Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Consumer Protection & Business Committee

HB 1464

Brief Description: Concerning home equity sharing agreements.

Sponsors: Representatives Hackney, Walen and Wylie.

Brief Summary of Bill

- Requires a home equity sharing agreement (HESA) originator to be licensed and subject to regulation by the Department of Financial Institutions (DFI) by July 1, 2026.
- Establishes obligations, required disclosures, prohibited acts, and violations for HESA originators, along with a variety of administrative, investigative, and enforcement duties for the DFI.

Hearing Date: 2/14/25

Staff: Megan Mulvihill (786-7304).

Background:

Financial Tools to Access Home Equity.
Homeowners have a number of options for accessing equity in their homes.

Home Equity Loans. This product allows a borrower to receive a lump sum equity draw in exchange for repaying the principle at a fixed interest rate. These loans are commonly referred to as second liens or second mortgages. Certain fees and credit checks are needed for approval from a lender.

Cash-out Refinance. This is a similar product to a home equity loan, but it refinances the entire value of the mortgage in addition to the amount of equity a borrower wants to take out of their home. A cash-out refinance requires certain fees and credit checks for approval from a lender. The additional proceeds from a cash-out refinance are not taxable.

Home Equity Line of Credit. A home equity line of credit (HELOC) provides a borrower a line of credit up to a set maximum. Rather than having to take a lump sum, as one does in a home equity loan or a cash-out refinance, a HELOC allows a borrower to pay interest on the amount of home equity they draw. This financial product has a variable interest rate which can increase or decrease a borrower's payment. Repayment begins once the draw period ends.

<u>Home Equity Sharing Agreements.</u>
Home equity sharing agreements (HESAs) are financial arrangements between a homeowner and an investor to share ownership and appreciation of a property. Typically, an investor provides funds to the homeowner for a share of a property's future value. The HESA has an established term, anywhere between 10 and 30 years, and the investor places a lien on the property. Upon expiration of the term, sale of the property, or another triggering event, the HESA must be settled. This often occurs by either the homeowner paying off a settlement amount to have the lien removed or by the home being sold and the HESA provider receiving their initial investment amount, plus a share of the property's equity.

The Legislature directed the Department of Financial Institutions (DFI) to study HESAs through a budget proviso during the 2024 legislative session. The study was published in September 2024 and contains information and data collected from inquiries sent to HESA providers. The study looked at how HESAs are established, including advertising, applications, origination, underwriting, appraisals, disclosures, servicing, and termination. The DFI also reviewed how HESA providers calculate the different values used in establishing HESAs and included data on HESA activity in Washington.

Summary of Bill:

<u>Home Equity Sharing Agreements</u>.
A HESA is defined as any nonrecourse obligation in which an advance sum of money is extended to a homeowner in exchange for an interest or future share of equity in the homeowner's primary dwelling or a future obligation to pay a sum upon the occurrence of an agreed-upon event. A HESA is not a residential mortgage loan or other form of loan regulated under the Consumer Loan Act. Additional terms are defined, such as: agreed home value, annualized cost, beginning home equity, HESA originator, investment amount, and settlement payment.

<u>Licensing Requirement</u>.
Beginning July 1, 2026, no person may conduct business as a HESA originator, or offer or originate a HESA, without first obtaining and maintaining a license from the DFI. Any HESA made concerning a homeowner's primary dwelling physically located in Washington is subject to

the regulations established. A person seeking to obtain a license must submit an application to the DFI with the required information, including fingerprints and information required to run a background check, pay the required investigation and license fee, and obtain and maintain a surety bond of a minimum of $30,000.

Department of Financial Institution's Responsibilities.
The DFI has broad administrative discretion and rulemaking authority in regulating HESAs. The DFI must issue licenses to applicants who meet conditions for licensure and collect annual assessments from each licensee. The DFI also has the authority to deny, condition, suspend, and revoke licenses under certain conditions, such as failure to pay fees or violating regulations.

The DFI has investigative authority and may at any time examine the business and books, accounts, records, papers, documents, files, and other information used by a licensee for the purpose of discovering violations. Every licensee examined or investigated by the DFI must pay for the cost of the examination or investigation. If needed, the Director of the DFI may apply for and obtain a court order authorizing a subpoena for testimony, documents, records, or evidence. Licensees are responsible for an annual assessment to be determined by the DFI.

The DFI also may order the discontinuance of any injurious or illegal practice, may issue temporary cease and desist orders, and may bring an action to enjoin the acts or practices that constitute violations and to enforce compliance. The Administrative Procedures Act governs proceedings for denying licenses, issuing cease and desist orders, suspending or revoking licenses, imposing civil penalties or other remedies, and appeals. The Director of the DFI may recover the state's costs for prosecuting violations, staff time for administrative hearings, and reasonable attorneys' fees when a violation is determined to have occurred.

Obligations of a Home Equity Sharing Agreement Originator.
A HESA originator has four key obligations:
- providing at least three business days in which the homeowner may rescind their acceptance of the HESA before it is effective and binding;
- ensuring the homeowner's beginning home equity is equal to or greater than 10 percent;
- ensuring appraisals or other valuation reports meet industry standards and are conducted by an independent third party, unless an affiliated appraisal or valuation is disclosed and consented to in writing by the homeowner; and
- ensuring the annualized cost of a HESA does not exceed 25 percent.

Required Disclosures.
A HESA originator is required to provide the homeowner with a disclosure before entering into a HESA. The disclosure must contain at least:
- a clear and conspicuous statement that entering into a HESA means a lien will be placed on the property and that failure to comply with the terms or an inability to settle the HESA may result in loss of the property, and the homeowner should obtain the advice of an attorney;
- a summary of the HESA's terms, including:

- the investment amount;
- an itemization of any charges and payments to third parties and any fees paid to the HESA originator that are deducted from the investment amount;
- net proceeds delivered to the homeowner at closing;
- the maximum term of the HESA;
- how the homeowner can settle the HESA and an explanation of how the settlement cost is calculated; and
- a summary of the types of fees that may be charged in connection with a settlement;
- the agreed home value without adjustment, the method used to determine the agreed home value, the amount of adjustments, and the value of the property used for purposes of calculating the share of appreciation or equity;
- the method of determining the final value of the property that is the subject of the HESA upon settlement;
- the maximum share of appreciation or equity in the property that the HESA originator may receive, or an explanation of other limits on the amount that the HESA originator may receive;
- any other amounts charged in connection with the HESA;
- settlement examples for the HESA after different specified time frames, and for each time frame, scenarios based on specified fluctuations in property value; and
- for each settlement example, the projected final value of the property, the share of equity that the HESA originator would receive, and an annual percentage rate equivalent based on the investment amount, the gross estimated cost of settlement, and the number of days from closing to settlement.

<u>Prohibited Acts</u>.
A HESA originator is prohibited from engaging in a variety of acts, including:
- charging penalties for early settlement of a HESA;
- preventing the homeowner from renting or using the property as the homeowner chooses;
- requiring the use of an appraisal or valuation report prepared or managed by an appraiser, appraisal management company, or other valuation services provider that is affiliated with the HESA originator, unless consented to by the homeowner;
- agreeing to a valuation that differs from the appraisal, unless fully disclosed and consented to by the homeowner;
- prohibiting the homeowner from refinancing a mortgage or lien on the property, provided that a HESA holder does not have to subordinate their lien;
- charging a settlement amount that exceeds the annualized cost limit of 25 percent; and
- taking any action in violation of unfair methods of competition and unfair or deceptive acts or practices under the Consumer Protection Act.

It is also a violation for a HESA originator to engage in fraud, deception, unfair practices, or misrepresentation, and to charge fees when no HESA is obtained, fail to provide disclosures or contract terms, make deceptive or false statements, pay appraisers with the purpose of influencing property values, violate state or federal law, and attempt to evade the regulations and requirements established.

Recordkeeping and Reporting Requirements.
Licensee's are required to keep all records that will enable the Director of the DFI to determine whether the licensee is in compliance. All records related to a HESA must be kept for at least three years. On or before March 1 of each year, each licensee must file a report with the DFI concerning the business and operations of each HESA originator's business conducted during the preceding calendar year. The report must be made under oath, and the DFI is responsible for publishing annually an analysis and recapitulation of the reports. A licensee who fails to file the required report is subject to a $50 penalty for each day's delay.

Penalties and Enforcement.
The DFI may impose fines of up to $100 per day, per violation or for failure to comply with any directive, order, or subpoena issued by the DFI. A person who violates, or knowingly aids or abets in a violation, or who fails to perform a required duty, for which no penalty is prescribed, is guilty of a gross misdemeanor.

In addition, a violation is considered an unfair and deceptive act or practice and an unfair method of competition in the conduct of trade or commerce under the Consumer Protection Act. Remedies provided under the Consumer Protection Act are considered cumulative and not exclusive.

Appropriation: None.

Fiscal Note: Available.

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