HOUSE BILL REPORT
EHB 1311

As Passed House:
March 3, 2009

Title: An act relating to reverse mortgage lending.

Brief Description: Regulating reverse mortgage lending practices.

Sponsors: Representatives Kirby, Bailey, Morrell, Sullivan, Kenney, Simpson and Nelson; by request of Department of Financial Institutions.

Brief History:

Committee Activity:

Financial Institutions & Insurance: 1/27/09, 1/29/09 [DP];
General Government Appropriations: 2/10/09, 2/17/09 [DP].

Floor Activity

Passed House: 3/3/09, 97-0.

Brief Summary of Engrossed Bill

- Establishes financial requirements for certain reverse mortgage lenders.
- Provides contractual standards for certain reverse mortgage loans.

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: Do pass. Signed by 11 members: Representatives Kirby, Chair; Kelley, Vice Chair; Bailey, Ranking Minority Member; Parker, Assistant Ranking Minority Member; Hurst, McCoy, Nelson, Roach, Rodne, Santos and Simpson.

Staff: Jon Hedegard (786-7127)

HOUSE COMMITTEE ON GENERAL GOVERNMENT APPROPRIATIONS

Majority Report: Do pass. Signed by 13 members: Representatives Darneille, Chair; Takko, Vice Chair; McCune, Ranking Minority Member; Armstrong, Blake, Dunshee, Hudgins, Kenney, Pedersen, Sells, Short, Van De Wege and Williams.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Staff: Serah Stetson (786-7109)

Background:

The Consumer Loan Act (CLA) authorizes the Department of Financial Institutions (DFI) to regulate consumer loan companies doing business in Washington. Consumer loan companies include mortgage lenders and consumer finance companies. Retail installment contracts are exempt from the CLA. The CLA:

- limits the rates and fees lenders may charge on loans;
- establishes methods of calculation of interest;
- establishes standards for billing cycles;
- restricts certain loan provisions (one example is prepayment penalties);
- requires that lenders fully disclose the terms of loans; and
- prohibits lenders from engaging in unfair and deceptive acts and practices.

In 2008 the Legislature passed Senate Bill 6471. This law applied the CLA to all loans made at any interest rate, not just those loans which exceed the rate established by the usury law (currently 12 percent). All loans must be calculated using a simple interest method which prohibits compounding interest. There are specific interest calculations for each billing cycle.

The Federal Housing Administration (FHA) is a federal program that provides mortgage insurance on specific types of loans. One such loan is a Home Equity Conversion Mortgage (HECM). A HECM is FHA's reverse mortgage program. To qualify a borrower must:

- be 62 years of age or older;
- own the property outright or have a small mortgage balance;
- occupy the property as their principal residence;
- not be delinquent on any federal debt; and
- participate in a consumer information session given by an approved HECM counselor.

The FHA allows a person to borrow against the equity in their home. There are five payment plan options:

- *tenure*- equal monthly payments as long as at least one borrower lives and occupies the property as a principal residence;
- *term* - equal monthly payments for a fixed period of months selected;
- *line of credit* - unscheduled payments or in installments, at times and in an amount of the borrower's choosing until the line of credit is exhausted;
- *modified tenure*- combination of line of credit plus scheduled monthly payments for as long as the borrower remains in the home; and
- *modified term* - combination of line of credit plus monthly payments for a fixed period of months selected by the borrower.

Payment options may be changed by the borrower for a fee of $20.

A HECM does not require repayment as long as the home is the borrower's principal residence. Lenders recover their principal, plus interest, when the home is sold. Any remaining value of the home goes to the borrower or their heirs. The borrower can never owe more than the home's value. If the sales proceeds are less than the amount owed, the FHA pays the lender the amount of the shortfall. The FHA collects an insurance premium from all borrowers to provide this coverage.

A HECM loan must be repaid in full when the borrower dies or sells the home. The loan also becomes due and payable if:

- the borrower does not pay property taxes or insurance or violates other obligations;
- the borrower permanently moves to a new principal residence;
- any borrower fails to live in the home for 12 months in a row; or
- the borrower allows the property to deteriorate and does not make necessary repairs.

Summary of Engrossed Bill:

A "reverse mortgage loan" is defined as a nonrecourse consumer credit obligation in which:

- a mortgage, deed of trust, or equivalent consensual security interest securing one or more advances is created in the borrower's dwelling;
- the broker or lender is licensed under Washington law or exempt from licensing under federal law; and
- any principal, interest, or shared appreciation or equity is due and payable, other than in the case of default, only after:
  1. the consumer dies;
  2. the dwelling is transferred; or
  3. the consumer ceases to occupy the dwelling as a dwelling.

Reverse mortgage loans are exempted from the compounding interest prohibition and the billing and interest calculations of the CLA.

Two categories of reverse mortgage loans are created:

- A "FHA-approved reverse mortgage" is defined as a "home equity conversion mortgage" or other reverse mortgage product guaranteed or insured by the federal Department of Housing and Urban Development (HUD).
- A "proprietary reverse mortgage loan" is any reverse mortgage loan product that is not a home equity conversion mortgage loan or other federally guaranteed or insured loan.

A licensee offering proprietary reverse mortgage loans must:

- maintain letters of credit in an amount necessary to fund all reverse mortgage loan requirements or $3 million, whichever is greater; and
- maintain a minimum capital of $10 million. A licensee may rely on the capital of a parent entity if the parent: (1) has a net worth of at least $100 million and (2) provides a binding written commitment to the licensee to make a minimum of $10 million available to the licensee.

The financial requirements do not apply if the licensee:

- fully disburses the proceeds of the proprietary reverse mortgage loans proceeds at the loan closing; or
- only originates proprietary reverse mortgage loans that are sold into the secondary market to an investor with a specified credit rating. There must be a written

commitment from the investor to purchase the loans prior to closing. Delivery must be made to the investor within 10 days of the loan closing.

A proprietary reverse mortgage lender must:

- only make a reverse mortgage loan for a resident of this state that is at least 60 years of age at the time the loan is executed;
- refer a prospective borrower to an independent housing counseling agency approved by the HUD for counseling. The counseling must meet the standards and requirements established by the HUD for reverse mortgage counseling. The lender must provide the borrower with a list of at least five independent housing counseling agencies approved by the HUD, including at least two agencies that can provide counseling by telephone;
- allow prepayment without penalty at any time during the term of the reverse mortgage loan, with limited exceptions. A borrower must be provided prior written notice of any permissible prepayment penalty under this section;
- pay a specified late charge to the borrower for any late advance. The lender forfeits the right to interest and a monthly servicing fee for any months in which the advance has not been timely made;
- issue advances directly to the borrower, or his or her legal representative. This does not apply to an initial disbursement of moneys to the closing agent;
- disclose any interest rate or other fees to be charged between the date that the reverse mortgage loan is due and payable and when it is paid in full;
- disclose that the deed of trust secures a reverse mortgage loan; and
- provide an annual disclosure statement to the borrower, including details of the loan advances, balance, and other terms. This may be provided by a loan servicer.

The reverse mortgage loan may become due and payable upon the occurrence of any one of the following events:

- the home securing the loan is sold or title to the home is otherwise transferred;
- a defaulting event occurs which is specified in the loan documents; or
- all borrowers cease occupying the home as a principal residence.

Temporary absences from the home not exceeding 180 days do not cause the mortgage to become due and payable. Extended absences from the home exceeding 180 consecutive days, but less than one year, do not cause the mortgage to become due and payable if the borrower has taken prior action that secures and protects the home in a manner satisfactory to the lender.

A reverse mortgage lender must not:

- require an applicant to purchase an annuity as a condition of obtaining a reverse mortgage loan;
- offer an annuity to the borrower prior to the closing or before the expiration of the right of the borrower's rescission rights;
- refer the borrower to anyone for the purchase of an annuity prior to the closing or before the expiration of the right of the borrower's rescission rights;
- provide marketing information or annuity sales leads to anyone regarding the borrower, or receive any compensation for such an annuity sale or referral;

- take a proprietary reverse mortgage loan application unless the applicant has received a statement advising the prospective borrower about counseling prior to obtaining the reverse mortgage loan within three business days of receipt of the completed loan application; and
- accept a final and complete application from a prospective applicant or assess any fees upon a prospective applicant without first receiving a certification that the applicant has received counseling. The certification must be signed by the borrower and the counselor. The lender must retain the certification for the term of the reverse mortgage.

Lender and any other parties that participate in the origination of a reverse mortgage loan may not require an applicant to purchase insurance or other products as a condition of the loan.

Lender and other parties that participate in the origination of a reverse mortgage loan are prohibited from selling any other insurance or financial product to the borrower.

A borrower in a proprietary reverse mortgage transaction has the right to rescind within three business days of the transaction.

A reverse mortgage loan may provide for a fixed or adjustable interest rate or a combination, including compound interest, and may also provide for interest that is contingent on the value of the property upon execution of the loan or at maturity, or on changes in value between closing and maturity.

A proprietary reverse mortgage loan product may not be offered without preapproval by the Department of Financial Institutions (DFI). The Director of the DFI may make rules regarding the preapproval process and may disapprove any proprietary reverse mortgage loan products that are unfair, ambiguous, misleading or are contrary to public policy. The DFI has specific authority to develop rules regarding the interpretation and implementation of this section.

If a lender defaults and fails to cure the default, the borrower, or the borrower's estate, is entitled to treble damages. A borrower may also seek other remedies provided under law.

A violation of federal legal requirements for an FHA-approved reverse mortgage is a violation of state law.

There are provisions for the treatment of advances and undisbursed reverse mortgage loan funds for the purpose of determining eligibility and benefits under means-tested programs.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony (Financial Institutions & Insurance):

(In support) Often, the implementation of legislation reveals inadvertent impacts. An unintended consequence from a bill last year impacted certain lenders. This bill fixes those problems and provides a regulatory framework for reverse mortgage lenders. The bill was worked on throughout the interim by the DFI and stakeholders. The DFI supports the bill. It corrects a problem from last year's bill that was not known at the time the bill was passed. Last year's bill put certain loans under the CLA. The CLA prohibits compounding interest. A reverse mortgage is based on compounding interest so certain types of reverse mortgages were unintentionally prohibited. The DFI reviewed reverse mortgage lending laws from around the country and developed a structure for this state. There have been many meetings with stakeholders and this bill is a product of those discussions. The state will be prepared for what may be a significant growth in the use of reverse mortgages. Reverse mortgages can be very useful but they can also be expensive and complex. This bill establishes certain consumer protections for borrowers. Certain reverse mortgages with federal oversight are not subject to this bill.

(Opposed) None.

Staff Summary of Public Testimony (General Government Appropriations):

(In support) This legislation corrects unintended consequences of Senate Bill 6471 which put certain loans under the Consumer Loan Act. Compounding interest is an integral part of reverse mortgage loans. This legislation is the result of work with stakeholders, industry and review of other state's best practices. Reverse mortgages are expected to rapidly increase in use and popularity. Reverse mortgage products can be very expensive and Washingtonians should know exactly what they are getting. The Department of Financial Institutions currently regulates this industry and this is simply an extension of that oversight.

(Opposed) None.

Persons Testifying (Financial Institutions & Insurance): Representative Kirby, prime sponsor; and Deborah Bortner, Department of Financial Institutions.

Persons Testifying (General Government Appropriations): Levi Clemmens and Cindy Fazio, Department of Financial Institutions.

Persons Signed In To Testify But Not Testifying (Financial Institutions & Insurance): None.

Persons Signed In To Testify But Not Testifying (General Government Appropriations): None.