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MEMORANDUM

TO: Clients and Friends of the Firm

FROM: J. Alton Alsup

DATE: February 20, 2002

SUBJECT: Recent Amendments to the Home Ownership and Equity Protection Act of 1994 (HOEPA) and New Chapter 343, Texas Finance Code, to Combat Predatory Lending Practices

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Introduction — I know It when I see It

Attempts to define all that is embraced by the newly coined term “predatory lending” today is reminiscent of U.S. Supreme Court Justice Potter Stewart’s famous 1964 pronouncement when attempting to define obscenity: “I shall not attempt further to define the kinds of materials I understand to be embraced … [b]ut I know it when I see it.” Today, so-called predatory lending is the rallying cry for reform legislation in Congress and legislatures across the country by politicians and special interest groups to combat abusive lending practices by some unscrupulous mortgage lenders, mortgage brokers, and even home improvement contractors who are said to target vulnerable consumers, including the elderly, the financially troubled or unsophisticated, and residents of low income and minority neighborhoods. While no statute has yet defined the term, predatory lending according to the Department of Housing and Urban Development (HUD) at least is generally characterized by acts of intentional deception or fraud, by which borrowers are manipulated through aggressive and high-pressure sales tactics variously to pay excessive, and often hidden, fees and charges, called “packing,” to refinance their loans in successive transactions that generate fees for the lender or broker but for which no apparent benefit is realized by the borrower, called “flipping,” and to borrow sums that they are incapable of repaying and that often can only be repaid through the proceeds of foreclosure.

This memorandum examines two recent and significant developments in predatory lending regulations affecting Texas mortgage lenders and brokers: (1) Amendments by the Federal Reserve Board to § 226.32 of Regulation Z (Truth in Lending) effective December 20, 2001, implementing the Home Ownership and Equity Protection Act (HOEPA), which was enacted in 1994 to curb abusive lending practices in the home-equity market by regulating certain defined “high-rate, high-cost” loans, often referred to as “Section 32” loans or “HOEPA” loans; and (2) Texas’ own first-generation predatory lending legislation (S. B. 1581, Acts 2001), creating new Chapter 343, Texas Finance Code, effective September 1, 2001, which regulates lender practices in regard to home loans, low-rate home loans, and high-cost home loans, as those terms are defined by Chapter 343.

New Amendments to Federal HOEPA Loan Regulations

1. Overview of Original HOEPA Provisions. The Federal Reserve Board first amended Regulation Z on March 24, 1995, to implement provisions of the Home Ownership and Equity Protection Act of 1994 (HOEPA) [Pub. L. 103-325, 108 stat. 2160] regarding certain defined "high-Rate, high-Cost" loans bearing interest rates or fees above a certain percentage or amount. These regulations were set out principally as § 226.32 of Regulation Z, and covered loans have come to be generally known as "Section 32 loans." Section 32 covers any closed-end consumer credit transactions secured by the consumer's principal dwelling, other than a residential mortgage transaction (i.e., a mortgage loan to finance the acquisition or initial construction of a principal dwelling) or a reverse mortgage loan, if *either* (i) the annual percentage rate (APR) at consummation will exceed the yield on U.S. Treasury securities of comparable maturities by more than 10 percentage points; or (ii) the total points and fees payable by the consumer at or before closing will exceed the greater of 8% of the total loan amount or $400 (adjusted to $480 for 2002, based on CPI Index). 'Points and fees" for this purpose include not only charges labeled as point or fees and included in the prepaid finance charge by lenders but all compensation paid to mortgage brokers (except yield spread premiums paid P.O.C.), any third-party fees for which the lender receives any direct or indirect compensation, and fees paid to an affiliate of the lender. A lender making a Section 32 loan, in addition to other required Truth in Lending disclosures, must make a pre-closing disclosure not less than three (3) business days prior to settlement that contains (i) a conspicuous warning in language mandated by the regulations (to the effect that the consumer is not required to complete the loan merely because the consumer has signed the loan application; that, if the loan is obtained, the lender will have a mortgage on the consumer's home; and that the consumer could lose the home if the consumer fails to meet his or her obligations under the loan); (ii) the APR and the amount of the monthly payment; and (iii) if the loan is an ARM, a statement that the rate can increase after consummation and the amount of the maximum monthly payment based on the rate cap. Once this disclosure is given, the lender may make no change in any of the terms of the loan unless new pre-closing disclosures are provided under the same timing rules. If changes are requested by the consumer, however, new disclosures may be given by telephone as long as new written disclosures are then given at closing and acknowledged by the creditor and consumer as having been timely given by telephone at least three business days prior to consummation. A Section 32 loan also has certain substantive limitations regarding balloon payments, negative amortization, prepayment penalties, post-default interest increases, and prepaid payments. Generally, any assignee of a Section 32 loan is held to the same liability as the original creditor and the assignor of a Section 32 loan is required to place the assignee on notice that the loan is covered by these provisions by including a prominent notice of the potential liability of assignees. Section 32 disclosures are "material disclosures" for Truth in Lending purposes, and violations of required disclosures or prohibited terms subjects a creditor to liability to a consumer for each transaction for actual damages plus an amount equal to all finance charges and fees paid by the consumer and could have the effect in a given case of extending the consumer's right of rescission for an extended period of three years from the date of closing.

2. New Amendments to HOEPA Regulations. The Federal Reserve Board (FRB) has adopted amendments to provisions of Regulation Z (Truth in Lending) and its Official Staff Commentary that implement HOEPA to further address abusive lending practices in the home equity lending market. The Final Rule, which amends § 226.32 and adds a new § 226.34 to Regulation Z, was effective upon publication December 20, 2001, in the Federal Register [66 F.R. 65604], but mandatory compliance is deferred until October 1, 2002. The FRB acted under its delegated authority under HOEPA to adjust the APR trigger, add certain charges to the Points and Fees trigger, and to prohibit certain acts or practices with respect to HOEPA loans. The Final Rule is intended to address certain so-called predatory lending practices that the FRB believes have increased measurably with the significant growth of the so-called “subprime” market segment of consumers with impaired credit. Predatory lending practices, according to the FRB, have included one or more of the following:

- Making unaffordable loans based on the borrower’s home equity without regard to the borrower’s ability to repay the obligation;

- Inducing a borrower to refinance a loan repeatedly, even though the refinancing may not be in the borrower’s interest, and charging high points and fees each time the loan is refinanced, which decreases the consumer’s equity in the home; and

- Engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower — for example, “packing” loans with credit insurance without a consumer’s consent.

Adjustments made in the amended HOEPA regulations to the APR trigger and the points and fees trigger are expected to significantly expand the coverage of HOEPA regulations from an estimated 9-12% of home equity loans nationwide to 26%, or by some estimates 38%, of all such loans.

a. APR Trigger on First-Lien Loans Lowered to 8 Percentage Points Over Comparable Treasuries. HOEPA requirements will now apply to loans secured by the consumer’s principal dwelling if the annual percentage rate (APR) at loan closing will exceed the yield on U.S. Treasury securities of comparable periods of maturity (as of the 15th of the month immediately preceding the month in which the loan application is made) by more than 8 percentage points (formerly 10 percentage points). With this change, home equity loans for which application was made in December, 2001, for a term of 10 years would be subject to HOEPA if the APR is 13%, or higher. The APR trigger for second-lien loans remains unchanged at 10 percentage points over comparable Treasuries.

b. Points and Fees Re-defined to Include Optional Credit Life or Other Debt Cancellation Insurance Premiums. “Points and Fees” for purposes of determining HOEPA coverage generally include all finance charges payable by the borrower (except interest) , but also can include some charges that are not finance charges, such as otherwise excluded real estate transaction closing costs, when paid to the lender or an affiliate of the lender. If required as a condition of the loan, credit life and other debt cancellation products have always been a finance charge, but HOEPA regulations now will include in the points and fees calculations even optional or voluntary premiums or other charges for credit life, accident, health, or loss-of-income insurance, or debt cancellation coverage (whether or not considered insurance under applicable law) written in connection with the loan transaction that provides for cancellation of all or a portion of the borrower’s liability in the case of an accident or in the event, as applicable, of loss of life, health, or income. Inclusion of even optional credit insurance premiums in the points and fees test is intended to discourage the abusive practice of “insurance packing” in which purported optional insurance is automatically included in the loan amount without the borrower’s request, with the result some borrowers may be unaware of its inclusion and others may perceive it as a required condition of the loan.

c. HOEPA Disclosure Form Revised to Include Amount Borrowed and Regular Payments, Including any Balloon Payment. Section 226.32 requires that, in addition to all other Truth in Lending disclosures that must be given a consumer at or before loan closing, lenders making loans covered by HOEPA provide abbreviated written disclosures to borrowers at least three business days before the loan is closed setting out information described briefly in subsection 1 above. New §§ 226.32(c)(3) and (c)(5) now require that those written disclosures be set out *in conspicuous type size* and be enhanced with the following additional disclosures:

- **Total Amount Borrowed.** For a mortgage *refinancing*, the total amount the consumer will borrow, as reflected on the face of the note, and whether the total amount borrowed includes any premiums or other charges for optional credit life or other debt cancellation coverage. The total amount borrowed must be accurate within a tolerance of $100. Although this enhanced disclosure is required only if the covered transaction is a mortgage refinancing, lenders expressly are permitted to include the disclosure for all HOEPA loans.

- **Regular Payments, Including Balloon Payment.** For all HOEPA loans, the amount of the regular monthly (or other periodic) payment and the amount of any balloon payment must be disclosed. Lenders are permitted to include optional or voluntary items in the regular payment disclosure only if the borrower has previously agreed to purchase those items. The amount of the regular payment must be accurate, but is considered accurate if accurate based on a total loan amount that is accurate within a $100 tolerance and disclosed.

The following Model Form H-16 to Regulation Z adopted by the FRB illustrates the amended form containing these enhanced disclosures:

H-16 — Mortgage Sample

> **You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application.**
>
> **If you obtain this loan, the lender will have a mortgage on your home.**
>
> **YOU COULD LOSE YOUR HOME, AND ANY MONEY YOU HAVE PUT INTO IT, IF YOU DO NOT MEET YOUR OBLIGATIONS UNDER THE LOAN.**
>
> You are borrowing $ ______ (optional credit insurance is __ is not __ included in this amount).
>
> The annual percentage rate on your loan will be: ______%.
> Your regular [frequency] payment will be: $ ______.
> [At the end of your loan, you will still owe us: $ [balloon amount.]
>
> [Your interest rate may increase. Increases in the interest rate could increase your payment. The highest amount your payment could increase is to $ ______.]

d. “Due on Demand” Clauses Prohibited. Demand or call features that permit the lender to accelerate the loan and demand repayment of the entire outstanding loan amount in advance of the original maturity date are now prohibited under HOEPA regulations except in certain cases when acceleration of the loan is justified. This limitation is intended to prevent unscrupulous lenders from arbitrarily calling a loan due for the purpose of forcing the borrow to pay additional points and fees to refinance the loan under threat of foreclosure. Under new § 226.32(d)(8), a lender may demand repayment only in the following circumstances:

- **Fraud.** There is fraud or material misrepresentation by the consumer in connection with the loan;

- **Default in Repayment.** The consumer fails to meet the repayment terms of the agreement for any outstanding balance; or

- **Action Affecting Security Interest.** There is any action or inaction by the consumer that adversely affects the creditor's security for the loan, or any right of the creditor in such security.

e. Prohibited Acts Now Include Loan "Flipping", Extending Credit without Regard to Repayment Ability, and Disguised Open-End Credits. The FRB acting under its delegated authority under HOEPA to prohibit certain acts or practices affecting mortgage loans if it finds the act or practice unfair, deceptive, or designed to evade HOEPA has adopted a new § 226.34 setting out (in addition to prohibited acts formerly contained in § 226.32(e)) three new prohibitions:

1. **Refinancing within a One-Year Period.** Frequent refinancing of home loans motivated primarily to generate additional fee income even when the borrower derives no benefit from the refinancing, a practice that strips equity and is sometimes referred to as "flipping," is considered among the most flagrant of lender abuses. Under § 226.34(a)(3), a lender making mortgage loans subject to HOEPA may not, within one year of having made a HOEPA-covered loan, refinance the loan to the same borrower into another loan subject to HOEPA, *unless the refinancing is in the borrower's interest*. The lender in this circumstance is prohibited from refinancing the HOEPA loan during the one-year period (whether or not the lender still holds or services the loan) or another HOEPA loan it may hold to that same borrower. Furthermore, any assignee of a HOEPA loan (who may be the true creditor funding the loan) is subject to this limitation and may not refinance the loan within the one-year period. Even if not the true creditor, an assignee is subject to this refinancing restriction to ensure that loans are not transferred as a means of evading the restriction. Moreover, lenders are prohibited from evading this flipping limitation by engaging in a pattern or practice of arranging refinancings of the loans with affiliates or arranging refinancings of their own HOEPA loans with unaffiliated creditors.

2. **Extending Credit without Regard to Repayment Ability.** New § 226.34(a)(4) prohibits a lender from engaging in a pattern or practice of making loans subject to HOEPA without regard to the borrower's ability to repay the loan, considering the borrower's current and expected income, current obligations, and employment status. Although this new section is merely a clarification of existing law, it specifies that the lender must use independent sources to verify and document a borrower's repayment ability. Moreover, it establishes a presumption that a lender has violated this prohibition if engaging in a pattern and practice of making HOEPA loans without verifying and documenting the borrower's repayment ability. Proof of isolated or random acts is not sufficient to establish a *pattern or practice*, however, and what constitutes a pattern or practice in any case is an elusive fact question in which the "totality of the circumstances" must be considered.

3. **Disguising a High Cost Loan as an Open-End Credit to Evade HOEPA Prohibitions.** New § 226.34(b) prohibits a lender from attempting to evade HOEPA requirements, which apply only to closed-end credits, by structuring a mortgage loan otherwise subject to HOEPA as an open-end credit line if the loan as structured does not meet the Truth in Lending Act definition of an open-end credit set out in § 226.2(20). This prohibition is intended to curb practices of lenders' documenting high cost loans as open-end revolving credit lines when there is no real expectation of repeat transactions under a re-useable line of credit, which is an essential element of the definition of an open-end credit. Under this provision, such disguised open-end credit loans can be found on the facts to be subject to the rules for closed-end credits, including HOEPA if the APR or points and fees test is met.

New Chapter 343, Texas Finance Code

1. Predatory Lending Laws Come to Texas. Texas has joined a growing number of states, and even municipalities, that have passed or are considering tougher consumer protection laws to combat so-called "predatory lending" practices. Governor Rick Perry signed Texas S.B. 1581, Laws of 2001, on June 11, 2001, generally effective September 1, 2001, to marshal in Texas' own version of a first-generation predatory lending bill. The Act adds a new Chapter 343 to the Finance Code that defines and regulates "home loans," "low-rate home loans", and "high-cost home loans" in various respects. Generally, lenders are required to provide loan applicants new disclosures in connection with home loans when the interest rate is 12% or greater and when the lender offers single premium credit insurance. Refinancing or flipping of low-rate loans directly made by government or non-profit lenders within seven years is prohibited, unless at lower rates and costs. And high-cost home loans (defined to apply to home loans with a principal amount today not exceeding $150,350 that generally meet the federal HOEPA standards) restrict balloon payments, negative amortization, collateral-based lending, and prepayment penalties. Chapter 343 expressly does not apply to a reverse mortgage or to an open-end account defined by § 301.002, Texas Finance Code.

2. Certain Definitions. Inevitably, an understanding of key defined terms is necessary to analysis:

a. A **"home loan"** is a loan that is:

- Made to one of more individuals for personal, family, or household purposes and secured in whole or in part by a manufactured home used or to be used as the borrower's principal residence; or
- Real property improved by a dwelling designed for occupancy by one to four families and used or to be used as the borrower's principal residence.

b. A "**high-cost home loan**" means a loan that:

- Is made to one or more individuals for personal, family, or household purposes;
- Is secured in whole or part by a manufactured home, used or to be used as the borrower's principal residence; or real property improved by a dwelling designed for occupancy by one to four families and used or to be used as the borrower's principal residence;
- Has a principal amount equal to or less than one-half of the maximum conventional loan amount for first mortgages as established and adjusted by Fannie Mae;
- Is a credit transaction described by 12 C.F.R. Section 226.32, as amended, except that the term includes a residential mortgage transaction, as defined by 12 C.F.R. Section 226.2, as amended, if the total loan amount is $20,000 or more and the annual percentage rate (APR) exceeds the rate indicated in 12 C.F.R. Section 226.32(a)(1)(i), as amended; or the total points and fees payable by the consumer at or before loan closing will exceed the amount indicated in 12 C.F.R. Section 226.32(a)(1)(ii), as amended.

c. "**Points and fees**" has the meaning assigned by 12 C.F.R. § 226.32(b), as amended.

[**NOTE:** References to Section 226.32, as amended, should now include new § 226.34, Regulation Z, described in A.2. above.]

3. Regulation of Home Loans with a Rate of 12% or More. Mortgage lenders are now required to deliver a new, written disclosure to loan applicants for home loans with an interest rate of 12% or more per year to comply with new Chapter 343, Texas Finance Code. The disclosure requirements apply to any home loan application received on or after September 1, 2001. The Texas Finance Commission adopted 7 Tex. Admin. Code § 5.1 on August 17, 2001, to implement the notice requirements for these home loans. These regulations cover the means by which lenders may comply with the notice requirements of Section 343.102 of the Texas Finance Code, and describe the applicability of the notice requirements, the actual content requirements of the notice, the timing and delivery requirements of the notice, and related matters. Generally, the notice must be delivered when the lender makes the disclosure required under RESPA for the good faith estimate, or if RESPA does not apply, three business days after the date the application is made. The lender also must provide to the borrower (1) a statement regarding the value of mortgage counseling before taking out a home loan; (2) a list of the nearest available housing counseling agencies approved by the HUD; (3) a list of other resources where mortgage information can be found, including toll-free telephone numbers and online resources; and other disclosures required by the Finance Commission, including an official notice regarding high-cost home loans. Lenders who knowingly and willfully violate the home loan disclosure requirements are liable to the aggrieved borrower for actual damages caused by the violation plus punitive damages not to exceed $10,000 in an action brought by the aggrieved borrower and court costs. By statute, the requirement to provide the notice on covered loans sunsets and expires September 1, 2003, unless continued by the Finance Commission after reconsideration beginning in June, 2003.

a. Applicability of Regulations. The regulations apply to any mortgage loan application received on or after September 1, 2001, for any home loan that is: (i) a fixed rate loan that has a *contract interest rate* (not a composite rate, or APR) of 12% or greater a year; or (ii) an adjustable rate loan that:

- has a maximum fixed rate of interest pursuant to a schedule of steps or tiered rates that is 12% or greater a year; or

- has a maximum variable rate of interest that when calculated upon the index's value at the time of application, plus maximum margin increases may result in an interest rate of 12% or greater a year.

This amended language addresses adjustable rate mortgages in two ways:

- an adjustable rate mortgage that may not initially bear a rate of 12%, but through a series of rates or steps specifies a fixed rate of 12% later in a contract would require the notice; and

- a variable rate mortgage with a floating index that, when applying the maximum margin, increases to the fully indexed rate at the time of application of 12% or greater would also require the Notice.

[**NOTE:** The Office of the Consumer Credit Commissioner has confirmed that even if the ARM note rate is less than 12% but the actual index value at the time of application plus the margin stipulated in the note equals 12%, or more, the administrative rule and notice requirements apply.]

b. Notice Requirements. The form of the notice must be substantially similar to that provided by the Finance Commission, and it must appear on a full, separate page, with no other text than as provided in the regulation. The regulation states that the state seal conveys the importance of the official notice and that it must be included in the text box at the bottom of the required notice. The notice need not be acknowledged, and, therefore, there is no need for a subsection requiring retention of the authenticated acknowledgments. However, a lender may request that the applicant authenticate the notice acknowledging applicant's timely receipt of the notice. The Notice must be given in Spanish when the borrower and lender are conducting the transaction primarily in Spanish, and since the rule does not prohibit a lender from providing a Spanish notice in every transaction lenders may choose to implement a form of notice with English on one side and Spanish on the other. The regulation and the form of Important Notice to Home Loan Borrowers in both English and Spanish have been posted to the Website of the Office of the Consumer Credit Commissioner at http://www.occc.state.tx.us/.

c. Housing Counseling Agencies and Disclaimer. Subsection (c)(4) of the regulations requires that a lender provide a borrower with a list of HUD-approved housing counseling agencies located in Texas (currently over 100). The statute requires that a lender distribute a list of the "nearest" housing counseling agencies. Therefore, the Finance Commission is permitting lenders flexibility in this area by allowing a lender to provide the applicant with either (1) a list of the Texas-located housing counseling agencies approved by HUD; or (2) a list of at least five HUD-approved housing counseling agencies nearest the applicant's residence. The required list must contain housing counseling agency information that is not more than 90 days old or, if more than 90 days old, is the most recent information available from HUD. The Finance Commission has no objection to a lender's adding a disclaimer to the list of counselors, such as: "The lender is not affiliated with any of the housing counseling agencies whose names are provided to you with this notice. The lender is not responsible for information or advice given by a housing counseling agency from which you may seek advice."

[**NOTE:** A list of HUD-approved counselors can be found at http://www.hud.gov/fha/sfh/hcc/hccprof14.html. Select "Texas."]

d. Timing and Means of Delivery. Subsection (d) of the regulations provides that the delivery procedure parallels those for other types of notices in mortgage loans, such as the delivery of the Good Faith Estimate disclosure under RESPA. If RESPA does not apply, or if the lender has not yet determined whether the home loan is a high-cost home loan, delivery of the notice must be made within three business days after application and at least one business day prior to closing. In the event of multiple applicants, it is necessary for the lender to deliver the notice to only one of the applicants. If the application is denied before the time for delivery of the notice, the lender is not required to provide the notice. The regulation sets out provisions for mail and electronic delivery of the notice.

4. Regulation of High-cost Home Loans. The notice prescribed by the Finance Commission for home loans with an interest rate of 12%, or more, also contains a required official notice regarding "high cost home loans, which reads as follows:

> OFFICIAL STATE OF TEXAS NOTICE
> **REGARDING HIGH COST HOME LOANS**
>
> **[STATE SEAL]**
>
> The loan you applied for <u>may</u> be a "high-cost home loan" as defined by state and federal law. Look at everything you earn and everything you owe and then ask yourself if you can afford to make the payments when due.
>
> **If you can't afford this loan, you may lose your home.**

It is important to note that a home loan with an interest rate of 12%, or more, may not be a high cost home loan. A loan with an interest rate of 12%, or more, would constitute a *high cost home loan* only if it meets both the loan size test under § 343.201(1)(c) (i.e., principal loan amount of less than $150,350, or if a purchase or initial construction loan transaction, between $20,000 and $150,350) and either the Annual Percentage Rate (APR) test or the points and fees test of a Section 32 or HOEPA loan set out in Regulation Z at 12 C.F.R. § 226.34 and discussed in B.2. of this section above. As of January 15, 2002, a home loan would be required to have an APR exceeding 13% to meet the definition of a high-cost home loan and to be subject to the notice and further regulations of Section 343.201-205 of the Texas Finance Code. Under the provisions of a related bill, S.B. 272, Acts of 2001, the Consumer Credit Commissioner is required to establish a program to address alternatives to high-cost lending in Texas. The program will, among other matters, study and report on the problem of high-cost lending not later than December 1 of each year.

[NOTE: Under APR trigger adjustments adopted by the Federal Reserve Board December 20, 2001, the APR trigger set out in § 226.32(a)(1)(i) has been reduced from 10 percentage points to 8 percentage points over U.S. Treasury securities of comparable maturities, reducing the APR trigger as of January 15 to rates exceeding only approximately 13%.]

Certain terms and practices are restricted for loans meeting the definition of a high cost home loan in Texas:

- **Balloon payments.** A *high cost* home loan may not provide for a scheduled payment that is more than twice as large as the average of earlier scheduled monthly payments, *unless* the balloon payment becomes due not less than 60 months after the date of the loan. This prohibition does not apply if the payment schedule is adjusted to account for seasonal or otherwise irregular income of the borrower or if the loan is a bridge loan in connection with the acquisition or construction of a dwelling intended to become the borrower's principal dwelling. A "bridge loan" means temporary or short-term financing requiring payment of only interest until the entire unpaid balance is due.

- **Negative amortization.** A high cost home loan may not provide for a payment schedule with regular periodic payments that cause the principal balance to increase, *except* when such negative amortization results as a consequence of a temporary forbearance, bridge loan, or restructure sought by the borrower. A "restructure" means a change in the payment schedule or other terms of a home loan as a result of the borrower's default.

- **Disregard for Inability to Repay.** A lender may not engage in a pattern or practice of extending credit to consumers under high-cost home loans based solely upon the value of the collateral without regard for the borrower's ability to pay, considering the borrower's and other obligor's (including co-signers and guarantors) income, current obligations, employment status, and other financial resources other than equity in the home securing the loan.

- **Prepayment Penalty**. A high cost home loan may not provide for a prepayment penalty. The Texas Finance Code, Section 301.002 defines "Prepayment Penalty" in its traditionally understood terms to mean consideration agreed on and contracted for a discharge of a loan … before its maturity or its regularly scheduled date of payment, as a result of an obligor's election to pay all of the principal amount before its stated maturity or a regularly scheduled date of payment.

5. Regulation of Low-cost Home Loans. A "low-rate home loan" is a home loan that at its inception carries an interest rate two percentage points or more below the yield on treasury securities having comparable periods of maturity to the loan maturity, *except* that if the loan's interest rate is a discounted introductory rate or a rate that automatically steps up over time, the fully indexed rate or the fully stepped-up rate, as appropriate, must be used instead of the rate at the loan's inception to determine whether the loan is a low-rate loan. A lender may not refinance, replace or consolidate a low-rate home loan directly made by a *government or non-profit lender* before the 7th anniversary of the date of the loan *unless* the new or consolidated loan has a lower interest rate and requires payment of a lesser amount of points and fees than the original loan or is a restructure to avoid foreclosure.