

BILL ANALYSIS

S.B. 43
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Pensions, Investments & Financial Services
Committee Report (Unamended)

BACKGROUND AND PURPOSE

Wrap loans are a legal mortgage product in Texas, often used by sellers to finance the sale of a property already subject to an existing mortgage lien. The intended use of these loan products results in buyers paying the wrap lender the down payment and monthly mortgage payments, and the wrap lender paying the lienholder. However, there are concerns about predatory lenders using these products to defraud buyers and sellers, particularly in underserved communities, because these loan products are not subject to the same oversight as other mortgage products. A fraudulent wrap lender may pocket the buyer's money instead of paying the lienholder, which can result in mortgage defaults, negative credit score reports, loss of money, and foreclosure.

S.B. 43 seeks to subject wrap loans to regulation like other mortgage loan products and provide certain protections for buyers and sellers, including written disclosures, a statute of limitations, closing requirements, and the establishment of fiduciary responsibilities.

CRIMINAL JUSTICE IMPACT

It is the committee's opinion that this bill does not expressly create a criminal offense, increase the punishment for an existing criminal offense or category of offenses, or change the eligibility of a person for community supervision, parole, or mandatory supervision.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the Finance Commission of Texas in SECTION 3 of this bill.

ANALYSIS

S.B. 43 amends the Finance Code to establish regulations for the financing of residential real estate purchases by means of a wrap mortgage loan, as defined by the bill, and to make certain other changes relating to exemptions from residential mortgage loan regulations.

License or Registration Required

S.B. 43 prohibits a person from originating or making a wrap mortgage loan unless the person is licensed or registered to originate or make residential mortgage loans under the Residential Mortgage Loan Company Licensing and Registration Act, the Mortgage Banker Registration and Residential Mortgage Loan Originator License Act, or statutory provisions regulating consumer loans, or the person is exempt from licensing or registration as provided under those laws.

Transaction Requirements and Related Remedies

S.B. 43 requires a wrap lender to provide to the wrap borrower by a specified deadline a separate written disclosure statement in at least 12-point type that contains the following:

- the information required for a written disclosure statement for the conveyance of

residential property encumbered by a lien; and

- a specified statement encouraging the buyer to consider purchasing property insurance coverage to protect their interests because insurance maintained by a seller, lender, or other person who is not the buyer may not provide coverage to the buyer in the event of loss or liability.

The bill requires the disclosure statement to be dated and signed by the wrap borrower on receipt and requires the Finance Commission of Texas by rule to adopt a model disclosure statement. The bill sets out a requirement for the provision of disclosure statements in a foreign language if applicable.

If the required disclosure statement and any required foreign language disclosure are received by the wrap borrower on or before the closing date of the wrap mortgage loan, the wrap borrower may rescind the wrap mortgage loan agreement and any related purchase agreement or other agreement relating to the loan transaction not later than the seventh day after the date of receipt of the disclosure statement, regardless of whether the disclosure is timely made. On rescission, the wrap borrower is entitled to a return of any earnest money, escrow amounts, down payment, or other fees or charges paid in connection with the wrap mortgage loan, the related purchase transaction, and any other related transaction.

S.B. 43 also provides for a wrap borrower's right to rescind the wrap mortgage loan agreement and the related purchase agreement if the wrap mortgage loan is closed without the wrap lender providing the required disclosure statement or any required foreign language disclosure. Such a rescission is made by providing the wrap lender notice in writing and may be made at any time, except that if the wrap borrower receives the disclosure after closing but before the wrap borrower provides notice of rescission, the wrap borrower may make the rescission on or before the 21st day after the date of receipt. With respect to such a rescission, the bill provides for the following:

- the wrap lender's return to the wrap borrower of applicable principal and interest payments, escrow amounts, and money or property given as earnest money, a down payment or otherwise in connection with the loan or purchase transaction not later than the 30th day after the date the wrap borrower provides notice of rescission;
- the wrap borrower's conveyance to the wrap lender or the lender's designee of the applicable residential real estate and the deadline by which the wrap borrower must surrender possession of that real estate; and
- the ability of the wrap lender to avoid rescission by taking the following actions by a specified deadline:
 - paying the outstanding balance due on certain debt;
 - paying any due and unpaid taxes or other government assessment on the residential real estate;
 - providing evidence of those payments to the wrap borrower; and
 - paying to the wrap borrower as damages for noncompliance the sum of \$1,000 and any reasonable attorney's fees incurred by the wrap borrower.

If a wrap lender fails to timely provide the required disclosure statement or fails to provide it in a foreign language as required, the limitations period applicable to certain causes of action against the wrap lender in connection with the loan transaction is tolled until the 120th day after the date the statement is provided.

S.B. 43 voids a lien securing a wrap mortgage loan unless the wrap mortgage loan and the conveyance of the residential real estate securing the loan are closed by an attorney or a title company. The bill authorizes a wrap borrower to bring an action as follows:

- to obtain declaratory or injunctive relief to enforce the bill's wrap mortgage loan transaction requirements;
- to recover any actual damages suffered by the wrap borrower as a result of a violation of those requirements; or
- to obtain other remedies available under the bill's provisions relating to transaction requirements and remedies or in an action under the Deceptive Trade Practices-

Consumer Protection Act as otherwise authorized by such bill provisions. The bill authorizes a wrap borrower who prevails in such an action to recover court costs and reasonable attorney's fees.

S.B. 43 voids any purported waiver of a right of a wrap borrower under the bill's provisions relating to transaction requirements and remedies and any purported exemption of a person from liability for a violation of such provisions. The bill prohibits a person who is a party to a residential real estate transaction from evading the application of those bill provisions by any device, subterfuge, or pretense and makes any attempt to do so void and a deceptive trade practice under the Deceptive Trade Practices-Consumer Protection Act and actionable under that act.

S.B. 43 authorizes the Finance Commission of Texas to adopt and enforce rules necessary for the intent of or to ensure compliance with the bill's provisions relating to transaction requirements and remedies.

Duties Owed to Wrap Borrower

S.B. 43 establishes that a person who collects or receives a payment from a wrap borrower under the terms of a wrap mortgage loan holds the money in trust for the benefit of the borrower. The bill establishes that a person who collects or receives a payment from a wrap borrower under the terms of or in connection with such a loan owes a fiduciary duty to the wrap borrower to use the payment in satisfaction of the following:

- the obligee's obligations under each debt incurred by a person other than the wrap borrower that was not paid off at the time the loan was made; and
- the payment of taxes and insurance for which the wrap lender has received any payments from the wrap borrower.

Wrap Borrower's Right to Deduct

S.B. 43 authorizes a wrap borrower, without taking judicial action, to deduct the following amounts from any amount owed to the wrap lender under the terms of a wrap mortgage loan for a purchase of residential real estate to be used as the wrap borrower's residence:

- the amount of any payment made by the wrap borrower to an obligee of a debt incurred by a person other than the wrap borrower that was not paid off at the time the loan was made, if that payment was made to cure a default by the wrap lender caused by the lender's failure to make payments for which the lender is responsible under the terms of the wrap mortgage loan; or
- any other amount for which the wrap lender is liable to the wrap borrower under the terms of the wrap mortgage loan.

Enforcement of Residential Mortgage Loan Servicer Registration Requirements

S.B. 43 authorizes the savings and mortgage lending commissioner to conduct an inspection of a wrap lender registered under the Residential Mortgage Loan Servicer Registration Act as the commissioner determines necessary to determine whether the wrap lender is complying with that act and applicable rules. The bill sets out the authorized scope of the inspection and also authorizes the commissioner, for reasonable cause, to investigate such a registered wrap lender at any time to determine compliance. The commissioner may conduct an undercover or covert investigation only if the commissioner, after due consideration of the circumstances, determines that the investigation is necessary to prevent immediate harm and to carry out the purposes of the act.

S.B. 43 requires the finance commission by rule to provide guidelines to govern such an inspection or investigation. The bill sets out provisions relating to the confidentiality of

information obtained during the inspection or investigation, the sharing of such information with a state or federal agency, and the issuance and enforcement of subpoenas during an investigation. The bill provides for reimbursement of expenses for each examiner for an on-site examination or inspection under specified circumstances and requires the finance commission by rule to set the maximum amount for such reimbursement.

Cease and Desist Orders

S.B. 43 authorizes the savings and mortgage lending commissioner, if the commissioner has reasonable cause to believe that a wrap lender or wrap mortgage loan originator to whom the bill's wrap loan provisions apply has violated or is about to violate those provisions, to issue without notice and hearing an order to cease and desist from continuing a particular action or an order to take affirmative action, or both, to enforce compliance with those provisions.

S.B. 43 provides for the order's content and requires the commissioner, if a person against whom the order is made requests a hearing within a specified time frame, to set and give notice of a hearing before the commissioner or a hearings officer under the Administrative Procedure Act. The commissioner by order may find a violation has occurred or not occurred based on the hearing officer's findings of fact, conclusions of law, and recommendations. If a hearing is not requested within the specified time frame, the order is considered final and not appealable.

S.B. 43 authorizes the commissioner, after giving notice and an opportunity for hearing, to impose against a person who violates a cease and desist order an administrative penalty capped at \$1,000 for each day of the violation. The bill authorizes the commissioner, in addition to any other remedy provided by law, to institute in district court a suit for injunctive relief and to collect the administrative penalty. A bond is not required of the commissioner with respect to injunctive relief granted under these provisions.

Exemptions

S.B. 43 establishes that its provisions relating to wrap mortgage loan financing do not apply to a wrap mortgage loan made by or on behalf of an owner of residential real estate on which a dwelling has not been constructed under certain conditions and do not apply to a wrap mortgage loan for a sale of residential real property that is the wrap lender's homestead. The bill exempts the following from the application of such provisions:

- a federally insured bank, savings bank, savings and loan association, Farm Credit System institution, or credit union or a subsidiary of such an entity;
- the state, an instrumentality of the state, or an employee of such an entity who is acting within the scope of the person's employment; and
- an owner of residential real estate who does not in any 12-consecutive-month period make, or contract with another person to make, more than five wrap mortgage loans to purchasers of the property for all or part of the purchase price of the residential real estate against which the mortgage is secured.

Residential Mortgage Loan Regulation Exemptions

S.B. 43 establishes that, in determining eligibility for the following exemptions, two or more owners of residential real estate or a dwelling, as applicable, are considered a single owner for the purpose of computing the number of mortgage loans made within an applicable period if any of the owners are affiliates or if any of the owners have substantially common ownership, as determined by the savings and mortgage lending commissioner:

- an exemption from the bill's provisions regarding wrap mortgage loan financing for an owner of residential real estate who makes wrap mortgage loans;
- an exemption from the Residential Mortgage Loan Company Licensing and Registration Act for an owner of residential real estate who makes residential mortgage loans;
- an exemption from provisions of the Mortgage Banker Registration and Residential

Mortgage Loan Originator License Act applicable to residential mortgage loan originators for employees of residential real estate owners when acting for the benefit of those owners; and

- an exemption from the Texas Secure and Fair Enforcement for Mortgage Licensing Act of 2009 for an owner of residential real estate or a dwelling who makes residential mortgage loans.

EFFECTIVE DATE

January 1, 2022.