



Friday, January 8, 2010

ACORN Home Equity Law Suit

On Friday January 8, 2010 the Third Court of Appeals in Austin reached an opinion in the four year old appeal of the suit by the Association of Community Organizations for Reform Now (ACORN) which challenged the Finance Commission's regulations for home equity loans in Texas.

Good News

With the exception of the regulations defining "interest," all the challenged regulations were supported by the court's decision. So it's business as usual for the use of POAs, mailing the 12 Day Notice, and issuing convenience checks for HELOCS, etc.

(not so) Bad News

The court affirmed the invalidation of the Finance Commission's definition of "interest." The importance of this definition relates to the constitutional 3% limit on fees and charges for home equity loans. Interest is excluded from the 3% calculation. The definition of interest adopted by the Finance Commission was the definition of interest that came out of Texas usury statutes and cases. That definition of interest is *extremely broad*. For example, it would include origination fees, processing fees, administration fees, etc. The Court rightly threw out that definition and all related references to interest in the regulations.

Net Effect

There is no regulatory definition of interest for home equity loans. That's it. We are back to the definition of interest used before the regulations came out.

Whether discount points are considered interest is a big issue. Before the regulations, there was case law concluding that *bona fide* discount points (actually charged to lower the interest rate on the loan) were interest and not included in the 3% calculation. Even ACORN in its brief to the Court acknowledged that true discount points are interest. **The recent ACORN decision did not say that lenders can no longer exclude discount points from the 3% fee calculation.** Hopefully, the Finance Commission will soon draft a replacement definition of interest that includes points so that lenders will not need to rely on older case law for the exclusion of discount points from the 3% calculation.

Suggested Actions

1. Check with your investors to make sure they are reacting correctly to this recent decision.
2. Only exclude discount points that were charged in exchange for a lower interest rate.
3. Have borrower(s) acknowledge in writing the specific exchange of points for lower rate.