

- SUBJECT:** Establishing requirements for certain residential mortgage loans
- COMMITTEE:** Pensions, Investments and Financial Services — committee substitute recommended
- VOTE:** 8 ayes — Anchia, Parker, Capriglione, Muñoz, Perez, Rogers, Stephenson, Vo
- 1 nay — Slawson
- WITNESSES:** For — Trish McAllister, Texas Access to Justice Commission; John Fleming, Texas Mortgage Bankers Association; Veronica Carbajal, Texas RioGrande Legal Aid, Inc.; Humberto Hernandez; (*Registered, but did not testify*: Ernest Garcia, Department of Savings and Mortgage Lending; Stephen Scurlock, Independent Bankers Association of Texas; Celeste Embrey, Texas Bankers Association; Laura Matz, Texas Community Associate Advocates)
- Against — None
- BACKGROUND:** Finance Code sec. 156.202 governs exemptions from residential mortgage loan company licenses and registration requirements. The following entities are exempt from certain requirements:
- a nonprofit organization;
 - a mortgage banker registered under the Mortgage Bankers and Residential Mortgage Loan Originator License Act;
 - any owner of residential real estate who in any 12-consecutive-month period makes no more than five residential 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; and
 - an entity that is a depository institution or a subsidiary of a depository institution that is owned and controlled by the depository institution and regulated by a federal banking agency, or

an institution regulated by the Farm Credit Administration.

Concerns have been raised about lack of regulatory scrutiny over wrap mortgages, which are legal mortgage products that often are used by sellers to finance the sale of a property already subject to an existing mortgage lien. Some have called for wrap mortgages to be regulated similar to other mortgage loan products.

DIGEST:

CSHB 216 would prohibit the origination of a wrap mortgage loan on residential property by a person who was not licensed or registered to make residential mortgage loans or was exempt from licensing or registration as provided in the bill. The bill would establish licensing and registration requirements for wrap mortgage lenders, loan financing provisions and fiduciary duties owed to wrap borrowers, and authorize the Savings and Mortgage Lending Commissioner to enforce and investigate violations and impose a penalty.

Wrap mortgage loan. Under the bill, a wrap mortgage loan would mean a residential mortgage loan made to finance the purchase of residential real estate that would continue to be subject to an unreleased lien that was attached to the residential real estate before the loan was made and secured a debt incurred by a person other than the wrap borrower that was not paid off at the time the loan was made. The wrap borrower would be obligated to the wrap lender for payment of a debt the principal amount of which included the outstanding balance of the debt and any remaining amount of the purchase price financed by the wrap lender.

License or registration requirements. A person would be prohibited from originating or making a wrap mortgage loan unless the person was 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 was exempt from licensing or registration as provided under those laws.

Transaction requirements, remedies. On or before the seventh day before the wrap mortgage loan was entered into, a wrap lender would be required to provide the wrap borrower a written disclosure statement that:

- contained the information required for a written disclosure statement for the conveyance of residential property encumbered by a lien; and
- included a statement that encouraged the buyer to consider purchasing property insurance to protect their interests because insurance maintained by the seller, lender, or other person who was not the buyer may not provide coverage to the buyer in the event of loss or liability.

The bill would require the disclosure statement to be dated and signed by the wrap borrower on receipt. The Finance Commission of Texas by rule would have to adopt a model disclosure statement. If the negotiations that preceded the execution of the wrap mortgage loan agreement were conducted primarily in a language other than English, the lender would have to provide the borrower with the disclosure statement in that language.

Right of rescission. The bill would establish provisions relating to a wrap borrower's option to rescind the wrap mortgage loan agreement and any related purchase agreement or other agreement related to the loan transaction, with different procedures depending on whether the wrap lender provided the required disclosure statement before closing or failed to do so. If a wrap lender failed to timely provide the required disclosure statement, the limitations period applicable to certain causes of action of the wrap borrower against the wrap lender in connection with the loan transaction would be tolled until the 120th day after the date the required disclosure statement was provided.

By the 30th day after the date the wrap borrower provided notice of rescission, the wrap lender would be required to return to the wrap borrower:

- all principal and interest payments made by the wrap borrower on the wrap mortgage loan;
- any money or property given as earnest money, a down payment, or otherwise in connection with the wrap mortgage loan or related purchase transactions; and
- any escrow amounts for the wrap mortgage loan or related purchase transaction.

On the date on which all of the returned money or property given as earnest money was received by the wrap borrower, the borrower would be required to convey to the wrap lender or the lender's designee the residential real estate. The wrap borrower would have to surrender possession of the residential real estate by the 30th day after the date of their receipt of the money or property returned.

The wrap lender could avoid rescission if by the 30th day after the date of receipt of notice of rescission the wrap lender:

- paid the outstanding balance due on any debt incurred by a person other than the wrap borrower that was not paid off at the time the loan was made;
- paid any due and unpaid taxes or other government assessment on the residential real estate made to finance the purchase of residential real estate that was subject to an unreleased lien;
- paid to the wrap borrower as damages for noncompliance \$1,000 and any reasonable attorney's fees incurred by the wrap borrower; and
- provided to the wrap borrower evidence of compliance.

A lien that secured a wrap mortgage loan would be voided unless the wrap mortgage loan and the conveyance of the residential real estate that secured the loan were closed by an attorney or a title company. The bill would authorize a wrap borrower to bring an action to:

- obtain declaratory or injunctive relief to enforce the bill's wrap mortgage loan transaction requirements;

- recover any actual damages suffered by the wrap borrower as a result of a violation of those requirements; or
- obtain other remedies available under the bill's provisions related to transaction requirements and remedies or in an action under the Deceptive Trade Practices-Consumer Protection Act as otherwise authorized by the bill's provisions.

A wrap borrower who prevailed in such an action could recover court costs and reasonable attorney's fees.

The bill would authorize the Finance Commission of Texas to adopt and enforce rules necessary for the intent of or to ensure compliance with the bill's provisions related to transaction requirements and remedies.

Duties owed a wrap borrower. A person who collected or received a payment from a wrap borrower under the terms of a wrap mortgage loan would hold the money in trust for the benefit of the borrower and owe a fiduciary duty to the borrower to use the payment to satisfy 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 had received any payments from the wrap borrower.

Borrower's right to deduct. The wrap borrower, without taking any judicial action, could deduct from any amount owed to the wrap lender under the terms of the wrap mortgage loan for the 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 had not been 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 was responsible under the terms of the wrap mortgage loan; or

- any other amount for which the wrap lender was liable to the wrap borrower under the terms of the wrap mortgage loan.

Enforcement of requirements. The bill would authorize 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 decided was necessary to determine whether the wrap lender had complied with that act and applicable rules. The commissioner could share evidence of criminal activity gathered during an inspection or investigation with any state or federal law enforcement agency.

At any time, the commissioner could, for reasonable cause, investigate a wrap lender to determine compliance. An undercover or covert investigation could be conducted only if the commissioner determined that the investigation was necessary to prevent immediate harm and to carry out the purposes of the Residential Mortgage Loan Servicer Registration Act.

The bill would require the finance commissioner by rule to provide guidelines to govern an inspection or investigation including rules to determine the information and records of the wrap lender to which the commissioner could demand access during an inspection or investigation and to establish what constituted reasonable cause for an investigation.

Information obtained by the commissioner during an inspection or investigation would be confidential unless disclosure of the information was permitted or required by other law. The commissioner could share such information with a state or federal agency, but only if the commissioner determined there was a valid reason to do so.

The bill would provide for reimbursement expenses for each examiner for an on-site examination or inspection under specified circumstances and require the finance commission by rule to set the maximum amount for reimbursement.

During an investigation, the commissioner could issue a subpoena addressed to a peace officer of this state or other person authorized by law to serve citation or perfect service. Persons who disobeyed a subpoena or refused to testify in connection with an investigation could, on petitioning by the commissioner, be ordered by a district court in Travis County to obey the subpoena, testify, or produce documents related to the matter.

Cease and desist orders. If the commissioner had reasonable cause to believe that a wrap lender or wrap mortgage loan originator had violated or was about to commit a violation of the bill's provisions, the commissioner could 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.

The cease and desist order would have to contain a reasonably detailed statement of the facts on which the order was made. If the person against whom the order was made requested a hearing, the commissioner would be required to set and give notice of a hearing before the commissioner or a hearing officer under the Administrative Procedure Act. The commissioner by order could find a violation had occurred or not occurred based on the hearing officer's findings of fact, conclusions of law, and recommendations. If a hearing was not requested on or before the 30th day after the date on which an order was made, the order would be considered final and not appealable.

After giving notice and an opportunity for a hearing, the commissioner could impose against a person who violated a cease and desist order an administrative penalty of not more than \$1,000 for each day of the violation. The bill would authorize 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 would not be required of the commissioner with respect to injunctive relief granted under the bill's provisions.

Exemptions. The bill would not apply to a wrap mortgage loan made by or on behalf of an owner of residential real estate on which a dwelling had

not been constructed under certain conditions and would not apply to a wrap mortgage loan for a sale of residential real property that was the wrap lender's homestead. Under the bill, the following would be exempt:

- 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 was acting within the scope of the person's employment; and
- an owner of residential real estate who did 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 was secured.

For the purposes of granting certain exemptions to mortgage regulations as specified in the bill, two or more owners of residential real estate or a dwelling, as applicable, would be considered a single owner for the purpose of computing the number of mortgage loans made within any 12-consecutive-month period if the owners were affiliated or if any of the owners had substantially common ownership, as determined by the savings and mortgage lending commissioner.

The bill would take effect January 1, 2022.