Approved February 7, 1983
Date

MINUTES OF THE House COMMITTEE ON Commercial & Financial Institutions.

The meeting was called to order by Representative David Miller at
Chairperson

3:30 a.m./p.m. on February 3, 1983 in room 527-S of the Capitol.

All members were present except:

Representative Dyck, Holderman, King, and Sand.

Committee staff present:

Bill Wolff, Research Department
Bruce Kinzie, Revisor of Statutes' Office
Martha Evans, Committee Secretary

Conferees appearing before the committee:

Jim Maag, Kansas Bankers Association
Tom Wilder, Kansas Saving & Loan League
Marvin Umholtz, Kansas Credit Union League

House Bill 2071 - Relating to types of adjustable loans; concerning types thereof; amending K.S.A. 1982 Supp. 16-207d and repealing the existing section.

Vice Chairman Miller announced that the hearings on HB 2079, canceled on Tuesday because of snow, would now be held on Monday, February 7, at 3:30. He then turned the Committee's attention to HB 2071 and HB 2072 which were on the day's agenda for hearings.

Vice Chairman Miller introduced Jim Maag of K.B.A. who had requested the bill. Mr. Maag distributed written testimony (Attachment 1) to the Committee and asked that HB 2071 be recommended favorable for passage in order to clarify the ambiguity in the existing law. Directing attention to the last sheet of his testimony, he stated that Section 2 required adoption of rules and regulations primarily for adjustable second mortgage loans and the index for adjustable loans. He said that when SB 559 was amended to include this section last year, he could recall no discussion of including commercial and agricultural loans in the rules and regulations of the financial institutions. The intent appeared to be that it apply only to adjustable loans for personal, family, or household purposes. He further noted that if bank examiners would interpret it to include commercial and agricultural loans, it would add additional restrictions on state-chartered banks that nationally-chartered banks would not have.

Representative Eckert inquired if the word "primarily" was of any significance in the bill. Mr. Maag responded that it was lifted from the U.C.C.C. and was of no special significance. Representative Eckert then asked what was the purpose of excluding commercial and agricultural loans to which Mr. Maag answered that commercial and agricultural loans have no ceilings while mortgages do have. Representative Miller inquired if rates on first mortgage real estate were controlled elsewhere and he was told that they were included in Section 2 of SB 559 which was a new section in the Statute Book.

Mr. Tom Wilder, representing the Savings & Loan League, was recognized and he advised the Committee that the Saving & Loans support HB 2071. He said that they felt the intention of the Legislature was not to include commercial and agricultural loans but felt it should be cleared up.

Marvin Umholtz of the Credit Union League passed around testimony (Attchmt 2) and, after supporting the bill, suggested amending "shall" to "may". Rep. Shelor inquired if the regulations would still be joint and Mr. Umholtz responded that they would be. Rep. Jarchow then asked if the new wording would present any problems to the K.B.A.; Mr. Maag said that he didn't think it would. Bill Wolff suggested that "may" is a permissive word and would allow three different sets of rules and regulations to three different financial institutions (i.e. they may jointly adopt; or separately adopt; or not adopt at all). Rep. Ott asked that if "shall" were retained could the Credit Unions support the bill. Mr. Umholtz said that the point was a minor one, and replied in the affirmative.

MINUTES OF THE House COMMITTEE ON Commercial & Financial Institutions,

room 527-S, Statehouse, at 3:30 ~~a.m.~~/p.m. on February 3, 1983.

House Bill 2072 - An act relating to credit cards; amending K.S.A. 16-842 and repealing the existing section.

Jim Maag of the KBA, which proposed the bill, addressed the Committee and distributed written testimony (Attachment 3). He said the bill referred to bank credit cards (Master Card and Visa Card) and not to debit cards (Zip Card). He said not all banks issue these; that there are less than ten in Kansas. He advised the Committee that the bill would accomplish two things; (1) clear up confusion between the state and federally chartered banks and (2) save money. He said that the largest credit card extender, the Fourth National Bank in Wichita issued about 75,000 annually and the smallest issuer, Commerce Bank in Topeka, issued between 10,000 and 15,000. He testified that approximately 99% of losses are reported by telephone which is more convenient and reduces the consumer's liability.

Representative Shelor asked if there was an 800 number. Mr. Maag said there was and that information on how to report a loss and that number accompany the issuance and re-issuance of credit cards, and most often the information is on the reverse side of the monthly statement. Representative Miller asked if this would apply only to bank credit cards or would it also apply to oil credit cards. Mr. Maag answered that he thought it applied only to bank credit cards but was not entirely certain. Representative Miller requested him to advise the Committee on this at the next meeting. Representative Ott inquired if this bill was introduced last year; Mr. Maag responded that the KBA had not requested it; Dr. Wolff said that he thought it was incorporated into another bill last year.

Vice Chairman Miller announced that the next meeting would be on Monday, February 7, at 3:30. He said that they would discuss the two bills just heard (HB 2071 and HB 2072) and possibly take action on them. Also, he reminded the Committee that HB 2079 would be heard at that meeting. He said to make a note that the Thursday meeting might have to be changed to Wednesday but they would be further advised on this at the Monday Meeting.

The minutes were approved on a motion by Representative Ott, seconded by Representative Nichols, and voted favorably by the Committee.

The meeting was adjourned at 4:10 p.m.

The KANSAS BANKERS ASSOCIATION
A Full Service Banking Association

February 3, 1983

TO: House Committee on Commercial and Financial Institutions

RE: HB 2071

Mr. Chairman and members of the Committee:

We appreciate very much the opportunity to appear before the Committee in support of HB 2071. The bill amends K.S.A. 16-207d to clarify that the rules and regulations to be promulgated by the state bank commissioner, the consumer credit commissioner, the savings and loan commissioner, and the credit union administrator shall apply only to adjustable rate loans "made primarily for personal, family, or household purposes" and would not apply to commercial or agricultural loans as defined by K.S.A. 16-207(f).

It is our belief that when SB 559 of the 1982 session was amended to include Section 2 (which is now 16-207(d) of the Kansas Statutes Annotated) those regulations to be issed were to apply only to adjustable rate loans for personal, family or household purposes and not to any adjustable rate commercial or agricultural loans and did not, at that time, place any further restrictions on the making of such loans. To our knowledge there was no discussion at the time that Section 2 was added to SB 559 during the 1982 session that agricultural and commercial loans should be included in any rules and regulations put forth by these various state commissioners for financial institutions. Therefore, to clarify any ambiguity in the existing law, we would respectfully request that the language contained in HB 2071 be added to K.S.A. 16-207(d).

It should be further noted that unless such an amendment is forthcoming and bank examiners interpret 16-207(d) to mean that all commercial and agricultural loans must adhere to the rules and regulations as set forth in 104-1-1 it would create a situation where state-chartered banks would have additional restrictions on the making of commercial and agricultural loans that nationally-chartered banks would not. In addition, it would place restrictions on agricultural and commercial loans which would not apply to any corporate loan.

We strongly believe that there should be a continuing movement towards uniformity in the powers and authority of both state and nationally chartered banks. The continued existence of K.S.A. 16-207(d) in its present form would be a movement in the opposite direction.

Again, we want to thank the Committee for the opportunity to appear on this legislation and we respectfully request that you recommend HB 2071 favorably for passage.

James S. Maag
Director of Research

Attachment 1
House C & F I 2/3/83

Office of Executive Vice President • 707 Merchants National Building
Eighth and Jackson • Topeka, Kansas 66612 • (913) 232-3444

State of Kansas

CONSUMER CREDIT COMMISSIONER
STATE DEPARTMENT OF CREDIT UNIONS
SAVINGS AND LOAN DEPARTMENT
STATE BANK COMMISSIONER

NOTICE OF PUBLIC HEARING ON JOINT PROPOSED ADMINISTRATIVE REGULATIONS

You are hereby notified that a public hearing will be held at 10:30 a.m. on August 11, 1982, in Room 313-S, Capitol Building, Topeka, Kansas on temporary and permanent regulation 104-1-1. All interested parties may present oral comments at the hearing. Written comments may be sent to any of the following state agencies:

Consumer Credit Commissioner 535 Kansas Avenue, Suite 1114 Topeka, Kansas 66603	Department of Credit Unions 535 Kansas Avenue, Suite 1008 Topeka, Kansas 66603
Bank Commissioner 818 Kansas Avenue Topeka, Kansas 66612	Savings and Loan Department 503 Kansas Avenue, Room 220 Topeka, Kansas 66603

The regulation to be adopted is as follows:

104-1-1. Adjustable rate notes secured by a real estate mortgage or a contract for deed to real estate. For the purpose of adjusting the interest rate, the lender may use any interest-rate index that is readily verifiable by the borrower and is beyond the control of the lender. Adjustments to the interest rate of an adjustable mortgage loan shall correspond directly to the movement of the index, subject to any rate-adjustment limitations that a lender may provide. The initial index value shall be the most recently available value of the index at, or within six months prior to, the closing date of the loan. The amount of a rate adjustment shall reflect the difference between the initial index value and either: (a) the index value most recently available as of the date of rate adjustment, if the payment is not simultaneously adjusted, or (b) the index value most recently available as of the date of notification of a payment adjustment. When the movement of the index permits an interest-rate increase, the lender may decline to increase the interest rate by the indicated amount. The lender may decrease the interest rate at any time.

Adjustments to the interest rate may be implemented through adjustments to the outstanding principal loan balance or the loan term, through changes in the payment amount, or both. Adjustments shall be subject to the following conditions: (a) the total loan term shall not exceed 40 years; (b) the adjustments shall reflect the movement of the index; (c) the initial payment amount shall be sufficient to fully amortize the loan at the beginning of the loan term; and (d) the payment amount shall be adjusted at least every five years to a level sufficient to amortize the loan at the then-existing interest rate and principal loan balance over the remaining term of the loan.

The borrower shall not be charged any costs or fees in connection with regularly-scheduled adjustments to the interest rate, the payment, the outstanding principal loan balance, or the loan term.

At least 30, but not more than 45 days, before adjustment of the payment, a lender shall send written notification to the borrower containing the following information:

(a) a statement that the payment on the loan with the lender, secured by a mortgage or deed of trust on property located at the named address, is scheduled to be adjusted on a particular date;

(b) the outstanding balance of the loan on the adjustment date, assuming timely payment of the remaining payments due by that date;

(c) the interest rate on the loan as of the adjustment date, the index value on which that rate is based, the period of time for which that interest rate will be in effect, the next payment adjustment date, and the rate adjustment dates, if any, between the upcoming payment adjustment date and the next payment adjustment date;

(d) the payment amount as of the payment adjustment date;

(e) the dates, if any, on which the rate was adjusted since the last payment adjustment, the rates on each such rate adjustment date, and the index values corresponding to each such date;

(f) the dates, if any, on which the outstanding principal loan balance was adjusted since the last payment adjustment, and the net change in the outstanding principal loan balance since the last payment adjustment;

(g) the fact that the borrower may pay off the entire loan or a part of it without penalty when the prepayment is made more than six months after execution of the note; and

(h) the title and telephone number of a lender employee who can answer questions about the notice.

An applicant shall be given, at the time of receipt of an application, or upon request, a disclosure notice in substantially the following form:

IMPORTANT INFORMATION ABOUT THE ADJUSTABLE MORTGAGE LOAN
PLEASE READ CAREFULLY

You have received an application form for an adjustable mortgage loan ("AML"). The AML may differ from other mortgages with which you are familiar.

GENERAL DESCRIPTION OF ADJUSTABLE MORTGAGE LOAN

The adjustable mortgage loan is a flexible loan instrument. Its interest rate may be adjusted by the lender from time to time. Such adjustments will result in increases or decreases in your payment amount, in the outstanding principal loan balance, in the loan term, or in all three (see discussion below relating to these types of adjustments). Regulations place no limit on the amount by which the interest rate may be adjusted at any one time or over the life of the loan, or on the frequency with which it may be adjusted. Adjustments to the interest rate must reflect the movement of a single, specified index (see discussion below). For this reason, if you desire to have certain rate-adjustment limitations placed in your loan agreement, you should negotiate that matter with the lender. You may also want to make inquiries concerning the loan terms offered by other lenders on AMLs to compare the terms and conditions.

Another flexible feature of the AML is that the regular payment amount may be increased or decreased by the lender from time to time to reflect changes in the interest rate. Again, regulations place no limitations on the amount by which the lender may adjust payments at any one time, or on the frequency of payment adjustments. If you wish to have particular provisions in your loan agreement regarding adjustments to the payment amount, you should negotiate those terms with the lender.

A third flexible feature of the AML is that the outstanding principal loan balance (the total amount you owe) may be increased or decreased from time to time when adjustments to the interest rate result in a payment amount that is too small to cover interest due on the loan, or a payment amount that is larger than necessary to pay off the loan over the remaining term of the loan.

The final flexible feature of the AML is that the loan term may be lengthened or shortened from time to time, corresponding to an increase or decrease in the interest rate. When the term is extended in connection with a rate increase, the payment amount does not have to be increased to the same extent as if the term had not been lengthened. In no case may the total term of the loan exceed 40 years.

The combination of these four basic features allows a lender to offer a variety of mortgage loans. For example, one type of loan could permit rate adjustments with corresponding changes in the payment amount. Alternatively, a loan could permit rate adjustments to occur more frequently than payment adjustments, limit the amount by which the payment could be adjusted, and/or provide for corresponding adjustments to the principal loan balance.

INDEX

Adjustments to the interest rate of an AML must correspond directly to the movement of an index, subject to any rate-adjustment limitations that may be contained in the loan contract. If the index has moved down, the lender must reduce the interest rate by at least the decrease in the index. If the index has moved up, the lender has the right to increase the interest rate by that amount. Although increasing the interest rate is optional for the lender, you should be aware that the lender has this right and that the lender may become contractually obligated to exercise it.

The following is important information about the index to be applied to your AML.

1. *Name and description of index to be used for applicant's loan:*
   (provide relevent information here)
2. *The initial index value (if known) or date of initial index value:*
   (provide relevant information here)
3. *A source or sources where the index may be readily obtained by the borrower:*
   (provide relevant information here)
4. *The high and low index rates during the previous calendar year:*
   (provide relevant information here)

KEY TERMS OF ADJUSTABLE MORTGAGE LOAN

Following is a summary of the basic terms on the type of AML to be offered to you. This summary is intended for reference purposes only. The following important information relating specifically to your loan will be contained in the loan agreement.

1. *The loan term:*
   (provide relevant information here)
2. *The frequency of rate changes:*
   (provide relevant information here)
3. *The frequency of payment changes:*
   (provide relevant information here)
4. *The maximum rate change, if any, at one time:*
   (provide relevant information here)
5. *The maximum rate change, if any, over the life of the loan:*
   (provide relevant information here)
6. *The maximum payment change, if any, at one time:*
   (provide relevant information here)
7. *The minimum increments, if any, of rate changes:*
   (provide relevant information here).
8. *The adjustments to the principal loan balance:*
   (provide relevant information here)

HOW YOUR ADJUSTABLE MORTGAGE LOAN WOULD WORK

INITIAL INTEREST RATE

The initial interest rate offered by (lender's name) on your AML will be established and disclosed to you on (commitment date) based on market conditions at the time.

A short description of each key term of the AML offered to you follows (headings identify the key terms).
(provide relevant information here)

NOTICE OF PAYMENT ADJUSTMENTS

(Lender's name) will send you notice of an adjustment to the payment amount at least 30 but not more than 45 days before it becomes effective. The following is a description of information contained in the notice, as required by K.A.R. _____:
(provide relevant information here)

PREPAYMENT PENALTY

You may prepay an AML in whole or part without penalty when the prepayment is made more than six months after execution of such note.

FEES

You will be charged fees by (lender's name) and by other persons in connection with the origination of your AML. The lender will give you an estimate of these fees after receiving your loan application. However, you will not be charged any costs or fees in connection with any regularly-scheduled adjustment to the interest rate, the payment, the outstanding principal loan balance, or the loan terms initiated by the lender.

(6) Notwithstanding subsections (1) and (2), a lender may contract for and receive a minimum finance charge of not more than $5 when the amount financed does not exceed $75, or not more than $7.50 when the amount financed exceeds $75.

(7) This section shall not apply to a loan secured by an interest in land the interest rate of which is governed by subsection (b) of K.S.A. 16-207, unless made subject hereto by agreement.

(8) This section shall not apply to a loan secured by an interest in land subordinate to a prior mortgage and held by a lender other than the lender of the first mortgage, the interest rate of which is governed by subsection (b) or (h) of K.S.A. 16-207, and any amendments thereto, unless made subject hereto by agreement.

~~(8)~~ *(9)* As an alternative to the rates set forth in subsection (1) and subsection (2)(d), during the period beginning on the effective date of this act and ending July 1, 1982, a supervised financial organization may contract for and receive a finance charge not exceeding 18% per year on the unpaid balance of the amount financed.

New Sec. 2. The state bank commissioner, consumer credit commissioner, savings and loan commissioner and credit union administrator shall jointly adopt rules and regulations for the purpose of governing loans made under the provisions of subsection (h) of K.S.A. 16-207, and any amendments thereto, and subsection (8) of K.S.A. 16a-2-401, and any amendments thereto. Such rules and regulations shall be published in only one place in the Kansas administrative regulations as directed by the state rules and regulations board.

Sec. 3. K.S.A. 16a-2-401 is hereby repealed.

Sec. 4. This act shall take effect and be in force from and after its publication in the statute book.

Approved May 10, 1982.

CHAPTER 95

Senate Bill No. 538

AN ACT amending the consumer credit code; concerning consumer credit insurance; amending K.S.A. 16a-4-103 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 16a-4-103 is hereby amended to read as follows: 16a-4-103. In this act "consumer credit insurance" means insurance, other than insurance on property, by which the satisfaction of debt in whole or in part is a benefit provided, but does not include:

Testimony of the

Kansas Credit Union League

on HB 2071, AML Regulation Clarifier

presented to the

House Commercial and Financial Institutions Committee

February 3, 1983

by Marvin C. Umholtz
Governmental Affairs Director

Mr. Chairman, Members of the Committee:

Thank you for the opportunity to appear before this Committee to provide comments on HB 2071 and the issues it raises.

We support the clarifying change recommended by the Kansas Bankers Association (KBA) in HB 2071. The amendment clarifies that K.A.R. 104-1-1 applies only to loans made primarily for personal, family or household purposes, and not business or agricultural purpose loans. Additionally, we would encourage the Committee to strike the word "shall" on line 0024 of HB 2071 and insert inlieu thereof the word "may."

Key to our association's consideration of this topic is our established policy position, which reads:

> Credit unions support obtaining and maintaining state and federal laws and regulations which are conducive to full participation by credit unions in all fields of lending.

KCUL can only support alternative mortgage transaction laws and regulations which allow the greatest ability of each credit union to tailor a lending program to serve its members. The amendments to HB 2071

on lines 0025 - 0026 would assist in alleviating any financial community concerns as to whether the state adjustable mortgage loan (AML) regulations do or do not apply to adjustable business or agricultural loans backed by real estate. With the amendment, they clearly would not.

KCUL considers the passage of HB 2071 as one legitimate approach that the legislature may take under the circumstances created by the passage of Title VIII of the Depository Institutions Act of 1982. We can support this option and certainly do not oppose it. If K.S.A. 1982 Supp. 16-207d is amended as indicated, the AML regulations promulgated by the National Credit Union Administration (NCUA) would be applicable for both state and federally chartered credit unions.

Section 804 of the DIA appears to be permissive. It reads, "... housing creditors may make, purchase and enforce alternative mortgage transactions..." (AMT). It is our view that a state chartered credit union could choose to make an AMT under either Title VIII (NCUA regulations) or K.A.R. 104-1-1, the state regulation.

KCUL also supports the passage of SB 50, currently under consideration by the Senate Commercial and Financial Institutions Committee. The measure repeals K.S.A. 1982 Supp. 16-207d. State chartered CU's would then clearly be subject to the NCUA regulations.

At this time, we would oppose any effort to override the use of the federal AMT regulations as is permitted by Section 805 of the DIA. Enough confusion still surrounds the interpretation of Title VIII to preclude hasty action in this area. We could only support an override of

the use of the federal regulations if the state regulators were statutorily directed to promulgate regulations no more restrictive than those provided by the respective federal regulators.

I have included the following attachments:

1. Title VIII of the Depository Institutions Act of 1982
2. Federal Register, Vol. 47, No. 233 12-3-82 reflecting the actions of the NCUA Board at its December 16, 1982 meeting.
3. NCUA Regulations 12 C.F.R. Sec. 701.21-6B and Sec. 701.21-2 (prior to the amendments made by the NCUA Board at its December meeting).

Under the NCUA regulations as amended in December, a credit union can make AMT's for:

- first and second mortgages for residential purposes, including manufactured housing (one to four family dwelling, residance of the borrower)
- 30 - 40 year maturities on first mortgages (includes refinancing)
- 15 year maturities on seconds
- no sales price restrictions
- provides for growth equity mortgages (GEM) (GEM is a mortgage that provides for accelerated repayment of the loan, either as a result of scheduled increases of payment of principal and interest or as a result of movements in an index)
- adjustable rate index must be by an index or an average of an index agreed upon in advance and must be beyond the control of the credit union and readily verifiable by the borrower.

Thank you for the opportunity to address the Committee. I stand ready to address questions at the direction of the Chairman.

GARN-ST GERMAIN DEPOSITORY INSTITUTIONS ACT OF 1982

PL 97-320

SEPTEMBER 30 (legislative day, September 8), 1982.—Ordered to be printed

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Mr. GARN, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany H.R. 6267]

TITLE VIII—ALTERNATIVE MORTGAGE TRANSACTIONS

SHORT TITLE

SEC. 801. This title may be cited as the "Alternative Mortgage Transaction Parity Act of 1982".

FINDINGS AND PURPOSE

SEC. 802. (a) The Congress hereby finds that—

(1) increasingly volatile and dynamic changes in interest rates have seriously impared the ability of housing creditors to provide consumers with fixed-term, fixed-rate credit secured by interests in real property, cooperative housing, manufactured homes, and other dwellings;

(2) alternative mortgage transactions are essential to the provision of an adequate supply of credit secured by residential property necessary to meet the demand expected during the 1980's; and

(3) the Comptroller of the Currency, the National Credit Union Administration, and the Federal Home Loan Bank Board have recognized the importance of alternative mortgage transactions and have adopted regulations authorizing federally chartered depository institutions to engage in alternative mortgage financing.

(b) It is the purpose of this title to eliminate the discriminatory impact that those regulations have upon nonfederally chartered housing creditors and provide them with parity with federally chartered institutions by authorizing all housing creditors to make, purchase, and enforce alternative mortgage transactions so long as the transactions are in conformity with the regulations issued by the Federal agencies.

DEFINITIONS

SEC. 803. As used in this title—

(1) the term "alternative mortgage transaction" means a loan or credit sale secured by an interest in residential real property, a dwelling, all stock allocated to a dwelling unit in a residential cooperative housing corporation, or a residential manufactured home (as that term is defined in section 603(6) of the National Manufactured Home Construction and Safety Standards Act of 1974)—

(A) in which the interest rate finance charge may be adjusted or renegotiated;

(B) involving a fixed-rate, but which implicitly permits rate adjustments by having the debt mature at the end of an interval shorter than the term of the amortization schedule; or

(C) involving any similar type of rate, method of determining return, term, repayment, or other variation not common to traditional fixed-rate, fixed-term transactions, including without limitation, transactions that involve the sharing of equity or appreciation;

described and defined by applicable regulation; and

(2) the term "housing creditor" means—

(A) a depository institution, as defined in section 501(a)(2) of the Depository Institutions Deregulation and Monetary Control Act of 1980;

(B) a lender approved by the Secretary of Housing and Urban Development for participation in any mortgage insurance program under the National Housing Act;

(C) any person who regularly takes loans, credit sales, or advances secured by interests in properties referred to in paragraph (1); or

(D) any transferee of any of them.

A person is not a "housing creditor" with respect to a specific alternative mortgage transaction if, except for this title, in order to enter into that transaction, the person would be required to comply with licensing requirements imposed under State law, unless such person is licensed under applicable State law, and such person remains, or becomes, subject to the applicable regulatory requirements and enforcement mechanisms provided by State law.

ALTERNATIVE MORTGAGE AUTHORITY

SEC. 804. (a) In order to prevent discrimination against State-chartered depository institutions, and other nonfederally chartered housing creditors, with respect to making, purchasing, and enforcing alternative mortgage transactions, housing creditors may make, purchase, and enforce alternative mortgage transactions, except that this section shall apply—

(1) with respect to banks, only to transactions made in accordance with regulations governing alternative mortgage transactions as issued by the Comptroller of the Currency for national banks, to the extent that such regulations are authorized by rulemaking authority granted to the Comptroller of the Curren-

cy with regard to national banks under laws other than this section;

(2) with respect to credit unions, only to transactions made in accordance with regulations governing alternative mortgage transactions as issued by the National Credit Union Administration Board for Federal credit unions, to the extent that such regulations are authorized by rulemaking authority granted to the National Credit Union Administration with regard to Federal credit unions under laws other than this section; and

(3) with respect to all other housing creditors, including without limitation, savings and loan associations, mutual savings banks, and savings banks, only to transactions made in accordance with regulations governing alternative mortgage transactions as issued by the Federal Home Loan Bank Board for federally chartered savings and loan associations, to the extent that such regulations are authorized by rulemaking authority granted to the Federal Home Loan Bank Board with regard to federally chartered savings and loan associations under laws other than this section.

(b) For the purpose of determining the applicability of this section, an alternative mortgage transaction shall be deemed to be made in accordance with the applicable regulation notwithstanding the housing creditor's failure to comply with the regulation, if—

(1) the transaction is in substantial compliance with the regulation; and

(2) within sixty days of discovering any error, the housing creditor corrects such error, including making appropriate adjustments, if any, to the account.

(c) An alternative mortgage transaction may be made by a housing creditor in accordance with this section, notwithstanding any State constitution, law, or regulation.

APPLICABILITY

SEC. 805. (a) The provisions of section 804 shall not apply to any alternative mortgage transaction in any State made on or after the effective date (if such effective date occurs on or after the effective date of this title and prior to a date three years after the effective date of this title) of a State law or a certification that the voters of such State have voted in favor of any provision, constitutional or otherwise, which states explicitly and by its terms that such State does not want the preemption provided in section 804 to apply with respect to alternative mortgage transactions subject to the laws of such State, except that section 804 shall continue to apply to—

(1) any alternative mortgage transaction undertaken on or after such date pursuant to an agreement to undertake such alternative mortgage transaction which was entered into on or after the effective date of this title and prior to such later date (the "preemption period"); and

(2) any renewal, extension, refinancing, or other modification of an alternative mortgage transaction that was entered into during the preemption period.

(b) An alternative mortgage transaction shall be deemed to have been undertaken during the preemption period to which this section applies if it—

(1) is funded or extended in whole or in part during the preemption period, regardless of whether pursuant to a commitment or other agreement therefor made prior to that period; or

(2) is a renewal, extension, refinancing, or other modification of an alternative mortgage transaction entered into before the preemption period and such renewal, extension, or other modification is made during such period with the written consent of any person obligated to repay such credit.

RELATION TO OTHER LAW

SEC. 806. Section 501(c)(1) of the Depository Institutions Deregulation and Monetary Control Act of 1980 shall not apply to transactions which are subject to this title.

EFFECTIVE DATE

SEC. 807. (a) This title shall be effective upon enactment.

(b) Within sixty days of the enactment of this title, the Comptroller of the Currency, the National Credit Union Administration, and the Federal Home Loan Bank Board shall identify, describe, and publish those portions or provisions of their respective regulations that are inappropriate for (and thus inapplicable to), or that need to be conformed for the use of, the nonfederally chartered housing creditors to which their respective regulations apply, including without limitation, making necessary changes in terminology to conform the regulatory and disclosure provisions to those more typically associated with various types of transactions including credit sales.

And the Senate agree to the same.

FERNAND J. ST GERMAIN,
HENRY S. REUSS,
FRANK ANNUNZIO,
J. W. STANTON,
CHALMERS P. WYLIE,
Managers on the Part of the House.

JAKE GARN,
JOHN TOWER,
DICK LUGAR,
DON RIEGLE,
ALAN CRANSTON,
Managers on the Part of the Senate.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 745

Conforming Amendments To Lending Regulations; Growth Equity Mortgages; Regulation of Due-on-Sale for Window Period Loans; Alternative Mortgage Transactions Study

AGENCY: National Credit Union Administration (NCUA)

ACTION: Final regulations.

SUMMARY: A number of provisions of the Garn-St Germain Depository Institutions Act of 1982 apply to loans made by credit unions and require action by NCUA. Title V amends the Federal Credit Union Act, revising the procedures for processing loan applications, removing certain restrictions on loans that Federal credit unions can grant, and confirming that Federal credit unions may make loans meeting secondary market requirements. It also requires NCUA to conform its lending regulations. Title III preempts state prohibitions on the enforcement of due-on-sale clauses. It requires NCUA to act to permit Federal credit unions to enforce due-on-sale clauses in certain loans made before October 15, 1982. Title VIII provides state credit unions parity with Federal credit unions in making alternative mortgage loans. It requires NCUA to study its regulations and identify those that will and those that will not apply to state credit unions in order to give state and Federal credit unions more flexibility to design their own loan programs as soon as possible. NCUA is simultaneously taking the necessary steps to implement the provisions of these Titles of the Garn-St Germain Act.

EFFECTIVE DATE: November 18, 1982.

FOR FURTHER INFORMATION CONTACT: Robert M. Fenner, Deputy General Counsel, or John L. Culhane, Jr., Senior Attorney, Department of Legal Services, National Credit Union Administration, 1776 G Street, N.W., Washington, D.C. 20456 or telephone (202) 357-1030.

SUPPLEMENTARY INFORMATION: A number of provisions of the Garn-St Germain Depository Institutions Act of 1982 apply to loans made by credit unions. To implement these provisions, NCUA is taking the following actions.

Conforming Amendments to Lending Regulations

Among other things, Title V of the Garn-St Germain Act amends the Federal Credit Union Act provisions that apply to loans made by Federal credit unions. It revises the procedures for processing loan applications, making a credit committee optional and requiring a loan to an official to be approved by the board of directors only where the official's total indebtedness exceeds $10,000 plus pledged shares, rather than $5,000 plus pledged shares, as had been the case. It expands the authority of Federal credit unions to make loans: allowing first mortgage loans to be made for more than 30 years, to be made regardless of the sales price, and to be refinanced; allowing second mortgage loans to be made for 15 years, regardless of the purpose; and allowing loans on terms acceptable to a government agency that has made an advance commitment to purchase the loans. It also confirms the ability of Federal credit unions to comply with secondary market requirements, permitting certain limits on the prepayment of mortgage loans and permitting the insurance of custodial accounts. These statutory changes require NCUA to conform its lending regulations.

As a result, NCUA is making the following changes to its regulations. References to the procedures for processing loan applications in §§ 701.21-1 and 701.21-4 are being revised to include the possibility that loans may be approved by the board of directors. In § 701.21-4, references to the trigger for board of directors approval of a loan to an official are being revised from $5,000 plus pledged shares to $10,000 plus pledged shares. NCUA's regulations on mortgage loans, §§ 701.21-6, 701.21-6A, and 701.21-6B, are being revised to allow first mortgage loans to be financed or refinanced for up to 40 years and to be made regardless of the sales price. These regulations are also being revised to permit certain limitations on the prepayment of mortgage loans. And a new § 745.3(d) is being added to provide for the insurance of custodial accounts. For convenience, certain technical changes are also being made at this time.

Growth Equity Mortgages

A growth equity mortgage is a mortgage that provides for the accelerated repayment of the loan, either as a result of movements in an index or as the result of scheduled increases in payments of principal and interest. Mindful of the emphasis that the Garn-St Germain Act places on equity loans made by Federal credit unions, as many of the amendments of Title V are designed to facilitate equity loans, and on alternative mortgage loans made by Federal and state credit unions, and as Title VIII is designed to facilitate alternative mortgage loans by providing state credit unions parity with Federal credit unions, the NCUA Board believes that it is appropriate at this time to authorize growth equity mortgages for Federal credit unions.

Section 701.21-6(b)(2) of NCUA's regulations requires that a fixed rate long term first mortgage loan be amortized by substantially equal monthly installments sufficient to retire the loan at maturity, although other amortization schedules may be approved with the prior written consent of the Administration. In promulgating this regulation, NCUA was exercising its plenary and exclusive authority set forth in sections 107(5)(A)(i) and 107(5)(A)(ix) of the Federal Credit Union Act to regulate the real estate loans granted by Federal credit unions and the amortization of loans granted by Federal credit unions. This exercise of the Board's authority preempted state laws purporting to address the ability of a Federal credit union to set its own loan amortization schedules, either directly or indirectly. Pursuant to that authority, and in accordance with its regulation, the NCUA Board hereby provides written consent for all Federal credit unions to make growth equity first mortgage loans with initial maturities in excess of 12 years.

Regulation of Due-on-Sale Clauses for Window Period Loans

A Federal credit union's ability to exercise a due-on-sale clause is now governed by section 341 of Title III of the Garn-St Germain Act. Under section 341, a Federal credit union may generally exercise a due-on-sale clause if the loan was made after October 15, 1982, or if the loan was made in a state that permitted the exercise of due-on-sale clauses; in states that prohibited the exercise of due-on-sale, a Federal credit union may not generally exercise a due-on-sale clause in the case of a transfer that took place before October 15, 1982.

Special rules apply, however, in the case of loans made during a "window" period, the length of which will vary from state to state. A state has a window period only if the state either passed a statute prohibiting the exercise of a due-on-sale clause or a state court handed down a decision, applicable state wide, prohibiting the exercise of a due-on-sale clause. In that case, the window period begins on the date of enactment, or date of decision, and ends October 15, 1982.

If a loan is made or assumed during the window period, then a Federal credit union cannot enforce a due-on-sale clause except in the case of transfers that take place on or after October 15, 1985. However, NCUA can adopt regulations to handle window period loans differently, either by shortening or lengthening the time the prohibition on the enforcement of due-on-sale clauses will apply. The time may not, however, be shortened to a date earlier than the date of adoption of the regulations.

NCUA is therefore republishing its regulations governing the exercise of due-on-sale clauses in long term first mortgage loans in order to enable Federal credit unions to exercise due-on-sale clauses in the case of transfers that take place on or before November 18, 1982. NCUA originally chose to require the use of an instrument containing a due-on-sale clause because of its belief that the ability of a Federal credit union to exercise the rights afforded by a due-on-sale clause was essential to a Federal credit union's safe and sound participation in the long term residential mortgage market. Because Federal credit unions assessed the risks of entering into this market in reliance upon NCUA's regulation, the NCUA Board believes that prompt action is necessary to protect the safety and soundness of those credit unions that chose to enter the long term residential mortgage market.

Alternative Mortgage Transactions Study

Title VIII of the Garn-St Germain Act provides state credit unions parity with Federal credit unions in making alternative mortgage loans. Section 807 of the Act requires NCUA to study its regulations to identify those regulations that will not apply to state credit unions.

For purposes of clarity, NCUA is making certain amendments to its regulations so that state credit unions may more easily locate those regulations under which Federal credit unions make alternative mortgage loans. Briefly, as amended, Federal credit unions make alternative mortgage loans under § 701.21-2 of NCUA's regulations (short term adjustable rate first mortgage loans, adjustable rate mobile home loans, adjustable rate second mortgage loans, et cetera), § 701.21-3 of NCUA's regulations (lines of credit), § 701.21-5 of NCUA's regulations (loans made pursuant to government insured or guaranteed loan programs or pursuant to an advance commitment by a government agency to purchase the loans), § 701.21-6 of NCUA's regulations (long term growth equity loans), and § 701.21-6B of NCUA's regulations (long term adjustable rate first mortgage loans).

A preliminary review of these regulations was conducted and various state credit union supervisors, trade associations and other interested parties were advised that it did not appear that any of the provisions of these regulations would be inappropriate for use by state credit unions. As none of these parties have objected to these conclusions, at this time the NCUA Board does not believe that there are any regulatory provisions that are inappropriate for use by state credit unions.

Procedures for Regulatory Development

The NCUA Board for good cause finds that notice and public comment on these regulations is unnecessary and contrary to the public interest. The conforming amendments to the lending regulations merely remove inconsistencies between the statutory and regulatory provisions governing lending by Federal credit unions. The due-on-sale regulations are necessary to preserve the safety and soundness of those Federal credit unions that entered into the long term residential mortgage market in reliance upon regulations promulgated after notice and public comment. The regulations adopted to facilitate alternative mortgage transactions by state credit unions merely clarify the authority currently afforded Federal credit unions. For the same reasons, and because the regulations remove restrictions, the final regulations are being made effective in less than 30 days.

The final regulations will not have a significant economic impact on a substantial number of small credit unions. The conforming amendments merely remove inconsistencies between the statutory and regulatory provisions governing lending and will therefore increase their flexibility. The due-on-sale regulations will not have a significant economic impact on a substantial number of small credit unions because only a few credit unions with less than $1 million in assets are making or have made long term residential mortgage loans. The regulations adopted to clarify the authority of Federal credit unions to make alternative mortgage loans will likewise not have a significant economic impact on a substantial number of small credit unions because only a few credit unions with less $1 million in assets will make alternative mortgage loans. Therefore, a Regulatory Flexibility Analysis is not required.

List of Subjects in 12 CFR Parts 701 and 745

Credit unions, Mortgages, Insurance.

By the National Credit Union Administration Board on the 18th of November 1982.

Rosemary Brady,

Secretary of the Board.

PART 701—[AMENDED]

Authority: 12 U.S.C. 1757, 1766(a), and 1789(a)(11).

Accordingly, 12 CFR Parts 701 and 745 are amended as set forth below.

1. 12 CFR 701.21-1(c) is revised to read as follows:

§ 701.21-1 Lending policies.

* * * * *

(c) Subject to limitations established by the board of directors, when a loan is approved the board of directors, the credit committee or the loan officer, whichever approved the loan, shall assure that a credit application is on file which supports the decision to extend credit.

2. 12 CFR 701.21-2(b) is revised to read as follows:

§ 701.21-2 Amortization and payment of loans to members.

* * * * *

(b) This rule is promulgated pursuant to the exclusive authority of the NCUA Board to regulate lending and loan amortization as set forth in sections 107(5), 107(5)(A)(ii) and 107(5)(A)(ix) of the Federal Credit Union Act, 12 U.S.C. 1757(5), (5)(A)(ii) and (5)(A)(ix). This exercise of the Board's authority preempts any state law purporting to address the subject of a Federal credit union's ability or right to make adjustable rate consumer loans, short term adjustable rate first mortgage loans, short term growth equity mortgage loans, adjustable rate mobile home loans, adjustable rate second mortgage loans, and other similar loans or to directly or indirectly restrict such ability or right.

§ 701.21-4 [Amended]

3. 12 CFR 701.21-4(b) is amended by adding the words "As provided in the bylaws, the board of directors," before the words "the credit committee or loan officer shall act upon all applications."

4. 12 CFR 701.21-4(c)(3) is amended by removing the word "$5,000" and by inserting in its place the word "$10,000."

5. 12 CFR 701.21-5 is added to read as follows:

§ 701.21-5 Insured, guaranteed and advance commitment loans.

(a) A loan secured by the insurance or guarantee of, or with advance commitment to purchase the loan by, the Federal Government, a State government, or any agency of either may be made for the maturity and under the terms and conditions specified in the law under which such insurance, guarantee or commitment is provided.

6. 12 CFR 701.21-6 is revised to read as follows:

§ 701.21-6 Long term fixed rate first mortgage loans.

(a) For purposes of this section: (1) "One-to-four family dwelling" means a structure designed for residential use by not more than four families. The term includes a one-to-four family unit in a cooperative housing development. The term also includes a one-to-four family unit in a planned unit development or condominium project where certain portions of the security property are owned in common with others.

(2) "Principal residence" means a structure where the member will be domiciled or will reside permanently within 6 months after initial disbursement of the loan, or within 18 months provided the structure is being newly constructed or extensively rehabilitated.

(3) "Value" means the lower of the appraised market value or the purchase price. In the case of a residence being rehabilitated, "Value" shall also include the cost of rehabilitation. The cost of rehabilitation shall be supported by a good faith estimate.

(4) "Appraisal" means an objective estimate of value based upon a physical examination and evaluation which shall disclose the market value of the security offered by use of the market sales approach which shall be supported by an analysis of comparable properties in the immediate area. The market value should also be supported by use of the cost and income appraisal methods if conditions warrant.

(5) "Appraiser" means a person who is experienced in the appraisal of one-to-four family dwellings and is actively engaged in such appraisal work and whose qualifications are demonstrated by membership in a national professional appraisal organization, or who is licensed to appraise in the state in which the residence is located or who is acceptable as an appraiser by an insuring or guaranteeing agency of the Federal or State government.

(6) "Market value" means the highest price which the residence will bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus.

(7) "Security instrument" means either a Deed of Trust, Mortgage or Leasehold Mortgage which constitutes a first lien, or in the case of a loan on a one-to-four family dwelling in a cooperative housing development, a Security Agreement which constitutes a first security interest in stock or a membership certificate issued to a tenant stockholder or resident member of a cooperative housing organization and which provides for the assignment of the borrower's interest in the proprietary lease or right of tenancy in property issued by such organization. Only in those areas of the United States of America, its territories and possessions, or the Commonwealth of Puerto Rico where an interest in real estate is customarily evidenced by leasehold or ground estates will the term "Leasehold Mortgage" be included in this definition.

(8) "Escrow account" means either a special limited withdrawal share account or accounts payable account for the accumulation of funds to pay for not more than one year's taxes, assessments, insurance premiums, construction proceeds, or other charges that could affect the credit union's first lien or first security interest.

(9) "Title insurance" means insurance protecting the credit union against loss due to clouds or defects in title to the residence equaling the current principal balance of the loan and also protecting and benefiting subsequent purchasers of the loan.

(10) "Hazard insurance" means property insurance affording protection against loss or damage from fire and other hazards covered by the industry's standard extended coverage endorsement which provides for payment of an amount sufficient to pay the loan balance in the event of a covered loss, with a standard clause in favor of the credit union and subsequent purchasers of the loan.

(b) Within the limitations of written policies adopted by the board of directors, Federal credit unions may originate loans secured by first liens on residential real property or secured by first security interests in residential cooperatives, with maturities in excess of 12 years and not exceeding 40 years, provided: (1) Loans shall be made to finance or refinance a one-to-four family dwelling that is or will be the principal residence of the Federal credit union member.

(2) Loans shall be amortized by substantially equal monthly installments sufficient to retire the loan at maturity. Each monthly installment shall be applied first to taxes and insurance due and payable (when an escrow account is established), then to interest currently due and payable, with the remainder to prinicpal. Amortization shall commence no later than 61 days after disbursemen of proceeds and shall not exceed 40 years from date of disbursement. With prior written consent of the Administration, loans may be amortized by other than substantially equal monthly installments.

(3) The aggregate dollar amount of such loans outstanding may not exceed 25 per centum of the Federal credit union's assets without prior written consent of the Administration. This limitation does not include loans with maturities not exceeding 12 years.

(4) The loan shall not exceed 90 per centum of value at the time of disbursement except that the loan amount may equal up to 95 per centum of value provided that private mortgage insurance is obtained for the amount of the loan in excess of 90 per centum of value.

(5) The loan application shall be the current revision of FHLMC Form 65/FNMA Form 1003 or its equivalent.

(6) The security instruments and notes shall be executed on the current revision of the FNMA/FHLMC Uniform Instruments for the jurisdiction in which the property is located or their equivalent. No prepayment penalty shall be allowed, although a Federal credit union may require that any partial prepayments be made on the date monthly installments are due and be in the amount of that part of one or more monthly installments that would be applicable to principal.

(7) The loan shall be secured by a perfected first lien or first security interest in favor of the credit union supported by a properly executed and recorded security instrument. No loan shall be secured by a residence located outside the United States of America, its territories and possessions, or the Commonwealth of Puerto Rico.

(8) Where an interest in real estate is customarily evidenced by leasehold or ground rent estates, loans shall comply with the preceding provisions of this section in addition to the procedures customarily followed to perfect an interest in a leasehold or ground rent estate.

(9) A Federal credit union may require the member/borrower to maintain an escrow share account. If a member's loan is assumed by a nonmember, any required escrow account shall be maintained as interest bearing account payable. The rate of interest paid on such accounts shall be at least equal to the lowest yielding dividend rate paid on any share accounts offered by the credit union.

(10) Each loan file shall contain the following: (i) A loan application supported by an executed sales contract and any modifications bearing the signature of the applicant(s).

(ii) A written appraisal on the current revision of FHLMC Form 70/FNMA Form 1004; FHLMC 465; FNMA Form 1004–A or their equivalent, prepared and signed prior to approval of the loan application by an appraiser who shall provide a certification on the current revision of FHLMC Form 439 or its equivalent.

(iii) When applicable, a private insurance certificate.

(iv) A complete settlement statement (Form HUD–1) detailing all charges and fees and distribution of the loan proceeds.

(v) An opinion of title signed by an attorney licensed to practice in the jurisdiction in which the property is located or a title insurance policy affirming the quality and the position of the first lien or first security interest.

(vi) A current hazard insurance policy.

(vii) A flood insurance policy, if required.

(viii) A properly executed note and security instrument and a document indicating the date and place(s) of recording of such instruments.

(c) The following restrictions shall be applicable to all loans made under this section: (1) A Federal credit union shall not grant any loan on the prior condition, agreement, or understanding that the borrower contract with any specific person or organization for the following: (i) Insurance services (as an agent, broker, or underwriter);

(ii) Building materials or construction services;

(iii) Legal services rendered to the borrower; and

(iv) Services of a real estate agent or broker.

(2) Notwithstanding the preceding paragraph, a Federal credit union may refuse to grant any loan if it believes, on reasonable grounds, that the insurance services provided by the person or organization selected by the borrower will afford insufficient protection to the credit union.

(3) A Federal credit union shall not make any loan if, either directly or indirectly, any commission, fee or other compensation is to be paid to, or received by, any of its officials or employees in connection with the procuring or insuring of the loan.

(4) Early repayment of a loan involving points or finance charges shall require recomputation. A refund, or an adjustment of the final payment, must be made to ensure that the true rate of interest has not exceeded the maximum rate authorized by law at the time the loan was granted. This requirement also applies to loans the credit union has sold in whole or in part.

(d) Due-on-sale clauses: (1) Except as otherwise provided herein, the exercise of a due-on-sale clause by a Federal credit union is governed exclusively by section 341 of the Garn-St Germain Depository Institutions Act of 1982 and by any regulations issued by the Federal Home Loan Bank Board implementing section 341 of the Garn-St Germain Act.

(2)(i) In the case of a contract involving a loan made pursuant to this section which was made or assumed, including a transfer of the liened property subject to the loan, during the period beginning on the date a State adopted a constitutional provision or statute prohibiting the exercise of due-on-sale clauses, or the date on which the highest court of such state has rendered a decision (or if the highest court has not so decided the date on which the next highest court has rendered a decision resulting in a final judgment if such decision applies state-wide) prohibiting such exercise and ending on October 15, 1982, a Federal credit union may exercise a due-on-sale clause in the case of a transfer which occurs on or after November 18, 1982, unless exercise of the due-on-sale clause would be based on any of the following:

(A) The creation of a lien or other encumbrance subordinate to the lender's security instrument which does not relate to a transfer of rights of occupancy in the property;

(B) The creation of a purchase money security interest for household appliances;

(C) A transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(D) The granting of a leasehold interest of 3 years or less not containing an option to purchase;

(E) A transfer to a relative resulting from the death of a borrower;

(F) A transfer where the spouse or children of the borrower become an owner of the property;

(G) A transfer resulting from a decree of a dissolution of marriage, legal separation agreements, or from an incidental property settlement agreement, by which the spouse of the borrower becomes an owner of the property;

(H) A transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property; or

(I) Any other transfer or disposition described in regulations prescribed by the Federal Home Loan Bank Board.

(ii) This section is being promulgated pursuant to the plenary and exclusive authority of the NCUA Board as set forth in Sections 107(5)(A)(i), 107(5)(A)(ix), and 107(13) of the Federal Credit Union Act to regulate, respectively, the real estate loans granted by Federal credit unions, the amortization of loans granted by Federal credit unions, and the sale of loans granted by Federal credit unions. This exercise of the Board's authority preempts state laws purporting to address the ability of a Federal credit union to exercise its rights under a due on sale clause to raise interest rates on these loans.

7. 12 CFR 701.21–6A is amended by revising paragraphs (b)(1), (b)(2)(i), (b)(2)(iii), and (b)(3) to read as follows:

§ 701.21–6A Business relationship with mortgage lender.

* * * * *

(b) * * *

(1) *General Loan Terms.* A loan will only be granted to finance or refinance the acquisition of a one-to-four family dwelling that is or will be the principal residence of the borrower. The maturity will not exceed 40 years. The loan will be secured by a first lien or first security interest on the dwelling.

(2) * * *

(i) *Interest Rate.* The interest rate charged on the loan will not exceed the maximum rate permitted a Federal credit union at the time the loan is granted.

(ii) * * *

(iii) *Prepayment.* The borrower will be able to repay the loan prior to maturity

in whole or in part on any business day without penalty, although the mortgage lender may require that any partial prepayment be made on the date monthly installments are due and be in the amount of that part of one or more monthly installments which would be applicable to principal.

(3) *Insured, Guaranteed or Advance Commitment Loans.* A loan secured by the insurance or guarantee of, or with advance commitment to purchase the loan by, the Federal Government, a State government, or any agency of either may be made under the additional terms and conditions specified in the law under which such insurance, guarantee or commitment is provided.

§ 701.21-6B [Amended]

8. 12 CFR 701.21-6B is amended by revising the title to read as follows:

§ 701.21-6B Long term adjustable rate first mortgage loans.

9. 12 CFR 701.21-6B(b)(1) is amended by removing the words "on residential real property" and inserting the words "or first security interests on the residence" and by removing the word "30" and by inserting in its place the word "40."

10. 12 CFR 701.21-6B(1)(ii) is amended by removing the words "Section 701.21-6(b)(4)" and by inserting in their place the words "Section 701.21-6(b)(3)."

11. 12 CFR 701.21-6B(1)(iii) is amended by removing the words "Section 701.21-6(b)(7)" and by inserting in their place the words "§ 701.21-6(b)(6)."

§ 701.21-7 [Amended]

12. 12 CFR 701.21-7(b)(3) is amended by removing the words "Part 701.21-6(b)(4) of this Chapter" and by inserting in their place the words "§ 701.21-6(b)(3)."

§ 701.21-8 [Amended]

13. 12 CFR 701.21-8(a)(3) is revised to read as follows:

(a) * * *

(3) "Real estate loan" means a loan granted on a one-to-four family dwelling that is or will be the principal residence of the borrower and which is secured by a first lien or first security interest on the dwelling.

* * * * *

14. 12 CFR 701.21-8(b)(iv) is amended by removing the words "section 701.21(6)(b)(4)" and by inserting in their place the words "§ 701.21-6(b)(3)."

PART 745—[AMENDED]

15. 12 CFR Part 745 is amended by adding a new § 745.3(d) to read as follows:

§ 745.3 Single ownership accounts.

* * * * *

(d) *Custodial Accounts.* Loan payments received by a Federal credit union prior to remittance to other parties to whom the loan was sold pursuant to section 107(13) of the Federal Credit Union Act and § 701.21-8 of NCUA's regulations shall be considered to be funds owned by the borrower and shall be added to any individual accounts of the borrower and insured up to $100,000 in the aggregate.

[FR Doc. 82-32337 Filed 12-2-82; 8:45 am]
BILLING CODE 7535-01-M

§701.21-6B Adjustable Rate Mortgage Loans

(a) Definition.

(1) An adjustable rate mortgage loan is a mortgage loan which permits the periodic adjustment of the rate of interest on the loan in response to the movement of an index which was agreed upon in advance by the borrower and the Federal credit union.

(b) Authorization.

(1) Federal credit unions are permitted to make adjustable rate mortgage loans to members. Such loans must be secured by first liens on residential real property and must have initial maturities in excess of 12 years and not exceeding 30 years. Loans which are made under the provisions of this rule shall also comply with all the provisions of Section 701.21-6 of the NCUA Rules and Regulations except for the following:

(i) The provisions of Section 701.21-6(b)(2) (which require substantially equal monthly payments);

(ii) The provisions of Section 701.21-6(b)(4) (which limit the aggregate dollar amount of fixed rate mortgage loans to 25 per centum of the credit union's assets); and

(iii) The provisions of 701.21-6(b)(7) (which require the use of the FNMA/FHLMC Uniform Instruments).

(2) This rule is promulgated pursuant to the plenary and exclusive authority of the NCUA Board as set forth in Sections 107(5)(A)(i), 107(5)(A)(ix), and 107(13) of the Federal Credit Union Act to regulate, respectively, the real estate loans granted by Federal credit unions, the amortization of loans granted by Federal credit unions, and the sale of loans granted by Federal credit unions. This exercise of the Board's authority preempts any state law purporting to address the subject of a Federal credit union's ability or right to make adjustable rate mortgage loans or to directly or indirectly restrict such ability or right.

(c) Amortization.

(1) Adjustable rate mortgage loans shall be amortized by monthly installments sufficient to retire the loan at maturity. If the principal balance of the loan is adjusted in response to a movement in the index, the amount of the monthly payment shall be adjusted at least every 5 years to a level sufficient to amortize the loan balance at the then existing interest rate over the remaining term of the loan.

(d) Adjustment Options.

(1) Adjustments to the interest rate may be implemented through changes in the monthly payment amount, through adjustment to the outstanding principal loan balance, through extension of the loan maturity or by a combination of these adjustments.

(2) Adjustments shall not cause the maturity to exceed 40 years.

(3) Adjustments may be made as frequently as monthly.

(4) The maximum amount of any one adjustment may be capped.

(e) Index.

(1) The adjustment in the interest rate shall correspond with the movement of an index or an average of an index agreed upon in advance, subject to such rate adjustment limitations, if any, as a Federal credit union may provide. The index must be beyond the control of the Federal credit union and readily verifiable by the borrower.

(2) Where the index or an average of an index has moved downward, a decrease in the interest rate is mandatory except to the extent that:

(i) The decrease is offset by previously permitted interest rate increases not taken;

(ii) The decrease exceeds a cap limitation;

(iii) The decrease in the interest rate is less than one-eighth of 1 percent; or

(iv) The decrease would reduce the interest rate below a minimum rate agreed upon in advance by the borrower and the Federal credit union.

(f) Costs or Fees.

(1) The borrower shall not be charged any costs or fees in connection with regularly scheduled adjustments to the interest rate, the monthly payment, the outstanding principal loan balance, or the loan maturity.

PART 701

§701.21-2 Amortization and Payment of Loans to Members

(a) General Rule: Loans shall be paid or amortized in accordance with written policies prescribed by the board of directors after taking into account the needs or conditions of the borrowers, the amounts and duration of the loans, the interests of the members and such other factors as the board deems relevant.

(b) This rule is promulgated pursuant to the exclusive authority of the NCUA Board to regulate consumer lending and loan amortization as set forth in sections 107(5), 107(5)(A)(ii), 107(5)(A)(iii) and 107(5)(A)(ix) of the Federal Credit Union Act. 12 U.S.C. 1757(5), (5)(A)(ii), (5)(A)(iii), and (5)(A)(ix). This exercise of the Board's authority preempts any state law purporting to address the subject of a Federal credit union's ability or right to make variable rate consumer loans or to directly or indirectly restrict such ability or right.

The KANSAS BANKERS ASSOCIATION
A Full Service Banking Association

February 3, 1983

TO: House Committee on Commercial and Financial Institutions

RE: HB 2072

Mr. Chairman and members of the Committee:

We appreciate the opportunity to appear before the Committee in support of HB 2072 which would amend K.S.A. 16-842 to conform with existing federal law and regulation. Since this Kansas statute was passed in 1972 setting forth the liability of a credit cardholder for any unauthorized use of a credit card, the federal government has altered the provisions requiring the credit card issuer to provide a card recipient a self-addressed, prestamped envelope to send back to the card issuer in case of loss or theft of the card by the cardholder. HB 2072 would simply strike the language in K.S.A. 16-842 requiring that such a self-addressed, prestamped envelope be provided in the intital notification to the cardholder.

The federal Truth-In-Lending Act in 15 USC 1643(a) says the credit card issuer must provide the cardholder with a description of notifying of the loss or theft, and Regulation Z (which amplifies Truth-In-Lending) says in Section 226.12(b) that the creditor must tell the cardholder his notification may be either oral or written. In other words, a telephone call to the credit card issuer will suffice and currently statistics of card issuers in the state of Kansas indicate that over 97% of the notifications to the card issuer of lost or stolen cards are received by telephone.

Card issuing banks in Kansas have long had a policy of accepting telephone notice for lost or stolen credit cards. Such contact is more convenient and more likely to minimize the consumer's liability for unauthorized use.

The description of the means of notification is a condition that must preceed imposing the $50 liability on the consumer that is allowed by both state and federal law. Kansas banks give the consumer such a description in the initial agreement and in every statement going to the customer. We strongly believe that this amendment to K.S.A. 16-842 will not only bring conformity between state-chartered and federally-chartered institutions, but it will also simplify the procedure for issuing credit cards and result in lower service costs for the issuing banks.

Thank you very much for the opportunity to appear and we respectfully request that the Committee recommend HB 2072 favorably for passage.

James S. Maag
Director of Research

Attachment 3

House C & F I 2/3/83

Office of Executive Vice President • 707 Merchants National Building
Eighth and Jackson • Topeka, Kansas 66612 • (913) 232-3444

6–748

226.12 (b) *Liability of cardholder for unauthorized use.* (1) *Limitation on amount.* The liability of a cardholder for unauthorized use [22] of a credit card shall not exceed the lesser of $50 or the amount of money, property, labor, or services obtained by the unauthorized use before notification to the card issuer under paragraph (b)(3) of this section.

(2) *Conditions of liability.* A cardholder shall be liable for unauthorized use of a credit card only if—

(i) The credit card is an accepted credit card;

(ii) The card issuer has provided adequate notice [23] of the cardholder's maximum potential liability and of means by which the card issuer may be notified of loss or theft of the card. The notice shall state that the cardholder's liability shall not exceed $50 (or any lesser amount) and that the cardholder may give oral or written notification, and shall describe a means of notification (for example, a telephone number, an address, or both); and

(iii) The card issuer has provided a means to identify the cardholder on the account or the authorized user of the card.

6–749

(3) *Notification to card issuer.* Notification to a card issuer is given when steps have been taken as may be reasonably required in the ordinary course of business to provide the card issuer with the pertinent information about the loss, theft, or possible unauthorized use of a credit card, regardless of whether any particular officer, employee, or agent of the card issuer does, in fact, receive the information. Notification may be given, at the option of the person giving it, in person, by telephone, or in writing. Notification in writing is considered given at the time of receipt or, whether or not received, at the expiration of the time ordinarily required for transmission, whichever is earlier.

(4) *Effect of other applicable law or agreement.* If state law or an agreement between a cardholder and the card issuer imposes lesser liability than that provided in this paragraph, the lesser liability shall govern.

(5) *Business use of credit cards.* If 10 or more credit cards are issued by one card issuer for use by the employees of an organization, this section does not prohibit the card issuer and the organization from agreeing to liability for unauthorized use without regard to this section. However, liability for unauthorized use may be imposed on an employee of the organization, by either the card issuer or the organization, only in accordance with this section.

6–750

(c) *Right of cardholder to assert claims or defenses against card issuer.*[24] (1) *General rule.* When a person who honors a credit card fails to resolve satisfactorily a dispute as to property or services purchased with the credit card in a consumer credit transaction, the cardholder may assert against the card issuer all claims (other than tort claims) and defenses arising out of the transaction and relating to the failure to resolve the dispute. The cardholder may withhold payment up to the amount of credit outstanding for the property or services that gave rise to the dispute and any finance or other charges imposed on that amount.[25]

[22] "Unauthorized use" means the use of a credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use, and from which the cardholder receives no benefit.

[23] "Adequate notice" means a printed notice to a cardholder that sets forth clearly the pertinent facts so that the cardholder may reasonably be expected to have noticed it and understood its meaning. The notice may be given by any means reasonably assuring receipt by the cardholder.

[24] This paragraph does not apply to the use of a check guarantee card or a debit card in connection with an overdraft credit plan, or to a check guarantee card used in connection with cash advance checks.

[25] The amount of the claim or defense that the cardholder may assert shall not exceed the amount of credit outstanding for the disputed transaction at the time the cardholder first notifies the card issuer or the person honoring

Continued

§ 1642. Issuance of credit cards

No credit card shall be issued except in response to a request or application therefor. This prohibition does not apply to the issuance of a credit card in renewal of, or in substitution for, an accepted credit card.

(Pub.L. 90–321, Title I, § 132, as added Pub.L. 91–508, Title V, § 502(a), Oct. 26, 1970, 84 Stat. 1126.)

Historical Note

Effective Date. Section 503(1) of Pub.L. 91–508 provided that: "Section 132 of such Act [this section] takes effect upon the date of enactment of this title [Oct. 26, 1970]."

Legislative History. For legislative history and purpose of Pub.L. 91–508, see 1970 U.S. Code Cong. and Adm.News, p. 4394.

Truth In Lending Regulations

Issuance, conditions, see § 226.12(a), set out following section 1700 of this title.

Library References

Consumer Credit ⇐8.

C.J.S. Interest and Usury; Consumer Credit § 348.

§ 1643. Liability of holder of credit card

Limits on liability

(a)(1) A cardholder shall be liable for the unauthorized use of a credit card only if—

(A) the card is an accepted credit card;

(B) the liability is not in excess of $50;

(C) the card issuer gives adequate notice to the cardholder of the potential liability;

(D) the card issuer has provided the cardholder with a description of a means by which the card issuer may be notified of loss or theft of the card, which description may be provided on the face or reverse side of the statement required by section 1637(b) of this title or on a separate notice accompanying such statement;

(E) the unauthorized use occurs before the card issuer has been notified that an unauthorized use of the credit card has occurred or may occur as the result of loss, theft, or otherwise; and

(F) the card issuer has provided a method whereby the user of such card can be identified as the person authorized to use it.

(2) For purposes of this section, a card issuer has been notified when such steps as may be reasonably required in the ordinary course of business to provide the card issuer with the pertinent information have been taken, whether or not any particular officer, employee, or agent of the card issuer does in fact receive such information.

Burden of proof

(b) In any action by a card issuer to enforce liability for the use of a credit card, the burden of proof is upon the card issuer to show that the use was authorized or, if the use was unauthorized, then the burden of proof is upon the card issuer to show that the conditions of liability for the unauthorized use of a credit card, as set forth in subsection (a) of this section, have been met.

Liability imposed by other laws or by agreement with issuer

(c) Nothing in this section imposes liability upon a cardholder for the unauthorized use of a credit card in excess of his liability for such use under other applicable law or under any agreement with the card issuer.

Exclusiveness of liability

(d) Except as provided in this section, a cardholder incurs no liability from the unauthorized use of a credit card.

(Pub.L. 90–321, Title I, § 133, as added Pub.L. 91–508, Title V, § 502(a), Oct. 26, 1970, 84 Stat. 1126, and amended Pub.L. 96–221, Title VI, § 617, Mar. 31, 1980, 94 Stat. 182.)

Text of Subsection (a) Effective Until October 1, 1982

Prior to its amendment by Pub.L. 96–221, effective upon the expiration of two years and six months after March 31, 1980, subsec. (a) of this section read as follows:

(a) A cardholder shall be liable for the unauthorized use of a credit card only if the card is an accepted credit card, the liability is not in excess of $50, the card issuer gives adequate notice to the cardholder of the potential liability, the card issuer has provided the cardholder with a self-addressed, prestamped notification to be mailed by the cardholder in the event of the loss or theft of the credit card, and the unauthorized use occurs before the cardholder has notified the card issuer that an unauthorized use of the credit card has occurred or may occur as the result of loss, theft, or otherwise. Notwithstanding the foregoing, no cardholder shall be liable for the unauthorized use of any credit card which was issued on or after the effective date of this section, and, after the expiration of twelve months following such effective date, no cardholder shall be liable for the unauthorized use of any credit card regardless of the date of its issuance, unless (1) the conditions of liability specified in the preceding sentence are met, and (2) the card issuer has provided a method whereby the user of such card can be identified as the person authorized to use it. For the purposes of this section, a cardholder notifies a card issuer by taking such steps as may be reasonably required in the ordinary course of business to provide the card issuer with the pertinent information whether or not any particular officer, employee, or agent of the card issuer does in fact receive such information.

Historical Note

1980 Amendment. Subsec. (a). Pub.L. 96–221 revised existing provisions into pars. (1) and (2) and, as so revised, in par. (1) made changes in structure and phraseology and revised means of notice and verification, and in par. (2) made changes in phraseology.

Effective Date of 1980 Amendment. Amendment by Pub.L. 96–221 effective upon the expiration of two years and six months after Mar. 31, 1980, with all regulations, forms, and clauses required to be prescribed to be promulgated at least one year prior to such effective date, and allowing any creditor to comply with any amendments, in accordance with the regulations, forms, and clauses prescribed by the Board prior to such effective date, see section 625 of Pub.L. 96–221, set out as an Effective Date of 1980 Amendment note under section 1602 of this title.

Effective Date. Section 503(2) of Pub.L. 91–508 provided that: "Section 133 of such Act [this section] takes effect upon the expiration of 90 days after such date of enactment [Oct. 26, 1970]."

Legislative History. For legislative history and purpose of Pub.L. 91–508, see 1970 U.S. Code Cong. and Adm.News, p. 4394. See, also, Pub.L. 96–221, 1980 U.S.Code Cong. and Adm.News, p. 236.