan proceeds received by the Company or its Title Insurance Agent are disbursed sooner than four calendar days after the insured mortgage and promissory note are executed.

3. Execution of Election Not to Rescind

The Company must delete subparagraph (c) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if a document purporting to evidence an election not to rescind the extension of credit secured by the lien of the insured mortgage is executed in the presence of an escrow officer at an office of the Company or its Title Insurance Agent on or before the date that the insured mortgage and the promissory note secured thereby are executed.

4. Document Copies

The Company must delete subparagraph (d) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the Company or its Title Insurance Agent do not provide each owner of the land with a copy of all documents related to the extension of credit secured by the lien of the insured mortgage that were executed by the owner at an office of the Company or its Title Insurance Agency on the date that the owner executed the insured mortgage and the promissory note secured thereby.

5. Fees

The Company must delete subparagraph (e) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if:

a. any fees are collected or disbursed by the Company or its Title Insurance Agent and said fees are not shown on the final settlement statement which was prepared by the Company or its Title Insurance Agent and executed by the owner and the spouse, if any, of the owner; or

b. no preliminary (unexecuted) settlement statement is requested from the Company or its Title Insurance Agent, by the lender named on the final settlement statement, prior to execution of the insured mortgage and promissory note by the owner or the spouse, if any, of the owner; or

c. a preliminary (unexecuted) settlement statement was requested by and sent to the lender, and the fees on the final settlement statement executed by the owner, or the spouse, if any, of the owner exceed the amount of fees on the final (unexecuted) settlement statement sent to the lender prior to execution of the insured mortgage and promissory note secured thereby.

6. Blanks in an Instrument

The Company must delete subparagraph (f) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if either (a) or (b) below occurs:

a. There are any blanks in an instrument left to be filled in when executed by the owner of the land in an office of the Company or its Title Insurance agent, and:

i. the instrument was prepared by the Company or its Title Insurance Agent, or

ii. the instrument is: (a) the purported written acknowledgment as to the fair market value; (b) the insured mortgage; (c) the promissory note secured thereby; or, (d) affidavits of compliance with Section 50(a)(6), Article XVI, Texas Constitution.

b. There are any blanks in an instrument left to be filled in when executed by the owner of the land in any of the following instruments when same are delivered to the Company or its Title Insurance Agent: (i) the purported written acknowledgment as to the fair market value; (ii) the insured mortgage; (iii) the promissory note secured thereby; or, (iv) affidavits of compliance with Section 50(a)(6), Article XVI, Texas Constitution.

7. Attachment of Appraisal or Evaluation

The Company must delete subparagraph (g) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the insured does not furnish to the Company or its Title Insurance Agent prior to execution of the insured mortgage and the promissory note secured thereby:

a. a document purporting to be written acknowledgment as to the fair market value of the land; and

b. a purported appraisal or evaluation which is attached to the purported written acknowledgment.

8. Signature of Acknowledgment of Fair Market Value

The Company must delete subparagraph (h) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if:

a. the purported written acknowledgment as to the fair market value is not provided by the insured to the Company or its Title Insurance Agent prior to the execution of the insured mortgage or the promissory note secured thereby; or

b. the purported written acknowledgment is not executed by the owner at an office of the Company or its Title Insurance Agent on the date that the insured mortgage and the promissory note secured thereby are executed.

9. No Land In Excess of Homestead Allotment

The Company must delete subparagraph (i) of paragraph 1 [~~(one)~~] of the Supplemental Coverage Equity Loan Mortgage [~~Mortgagee~~] Endorsement (T-42.1) if: (a) or (b) below is true:

(a) The Company does not receive a satisfactory affidavit from each owner of the land, and that owner's spouse, stating that:

(i) all of the land is the homestead of the owner and that owner's spouse; and,

(ii) no portion of the land is non-homestead property of the owner or owner's spouse; and

(iii) the owner of the land, and that owner's spouse do not claim other land as homestead, unless that other land is described in the affidavit.

(b) The Company does not receive one of the following:

(i) a satisfactory surveyor's certificate or letter from a Texas Licensed Registered Professional Surveyor, stating the exact amount of acreage or square footage of the land and such other facts as may be required by the Company, including whether or not the land is located within the boundaries of an incorporated municipality; or,

(ii) a computation of the acreage or square footage of the land made pursuant to a software program designed for calculation of the acreage or square footage of the land and computer generated drawings of the boundaries of the land pursuant to entry of the boundary description calls.

10. No Other Land With a Home Equity Mortgage

The Company must delete subparagraph (j) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage [~~Mortgagee~~] Endorsement (T-42.1) if the Company does not receive a satisfactory affidavit from each owner of the land and that owner's spouse, if any, stating:

(a) the owner and the owner's spouse, if any, do not have or claim any other land as homestead for tax or other purposes except: (i) the land described in Schedule A of the Commitment for Title Insurance; and (ii) other land described in the affidavit; and,

(b) any business operated by the owner or the spouse of the owner, if any, and situated upon land owned or leased by the owner or owner's spouse is not subject to an extension of credit pursuant to Subsection (a)(6) or Section 50, Article XVI, Texas Constitution; and,

(c) the residence, owned or leased by the owner or owner's spouse, if any, at which the owner and the owner's spouse live is not subject to an extension of credit pursuant to Subsection (a)(6) of Section 50, Article XVI, Texas Constitution.

The Company may add the phrase "or in an adjoining county" after the phrase "described in Schedule A is located" in subparagraph (j) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if (i) the land is located within the boundaries of an incorporated municipality; (ii) the municipality is located in more than one county; and, (iii) the Company considers the risk insurable.

11. No Other Land With Released Home Equity Mortgage Within Past Twelve Months

The Company must delete subparagraph (k) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage [~~Mortgagee~~] Endorsement (T-42.1) if the Company does not receive a satisfactory affidavit from each owner of the land and that owner's spouse , if any, stating:

(a) the owner and the owner's spouse, if any, do not have or claim any other land as homestead for tax or other purposes except: (i) the land described in Schedule A of the Commitment for Title Insurance; and (ii) other land described in the affidavit; and,

(b) any business operated by the owner or the spouse of the owner, if any, and situated upon land owned or leased by the owner or owner's spouse has not been subject to an extension of credit pursuant to Subsection (a)(6) or Section 50, Article XVI, Texas Constitution, closed within one year prior to Date of Policy; and,

(c) the residence, owned or leased by the owner or owner's spouse, if any, at which the owner and the owner's spouse live has not been subject to an extension of credit pursuant to Subsection (a)(6) of Section 50, Article XVI, Texas Constitution, closed within one year prior to Date of Policy.

The Company may add the phrase "or in an adjoining county" after the phrase "described in Schedule A is located" in subparagraph (k) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if (i) the land is located within the boundaries of an incorporated municipality; (ii) the municipality is located in more than one county; and, (iii) the Company considers the risk insurable.

12. Final Disclosure of Fees

The Company must delete subparagraph (l) of paragraph 1 of the Supplemental Coverage Equity Loan Mortgage Endorsement (T-42.1) if the Company or its Title Insurance Agent does not provide each owner with a copy of the final settlement statement at least one business day before the business day that the owner executes the insured mortgage and the promissory note secured thereby. As used in this item 12, the term business day shall have the meaning assigned to such term by the Texas Finance Commission and/or the Texas Credit Union Commission pursuant to the authority granted such agencies by sections 11.308 and 15.413 of the Texas Finance Code, respectively.

PROPOSED

EXHIBIT D

Ann. 03-10: Texas Section 50(a)(6) Mortgages (10/15/03)

Amends these Guides: Selling and Servicing

On September 13, 2003, Texas voters approved an amendment to the Texas Constitution that changed the rules governing Section 50(a)(6) first mortgages that are secured by Texas homestead properties. The Amendment, which became effective on September 29, 2003, provides detailed provisions for curing origination defects, requires a new notice to be given at least one business day before the closing of the loan setting forth the final closing costs, and permits the refinance of a Section 50(a)(6) mortgage into a reverse mortgage, among other things. We view the changes favorably in terms of providing both lenders and borrowers more certainty regarding the meaning of the law and providing a clear means of resolving origination problems, and we expect the changes will, as a result, provide enhanced opportunities in this market.

This Announcement describes the changes we are making to our servicing policies, closing procedures, and mortgage documentation requirements as a result of the Amendment and amends both the Selling Guide (Part I, Section 202.01; Part IV, Section 102.04; Part IV, Chapter 1, Ex.1; Part IV, Chapter 2, Ex.1; Part IV, Chapter 2, Ex. 2; Part IV, Section 503; Part IV, Chapter 5, Ex. 1; Part V, Section 202.09; and Part VII, Sections 112, 112.01 and 112.05) and the Servicing Guide. Except for the changes discussed in this Announcement, all requirements in the Guides relating to Section 50(a)(6) first mortgages, including the requirement that a lender obtain special approval to sell and service such mortgages, remain in effect. Although the discussion below includes a general overview of certain provisions of the Amendment, it is the lenders' responsibility to ensure compliance with applicable law, and lenders should consult their own counsel with respect to the provisions of the Amendment.

New Cure Provisions

Prior to the adoption of the Amendment, the Texas Constitution provided that all principal and interest for a Section 50(a)(6) mortgage would be forfeited if the lender failed to comply with its obligations under the mortgage within a reasonable time after receiving notification of the failure to comply. The term "reasonable time" was not defined.

Under the Amendment, lenders are given sixty days after receiving notification of a failure to comply to correct the failure. In addition, the Amendment explains how various failures to comply can be corrected. Generally:

- If a lender has charged more than the permitted amount of fees, has charged excessive interest, or has charged a penalty or other charge as a condition to paying the mortgage in

advance, the lender may correct its failure to comply by paying the owner of the property an amount equal to the overcharge paid by the owner.

- If a lender has originated a mortgage in an amount that exceeds the maximum permitted amount, the lender may correct its failure to comply by sending the owner a written acknowledgment that the lien is valid only up to the maximum permitted amount.
- If a lender has originated a mortgage secured by real or personal property other than the homestead or has made a loan secured by an ineligible homestead property designated for agricultural use, the lender may correct its failure to comply by sending the owner a written acknowledgment that the mortgage is not secured by the ineligible collateral.
- A lender may send an owner a written notice modifying any other amount, percentage, term, or other provision of a mortgage and adjust the borrower's account to ensure compliance with Section 50(a)(6). (Sometimes the Amendment uses the term "owner," and sometimes the Amendment uses the term "borrower." Our Announcement tracks the language of the Amendment.)
- If a lender failed to timely provide the owner a copy of all documents signed by the owner in connection with the mortgage, the lender may correct its failure to comply by delivering the required documents to the borrower.
- If a lender failed to obtain a written acknowledgment of the fair market value of the property signed by both the owner and the lender, the lender may correct its failure to comply by obtaining the appropriate signatures.
- A lender may send the owner a written acknowledgment that the accrual of interest and all of the owner's obligations under the mortgage are abated until a prior prohibited lien is no longer secured by the property.
- If a lender's failure to comply is curable and cannot be cured in any of the ways discussed above, the lender may cure the failure to comply by giving the owner a refund or credit in the amount of $1,000 and offering the owner the right to refinance the mortgage for its remaining term at no cost and on the same terms, including interest rate, as the original loan with any modifications necessary to comply with Section 50(a)(6).

A servicer's failure to cure within 60 days after being notified of a failure to comply will result in the forfeiture of all principal and interest due under the Section 50(a)(6) mortgage. Therefore, servicers must have in place adequate procedures to receive and timely respond to borrower inquiries, claims of defects, and other complaints (whether or not the borrower specifically references Section 50(a)(6)). In addition, a servicer that receives a notification of failure to comply with respect to a Section 50(a)(6) mortgage owned by Fannie Mae should immediately notify a member of its Fannie Mae customer account team of the notification and, if the notification is in writing, provide Fannie Mae with a copy of the notification. Fannie Mae expects its servicers to timely cure all curable defects in accordance with applicable law.

When a lender sells us a Section 50(a)(6) mortgage, the lender warrants to us, among other things, that it, or any third-party originator of the mortgage, has complied with all of the provisions of Section 50(a)(6) that relate to origination and servicing of the mortgage. Fannie Mae has a variety of remedies available for a breach of a selling or servicing warranty (including repurchase and indemnification). In determining whether to enforce a particular remedy, Fannie

Mae will consider relevant factors, such as the reasons for the breach, the nature of the breach, the number of other loans affected, whether the breach was cured timely, and the consequences of the breach.

A mortgage that has been repurchased by a servicer and refinanced to cure a failure of the original mortgage to comply with Section 50(a)(6) is eligible for sale to Fannie Mae provided that it complies in all respects with our requirements.

As under prior law, when a lender originates a Section 50(a)(6) mortgage, it must confirm that at least 12 months have passed since any previous Section 50(a)(6) mortgage secured by the homestead property was closed. Under the Amendment, however, there is an exception to the 12-month limitation for a refinance done to cure a failure of the original mortgage to comply with Section 50(a)(6).

New Notice Provision

In addition to the 12-day cooling off period, the law was amended to add the requirement that a Section 50(a)(6) mortgage cannot close until one business day after the date that the owner receives a final itemized disclosure of the actual fees, points, interest, costs, and charges that will be charged at closing. The Amendment recognizes an exception to this rule if a bona fide emergency or another good cause exists and the lender obtains the written consent of the owner to provide the documentation on the date of closing or to modify previously provided documentation on the date of closing.

The Amendment does not define the term "business day" or explain how a business day is calculated. We understand that the Texas Finance Commission and the Texas Credit Union Commission will soon issue interpretations on, among other things, the definition of the term "business day." Until there is definitive guidance on these issues, we will require lenders to apply a conservative definition of business day that, at a minimum, excludes all days state or federal governments are closed for business, Sundays, and Saturdays (unless the lender is customarily open for business on Saturday). We will further require that at least one business day as so defined elapses after the day on which the notice is given and before the day on which the borrower signs the mortgage documents.

Title Insurance

For Section 50(a)(6) first mortgages, we continue to require a Mortgagee Policy of Title Insurance (Form T-2), which is supplemented by an Equity Loan Mortgage Endorsement (Form T-42) and a Supplemental Coverage Equity Loan Mortgage Endorsement (Form T-42.1). There may be no exceptions or deletions to the coverage provided by Paragraphs 2(a) through (e) of the T-42 endorsement, and the endorsement must include the optional coverage provided by Paragraph 2(f), as well as the additional coverage provided by Endorsement T-42.1. We understand that Endorsements T-42 and T-42.1 are likely to be amended as a result of the Constitutional Amendment to ensure compliance with the requirement for the new notice regarding closing costs, among other things, and we will require that all mortgages originated after the revised endorsements become available have the revised endorsements.

Relationship to Reverse Mortgages

The Amendment permits Section 50(a)(6) mortgages to be refinanced into reverse mortgages at any time. This is a new exception to the rule that "once a Section 50(a)(6) mortgage, always a

Section 50(a)(6) mortgage." As a result, once a borrower obtains a Texas Section 50(a)(6) mortgage (either a first lien or a subordinate lien), any subsequent refinancing of the homestead property (*except for a refinance which is a reverse mortgage*) will be subject to all of the provisions of Section 50(a)(6) if any of the proceeds are used to pay off the Section 50(a)(6) mortgage -- even if the borrower does not receive any cash out of the refinance proceeds.

New Documents

To facilitate compliance with the provisions of the Amendment, we have revised the following:

Texas Home Equity Security Instrument (First Lien) (Fannie Mae/Freddie Mac Form 3044.1) (Rev. 10/03)

Texas Home Equity Note (Fixed Rate-First Lien) (Fannie Mae/Freddie Mac Form 3244.1) (Rev. 10/03)

Texas Fixed/Adjustable-Rate Note (Nonconvertible) -- (First Lien) (Form 3522.44) (Rev. 10/03)

Texas Equity Fixed/Adjustable-Rate Note (Convertible) -- (First Lien) (Form 3523.44) (Rev. 10/03)

Texas Fixed/Adjustable-Rate Note (Two-Step) -- (First Lien) (Form 3263.44) (Rev. 10/03)

Texas Home Equity Affidavit and Agreement (First Lien) (Fannie Mae/Freddie Mac Form 3185) (Rev. 10/03)

We request that lenders begin using the revised forms as soon as possible and require that they be used for all Section 50(a)(6) mortgages delivered to Fannie Mae that are originated after January 15, 2004. Lenders are expected to reproduce their own supply of the revised forms. This may be done by using a print-out of the electronic version of the revised forms that are available through our Web site (www.efanniemae.com). (We will not be issuing a camera-ready copy of these forms to lenders.) Lenders that do not have access to the Internet may obtain the revised forms from their forms vendor. To obtain the forms from our Web site, go to the address indicated above. Once there, under the "Single-Family" drop down menu, select "Originating and Underwriting," then "Mortgage Documents" (located under "Forms & Guidelines"), then the type of form, and then the specific form to be viewed, downloaded, or printed.

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Lenders should contact their Customer Account Manager in their lead Fannie Mae office if they have any questions about the changes discussed in this Announcement.

Pamela S. Johnson

Senior Vice President