



Compliance Journal

Special Focus

Update on Loan Renewals in Wisconsin

WBA is commonly asked whether standard loan closing disclosures are required when a lender renews an existing consumer loan. This article is intended to update information regarding loan renewals in Wisconsin found in Notice 2008-2, which appeared in the February 2008 *WBA Compliance Journal*.

For purposes of this article, a renewal is an extension of the term of an existing closed end loan (without additional advances) by the lender that originally made the loan to the same consumer. Commonly, the interest rate may change to reflect market conditions at the time of renewal and the payment schedule may be modified to reflect the continuing amortization of the loan based on the new interest rate. The following summarizes disclosure requirements and their applicability to such loan renewals.

1. Truth-in-Lending and Regulation Z.

Under Reg Z, disclosures must be given at or prior to the consummation of a loan. This includes, for example, personal consumer loan disclosures and TRID disclosures. When a loan is renewed, must the lender give these disclosures again? New disclosures will be required only if the renewal is considered a refinancing, as defined in Reg Z. A refinancing occurs when an existing obligation is satisfied and replaced by a new obligation undertaken by the same consumer. If the renewal is not a

refinancing as defined in Reg Z, (that is, the loan to the consumer has not been satisfied and replaced with a new obligation) new disclosures are not required. There are two exceptions. New disclosures are always required for a renewal if:

- a variable rate feature is added to the obligation at the time of the renewal; or
- the interest rate is increased based on a variable rate feature that had not been properly disclosed when the loan was made.

See the section below on **Taking Steps to Document a Renewal and Maintaining Priority**, for WBA recommendations to avoid having a renewal note characterized as a refinancing.

The last paragraph just concluded that if the loan is a refinancing – that is, the lender satisfies and replaces an obligation with a new obligation to the same consumer – new disclosures are required. Reg Z includes five exceptions to this rule. Even if the loan meets the definition of a refinancing, new disclosures are not required if the purpose of the new transaction is to:

- renew a single payment obligation with no change in the original terms;
- reduce the APR with a corresponding change in the payment schedule;

- enter into an agreement involving a court proceeding;
- enter into certain agreements resulting from default or delinquency; and
- renew optional insurance purchased by the consumer and added to an existing transaction if the initial purchase of insurance was properly disclosed.

In summary, subject to the two exceptions for adding a variable rate feature to the renewal or having incorrectly disclosed a variable rate feature initially, new consummation disclosures are not required unless the original obligation is satisfied and replaced by a new obligation undertaken by the same consumer. Further, even if the obligation is satisfied and replaced by a new obligation by the same consumer, new disclosures are not required if the new obligation falls within one of the five exemptions listed above.

The right of rescission, which applies to credit transactions in which a security interest is or will be taken in the consumer's principal dwelling, is not required for renewals. However, if the transaction is a refinancing or consolidation by the same creditor of an extension of credit secured by the dwelling, the right of rescission does apply to any new advance of money. Also, for purposes of rescission, if a security interest in a consumer's principal dwelling is added to the transaction, rescission will apply to the addition of the security

interest. Finally, a refinancing by a different lender is always considered a new loan, subject to all of the disclosures and the right of rescission under Reg Z.

2. RESPA.

Although certain disclosures previously required under RESPA are now incorporated into Truth-in-Lending/Reg Z (TRID disclosures), RESPA continues to require the provision of certain other disclosures – for example, the Homeownership Counseling Notice. Subject to certain specific exemptions, RESPA applies to loans secured by first or subordinate liens on residential real estate, including the refinancing of any loan secured by residential real estate. RESPA incorporates the basic Reg Z definition of refinancing. That is, if the loan is satisfied and replaced by a new obligation by the same borrower, the transaction is a refinancing and the RESPA rules applicable to refinancings apply. The RESPA disclosures do not apply if the loan is not satisfied and replaced by a new obligation by the same borrower.

3. HMDA and Regulation C.

A HMDA-reportable financial institution is required to report the renewal of a covered loan only to the extent that it is considered a refinancing. Under HMDA and Reg C, a refinancing means a new, dwelling-secured debt obligation that satisfies and replaces an existing dwelling-secured debt obligation by the same borrower.

If the loan renewal does not satisfy and replace the existing debt obligation, the loan is not a refinancing. This is true under existing HMDA requirements, as well as the new HMDA rules expanding reportable loans which take effect January 1, 2018.

4. Equal Credit Opportunity Act and Regulation B.

Regulation B requires the provision of disclosures and notices, as well as the collection of certain information about applicants. The definition of application under Reg B can include a renewal of credit. As a result, if a consumer applies for the renewal of a loan, lenders must follow applicable Reg B provisions, including the requirement to provide applicants with the “Right to Receive A Copy of Appraisals” for first-lien, dwelling-secured loans for which the lender conducts a new appraisal or valuation on the property. Additionally, adverse action notice requirements must be followed.

Additionally, collection of government monitoring information under Reg B is only required and permitted for applications for the purchase or refinance of a principal dwelling, and not for loan renewals. Thus, monitoring information may only be collected on a renewal application if the renewal is considered a refinancing. As with Reg Z and HMDA, under Reg B, a renewal is not a refinancing unless the debt is satisfied and

replaced by a new obligation to the borrower. Note that even in a refinancing, collection of government monitoring information is optional if it was obtained in an earlier transaction.

5. Privacy.

Privacy notices must be provided to individual customers not later than the time the customer relationship is established. Assuming the notice was properly provided in connection with the original loan (or earlier than that if the individual was already a bank customer), a loan renewal does not trigger the requirement to provide an initial privacy notice.

6. Flood Insurance.

Lenders may not renew any loan secured by improved real estate or a mobile home located in a special flood hazard area unless the property is covered by flood insurance. At the time of loan renewal, lenders must determine whether flood insurance must be placed. A lender should order an updated flood determination for loan renewals, unless it is able to rely on a previous determination. The lender may rely on a previous determination if the determination is not more than seven years old and the basis for determination was recorded on the Standard Flood Hazard Determination Form. Prior determination forms may not be relied upon if map revisions or updates show the property is in a special flood hazard area.

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Regardless of whether an updated flood determination is required at the time of renewal, lenders must provide the Notice of Flood Hazards and Availability of Disaster Relief Assistance to borrowers for any loan renewal secured by improved real estate or a mobile home located in a special flood hazard area.

Wisconsin Consumer Act.

- **Tattletale Notice.** Lenders must notify a non-applicant spouse of an extension of credit if the loan is governed by the Wisconsin Consumer Act (WCA). This disclosure is generally referred to as the tattletale notice. The tattletale notice is not required in connection with the renewal of a loan.
- **Explanation of Personal Obligation.** The WCA does not address disclosures for renewals. The WBA recommends that a lender provide an Explanation of Personal Obligation in connection with renewal notes to any person entitled to an Explanation of Personal Obligation in connection with the initial loan (or provide copies of the documents if that is the way the lender complies with the notice requirement, if applicable, under the WCA).

Taking Steps to Document A Renewal and Maintaining Priority.

When renewing loans, lenders strive to maintain priority on real estate collateral. To maintain priority, lenders want to treat a loan renewal as a continuation of an existing loan rather than a substitution and replacement of the initial loan with a new loan (a refinance). In general, the priority of an optional loan secured by real estate dates from the time of the loan. So, it is important that the date of a loan secured by

real estate remain tied to the initial advance. The lender does not want a court to re-characterize a renewal as a new loan with a new advance date.

When renewing loans, the WBA recommends following procedures to avoid a re-characterization of a renewal loan as a refinancing or a new loan. These procedures include:

1. Clarifying the party's intent that the initial note is renewed by the renewal note and not replaced, by marking the initial note "renewed but not paid" and by retaining the initial note in the file until the obligation has been paid and satisfied.
2. Completing any provision in the renewal note that indicates that the loan renews a prior note by referring to the prior note(s).
3. Recognizing the risk that a loan may more likely be characterized as a refinancing rather than a renewal to the extent that the terms of the renewal note deviate from the terms of the initial obligation. Wisconsin cases have established a doctrine that a renewal of an existing note is not a discharge of an original obligation and the creation of a new obligation, unless it appears that the parties agreed that it should be destruction of the old and the creation of a new obligation. However, the cases address extension of the term, and do not specifically address other amendments made at the time of the renewal loan.

When the terms of the renewal note deviate from the initial note, the lender may decrease the risk of losing priority at the time of renewal by using title insurance to insure continuing priority. For example, an existing title insurance policy may

be brought current with a date down endorsement or other update. Alternatively, a lender could consider obtaining a title search at the time of renewal to determine if there are junior creditors that the lender should consider contacting for consent or a subordination to lender's mortgage. Lenders may choose to be more or less conservative when priority could be affected by the determination of whether a loan is renewed or refinanced.

Charging a Renewal Fee.

Lenders may collect a fee paid in cash by the consumer as a condition to renewing a note. The lender should document the consumer's obligation to pay the fee in writing, perhaps by adding the consumer's agreement to additional provisions in the renewal note or via a separate agreement outside the note. Lenders considering financing renewal fees should consider the consequences. If a renewal fee is financed (rather than paid by the consumer in cash), the lender increases the loan amount. Lenders that increase the loan amount on a renewal note, including by financing fees, without treating the loan as a full refinancing, may have additional disclosure and priority issues and should obtain legal advice as to the consequences. ■

