

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 1 of 12**

*Title 7. Banking and Securities
Part 4. Texas Department of Savings
and Mortgage Lending
Chapter 77. Loans, Investments,
Savings and Deposits
Subchapter A. §77.1, §77.31, §77.72,
§77.74, and §77.94; and,
Subchapter B. §77.115*

The Finance Commission of Texas (the "Commission") adopts amendments to Subchapter A. §77.1, concerning loans authorized, §77.31, concerning loan policies and documentation, §77.72, concerning liquidity, §77.74, concerning local service area investment requirement, and §77.94, concerning subsidiary operations; and, Subchapter B. §77.115, concerning user safety at unmanned teller machines, in conjunction with the Commission's review of Chapter 77.

Sections 77.31, 77.72, 77.94, and 77.115, are adopted without changes to the text as published in the August 22, 2008, issue of the *Texas Register* (33 TexReg 6661-6662), and will not be republished.

Sections 77.1 and 77.74 are adopted with changes to the text as published in the August 22, 2008, issue of the *Texas Register* (33 TexReg 6661-6662), and are being republished.

In general, the purpose of the amendments is to conform the rules to the Department's current practice, to eliminate obsolete provisions, and to add clarification. Sections 77.1, 77.31, 77.72, 77.74, and 77.94 have been revised to clarify current practice. Section 77.115 has been revised to correct the Department's name.

The 30-day comment period ended September 22, 2008, during which we received various comments regarding the proposed rule amendments. A summary of the comments relating to the proposed amendments and the Department's responses follows.

Comment: The update to loan policies and general documentation in 7 TAC §77.31 (1) regarding the dating of the signature on a loan application was questioned regarding telephone applications.

Response: The Department notes that even in a telephone application, a signature must eventually be obtained, and can therefore then be dated.

Comment: The expansion of local service area investments to include local consumer installment loans received a comment regarding several aspects of the proposed amendment. The Department proposed adding a definition of local consumer installment loans to 7 TAC §77.1. The commenter suggested that the definition was not necessary due to the fact that those type of loans would already fall under existing definitions of personal property loans or unsecured loans. The proposed description of the added loan types as local consumer installment loans was suggested to be changed to consumer loans. The commenter suggested that the Department also add small business loans to the local service area investments of 7 TAC §77.74.

Response: The Department agrees that the definition is not needed in 7 TAC §77.1. Regarding the other

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 2 of 12**

comments, the Department has concluded that in order to conform to statute at *Finance Code* §94.201 (6), the exact wording from that section of statute will be added to the rule at 7 TAC §77.74 (6). This responds to all of the comments and broadens the scope of local service area in the rule to the exact scope to which the statute was expanded in 2005.

The amendments are proposed under Texas Finance Code §11.302, which authorizes the Commission to adopt rules to enforce Title 3 of the Texas Finance Code.

The statutory provisions affected by the proposed amendments are contained in Texas Finance Code, Chapters 94 and 95.

Subchapter A. Authorized Loans and Investments.

§77.1. Loans Authorized.

(a) A savings bank may originate, invest in, sell, purchase, service, participate, or otherwise deal in (including brokerage or warehousing) the following types of loans or participations, subject to the limitations of this subchapter:

(1) residential real estate loans, including loans on the security of leasehold interests in residential real estate, in accordance with §77.3 of this title (relating to Residential Real Estate Loans);

(2) home improvement loans, in accordance with §77.4 of this

title (relating to Home Improvement Loans);

(3) manufactured home loans, in accordance with §77.5 of this title (relating to Manufactured Home Loans);

(4) interim construction loans, in accordance with §77.6 of this title (relating to Interim Construction Loans);

(5) other real estate loans, including loans on the security of leasehold interest in real estate, in accordance with §77.7 of this title (relating to Other Real Estate Loans);

(6) personal property loans, in accordance with §77.8 of this title (relating to Personal Property Loans);

(7) commercial real estate loans, including loans on the security of leasehold interest in real estate, in accordance with §77.9 of this title (relating to Commercial Real Estate Loans);

(8) non-real estate commercial loans, in accordance with §77.10 of this title (relating to Non-Real Estate Commercial Loans);

(9) loans fully secured by savings accounts owned or otherwise pledged for or by the borrower;

(10) unsecured loans, in accordance with §77.11 of this title (relating to Unsecured Loans);

~~(11) local consumer installment loans which are made for~~

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 3 of 12**

~~personal, family, or household purposes, including loans fully secured by savings accounts owned or otherwise pledged for or by the borrower; and~~

(11) ~~(12)~~ loans which are insured or guaranteed by the United States or any instrumentality thereof.

(b) A savings bank may purchase or commit to purchase any loan it could make if it were incorporated and operating as a federal savings bank domiciled in this state, so long as for each such transaction the savings bank complies with all applicable regulations governing such activities by federal savings banks. However, all such loans must be documented in accordance with the applicable requirements of this chapter.

§77.31. Loan Policies and Documentation.

(a) Each savings bank shall establish written policies approved by its board of directors establishing prudent credit underwriting and loan documentation standards. Such standards must be designed to identify potential safety and soundness concerns and ensure that action is taken to address those concerns before they pose a risk to the association's capital. Credit underwriting standards should consider the nature of the markets in which loans will be made; provide for consideration, prior to credit commitment, of the borrower's overall financial condition and resources, the financial stability of any guarantor, the nature and value of underlying collateral, and the borrower's character and willingness to repay as agreed; establish a system of

independent, ongoing credit review and appropriate communication to senior management and the board of directors; take adequate account of concentration of credit risk; and are appropriate to the size of the savings bank and the scope of its lending activities. Loan documentation standards should be established and maintained to enable the savings bank to make informed lending decisions and assess risk, as necessary, on an ongoing basis; identify the purpose of the loan and source of repayment, and assess the ability of the borrower to repay the indebtedness in a timely manner; ensure that any claim against a borrower is legally enforceable; demonstrate appropriate administration and monitoring of a loan; and consider the size and complexity of a loan. The following documents are generally appropriate and can be used as a guideline for prudent lending; however, unless such documents are specifically required by other state and federal statutes or regulations, there may be alternative documents equally suitable in satisfying the safety and soundness intent of this section which the savings bank may substitute and still address the safety and soundness concern:

(1) an application for the loan, signed and dated by the borrower or his agent (and if the borrower is a corporation, a board of directors' resolution authorizing the loan), which discloses the purpose for which the loan is sought, the identity of the security property, and the source of funds which will be used to repay the loan;

(2) a statement signed by the borrower or his agent, or a copy of the executed contract, disclosing the

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 4 of 12**

actual price at which the security is being purchased by the borrower, if the loan is made for the purpose of financing the purchase of the security for the loan;

(3) current financial statements signed by the borrower and all guarantors and/or current documented credit reports disclosing the financial ability of the borrower and guarantors (a current financial statement is as of a date within 180 days before the application is filed) together with written certification by the borrower and guarantors that no material adverse changes in financial condition have occurred since the financial statement was prepared;

(4) a loan approval sheet (which may be part of the loan application form) indicating the amount and terms of the loan, the date of loan approval, by whom approved, the signatures of the persons approving the loan, any conditions of approval, and verifying that the persons approving the loan have confirmed applicable loan-to-one-borrower limitations are met;

(5) a loan disbursement statement or other documentation, indicating the date, amount, and ultimate recipient of every disbursement of the proceeds of such loan (this requirement is not met by showing one or more disbursements to a title company or other escrow agent, but for a construction loan, this requirement may be met by documenting bona fide construction draw disbursements to the general contractor of the project, upon his completion of an affidavit stating that all bills for labor and materials have been paid as of the date of the disbursement);

(6) a loan settlement statement, indicating in detail the expenses, fees, and charges the borrower or borrowers have paid in connection with such loan;

(7) the promissory note or notes containing the borrower's obligation to repay duly executed by the borrower and all guaranty agreements duly executed by the guarantors (a copy of the note or notes may be kept in the loan file, if the original notes are stored for safekeeping in another location at the savings bank);

(8) the original mortgage, deed of trust, or other instrument creating or constituting the lien securing the loan;

(9) for real estate loans, an attorney's opinion letter based on an abstract of title, or a policy of title insurance, or binder of same, issued by a title company authorized to insure titles in the state in which the security for the loan is located, showing that the lien securing such loan meets the applicable requirements of this chapter for liens securing the loan in question;

(10) evidence that the insurable improvements of the real estate are insured against loss by a fire and extended coverage policy or its equivalent issued by an insurance company authorized to do business in the state in which the real estate security is located and naming the savings bank as a co-insured, as its interest may appear;

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 5 of 12**

(11) for real estate loans in which the transaction value exceeds \$250,000, a professional appraisal report by an appraiser or committee of appraisers, who may be employees of the savings bank, is required. Reappraisals may be required by the commissioner on real estate or other property or interests therein securing loans, at the expense of the savings bank, when the commissioner has reason to believe the value of the security is overstated for any reason. The appraisal report shall be in writing and in a form approved by the American Institute of Real Estate Appraisers, the Society of Real Estate Appraisers, the Federal Home Loan Mortgage corporation, the Federal National Mortgage Corporation and shall be signed by the appraiser or committee of appraisers. In case of renewal of a loan where additional funds are advanced by the savings bank, a written certification of current value by the original appraiser or an acceptable substitute shall satisfy this subsection;

(12) for personal property loans, a detailed explanation of how the savings bank arrived at the appraised or market value of the security property;

(13) any loan agreement or other ancillary documents relating to the loan; and

(14) any documents required by the Texas Credit Code, Title 4 of the Finance Code.

(b) Smaller loans in an amount less than \$50,000 would generally be expected to meet more limited documentation guidelines of subsection (a)(1)-(8) of this section. Further,

§77.4(c) and §77.5(d) of this title (relating to Home Improvement Loans and Manufactured Home Loans) provide additional documentation guidelines for making home improvement or manufactured housing loans.

(c) Documentation guidelines for unsecured loans under this chapter would generally include the documents in subsection (a)(1) and (3)-(7) of this section.

(d) Loan documentation which meets the documentation requirements of the applicable agency meets the requirements of this section for any loan of which at least 80% of the principal is guaranteed by the United States or any agency or instrumentality thereof, or which is guaranteed in any amount by the Veteran's Administration, Federal Housing Administration, or Farmer's Home Administration.

(e) A savings bank may designate as escrow agent an attorney or a title company, either of which must be duly licensed in the state where the transaction is closed. However, where an escrow agent is used, all original documents shall be forwarded to the savings bank within five business days after closing, or immediately after recording, for those documents which require filing of record.

(f) Permanent Loan File Requirements.

(1) Loan documentation shall be in the possession of the savings bank or an escrow agent designated by the savings bank before funding, together with a signed certification by an officer or employee that the loan

documentation was complete before funding and such documents and records shall be placed in one permanent loan file immediately upon receipt by the savings bank.

(2) The permanent loan file required by this section shall be located at an office of the savings bank. Duplicate loan files or other files containing loan documentation not required by this rule may be maintained at the savings bank's discretion. Files for loans which are fully secured by accounts at the savings bank may be maintained at the office where the loan was originated.

(3) The permanent loan file shall contain evidence that the savings bank obtained the prompt recording in the proper records of every mortgage, deed of trust, or other instrument creating, constituting or transferring any lien securing in whole or part any loan made under this chapter, or the savings bank's interest therein. This requirement shall not apply to loan participations purchased by the savings bank.

(4) Where the proceeds of a loan are disbursed over the term of the loan in the form of draws by the borrower, the documentation supporting each draw shall be part of the permanent file.

(5) When a savings bank purchases whole loans or participations in loans, it shall cause the assignment or transfer of its interest in the liens securing such loans to be in recordable form and maintained in the permanent file. If such loans are serviced by others,

the servicing agreement shall be a part of the permanent file. The savings bank shall obtain a certification from the seller of the loan or participation that the seller is in possession of all documents required by this section.

(g) The records of the savings bank shall reflect that the board of directors has by appropriate resolution established procedures for the approval of all loans, loan commitments or letters of credit made by the savings bank and specifically fixing the authority and responsibility for preliminary loan approval by officers and employees of the savings bank. Loans originating in branch offices, loan offices, or agencies shall be approved in the same manner as loans originating in the principal office.

(h) A savings bank shall maintain a register of all outstanding loan commitments, including commitments to purchase loans or participations, containing the name and address of the customer to whom the commitment is made, dollar amount of the commitment, and a summary of all material terms of the commitment, with a description of any written documents evidencing the loan commitment.

§77.72. Liquidity.

A savings bank shall maintain liquidity in an amount not less than 10% of an amount equal to its average daily deposits for the most recently completed calendar quarter in cash or readily marketable investments. The term "cash" shall include unpledged demand accounts in other federally insured depository institutions, a Federal Home Loan or Federal Reserve Bank. Whether

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 7 of 12**

a security is readily marketable must be determined on an individual security basis; however, to be eligible for inclusion in "readily marketable investments" category:

(1) the security must be a permissible investment under §77.71 of this title (relating to Investment in Securities);

(2) the security must not be pledged or otherwise encumbered;

(3) there must be an organized, regularly available market for exchange of the security; and

(4) a sale of the security must settle (convert to cash) in the market within five business days or less. U.S. government or agency securities meet these requirements, including Federal Home Loan Bank stock. Private issue securities with a AAA or AA rating normally meet these criteria as well.

§77.74. Local Service Area Investment Requirement.

(a) A savings bank shall maintain an amount equal to at least 15% of its local service area deposits invested in the following categories of assets and investments:

(1) first and second lien residential mortgage loans or foreclosed residential mortgage loans originated from within the savings bank's local service area;

(2) home improvement loans;

(3) interim residential construction loans;

(4) mortgage-backed securities secured by loans from within the savings bank's local service area;

(5) loans for community reinvestment purposes; and

(6) other loans made to customers in the savings bank's local service area that meet the definition of qualified thrift assets under Section 92.204 ~~local consumer installment loans.~~

(b) The board of directors of each savings bank shall approve at least annually the definition of the institution's local service area which shall incorporate the primary area, or areas from which the institution receives savings deposits. At the time a savings bank is chartered or converts into a savings bank, a savings bank may seek approval from the commissioner of the definition of its local service area and unless otherwise agreed to by the institution and the commissioner, the savings bank may rely on this definition for the duration of its corporate existence as a savings bank.

(c) For purposes of identifying qualifying loans and investments under subsection (a) of this section.

(1) Mortgage-backed securities shall include mortgage-backed bonds, mortgage pass-through securities, collateralized mortgage obligations, and such other securities approved by the commissioner which are collateralized by first or second lien residential mortgages.

(2) It shall be the responsibility of each institution to provide such information and evidence necessary to identify particular mortgage-backed securities as being secured by loans from within the institution's local service area such as the originator, the originator/servicer or such other information as may identify the underlying loans as being from the institution's local service area.

(3) Loans and investments described in subsection (a) of this section may include first and second lien residential mortgage loans and home improvement loans or residential construction loans originated from within the institution's local service area and sold by the institution or any subsidiary (including finance subsidiaries) of the savings bank within the preceding 12 months.

(d) Upon application by a savings bank, the commissioner may grant a limited term waiver from the requirements of subsection (a) of this section. Such application must include information and evidence that quality loans in the categories described in subsection (a) of this section are not available from within the institution's local service area.

§77.94. Subsidiary Operations.

(a) The savings bank shall obtain prior written approval of the commissioner for the establishment and location of the main office, and any branch office, agency office, or any other office or facility of the corporation,

and for any change of name of the subsidiary.

(b) A verified copy of all contracts, instruments, joint ventures, and partnership agreements and financing arrangements of the subsidiary investments shall be furnished to the savings bank within 30 days from date of execution.

(c) The corporation agrees to furnish, at the expense of the corporation or savings bank, an independent appraiser's report or other expert opinion as determined to be necessary by the commissioner for the purpose of establishing the value of any investments made by the corporation.

(d) Each corporation shall maintain bond coverage with an acceptable bonding company in an amount to adequately cover each director, officer, employee, and agent who has access to cash or securities of the corporation. Such bond amount shall be in an amount equivalent to 1.0% of total assets but in no event shall be less than \$25,000 nor more than \$2 million. In lieu of a separate surety bond for the corporation, the savings bank may obtain an extension rider to the surety bond coverage of the parent savings bank.

(e) All directors of the savings bank and corporation shall furnish affidavits fully disclosing any direct or indirect interest they may have in each investment made by the corporation.

Subchapter B. Savings and Deposits.

§77.115. User Safety at Unmanned Teller Machines.

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 9 of 12**

(a) Definitions. Words and terms used in this section that are defined in the ATM User Safety Act, §1, have the same meanings as defined in the ATM User Safety Act. The following words and terms when used in this section shall have the following meanings, unless the context clearly indicates otherwise.

(1) Access device--A card, code, or any combination thereof, or other means of access, to a customer's account at a financial institution, that may be used by the customer to initiate a transaction at an ATM.

(2) ATM--A machine, sometimes referred to as an unmanned teller machine or remote service unit, other than a night depository, a telephone, or a customer convenience terminal, capable of being operated solely by a customer, by which a customer may communicate to the financial institution:

(A) a request to withdraw money directly from the customer's account or from the customer's account pursuant to a line of credit previously authorized by the financial institution for the customer;

(B) an instruction to deposit funds into the customer's account with the financial institution;

(C) an instruction to transfer funds between one or more accounts maintained by the customer with the financial institution but not as between the customer's account and an account maintained in the financial institution or in some other financial institution by some other customer;

(D) an instruction to apply funds against an indebtedness of the customer to the financial institution;

(E) a request for information concerning the balance of the account of the customer with the financial institution; or

(F) any other form of transaction a customer may conduct at an ATM using an access card.

(3) ATM User Safety Act--Texas Civil Statutes, Article 342-903d, as enacted by Act of May 27, 1995, 74th Legislature, Chapter 647, 1995 Texas Session Law Service 3528.

(4) Customer convenience terminal--A particular kind of unmanned teller machine, the use of which does not involve personnel of a financial institution by which:

(A) a customer of a financial institution can authorize and effect the electronic transfer of funds from the customer's account at the financial institution in order to obtain cash or purchase or rent or pay for goods or services or both; and

(B) the merchant can ascertain that the transaction has been completed and the funds have been or will be transferred to the merchant's account at the merchant's financial institution.

(5) Department--The Texas Department of Savings and Mortgage Lending.

(b) Measurement of Candle foot Power. For purposes of measuring

compliance with the ATM User Safety Act, §3, candle foot power should be determined under normal, dry weather conditions, without complicating factors such as fog, rain, snow, sand or duststorm, or other similar condition.

(c) Leased Premises.

(1) Noncompliance by Landlord. Pursuant to the ATM User Safety Act, §3(c), the landlord or owner of property is required to comply with the safety procedures of the ATM User Safety Act if an access area or defined parking area for an ATM is not controlled by the owner or operator of the ATM. If an owner or operator of an ATM on leased premises is unable to obtain compliance with safety procedures from the landlord or owner of the property, the owner or operator shall notify the landlord in writing of the requirements of the ATM User Safety Act and of those provisions for which the landlord is in noncompliance.

(2) Enforcement. Noncompliance with safety procedures required by the ATM User Safety Act by a landlord or owner of property after receipt of written notification from the owner or operator constitutes a violation of the Act, which may be enforced by the Texas Attorney General.

(d) Safety evaluations.

(1) The owner or operator of an ATM shall evaluate the safety of each machine on a basis no less frequently than annually.

(2) The safety evaluation shall consider at the least the factors

identified in the ATM User Safety Act, §4.

(3) The owner or operator of the ATM may provide the landlord or owner of the property with a copy of the safety evaluation if an access area or defined parking area for an ATM is not controlled by the owner or operator of the machine.

(e) Notice.

(1) Existing Accounts. No later than January 1, 1996, an issuer of access devices shall furnish its customers with a notice of basic safety precautions that each customer should employ while using an ATM. The notice may be included as a statement stuffer with another mailing or may be delivered personally or mailed to each customer whose mailing address is in this state and who has been issued an access device.

(2) New Access Devices. An issuer of access devices shall furnish its customer with a notice of basic safety precautions at the time the initial disclosure of terms and conditions is provided to such customer.

(3) Annual Notice. After January 1, 1996, an issuer of access devices shall furnish its customers with a notice of basic safety precautions on a basis no less frequently than annually.

(4) Content. The notice of basic safety precautions required by this subsection must be provided in written form which can be retained by the customer and may include recommendations or advice regarding:

**PROPOSED ADOPTION OF AMENDMENTS TO 7 TAC
CHAPTER 77, SUBCHAPTERS A and B
Page 11 of 12**

(A) security at walk-up ATMs;

(B) security at drive-up ATMs;

(C) protection of code or personal identification numbers;

(D) procedures for lost or stolen cards;

(E) reaction to suspicious circumstances;

(F) safekeeping and disposition of ATM receipts, such as the inadvisability of leaving an ATM receipt near the ATM;

(G) the inadvisability of surrendering information about the customer's access device over the telephone;

(H) safeguarding and protecting of the customer's access device, such as a recommendation that the customer treat the access device as if it was cash;

(I) protection against ATM fraud, such as a recommendation that the customer compare ATM receipts against the customer's monthly statement; and

(J) other recommendations that the issuer reasonably believes are appropriate to facilitate the security of its ATM customers.

(f) Video Surveillance Equipment. Video surveillance

equipment is not required to be installed at all ATMs. The owner or operator must determine whether video surveillance or unconnected video surveillance equipment should be installed at a particular ATM site, based on the safety evaluation required under the ATM User Safety Act, §4. If an owner or operator determines that video surveillance equipment should be installed, the owner or operator must provide for selecting, testing, operating, and maintaining appropriate equipment.

(g) ATMs Located in a Savings Bank Vestibule. The provisions of the ATM User Safety Act and this section are applicable to an ATM located in a savings bank vestibule if there is 24-hour access to the vestibule from outside the building.

(h) Certification of Compliance. The security officer of each depository shall certify compliance with the ATM User Safety Act and this regulation on a basis no less frequently than annually.

(i) Mandatory Compliance Date. Subject to the exemption provided by ATM User Safety Act, §6, compliance with the safety requirements of the ATM User Safety Act and this section is required not later than September 1, 1996.

Certification

This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's legal authority to adopt.

Issued in Austin, Texas on October 17, 2008.

Jane Black

General Counsel

Department of Savings and Mortgage
Lending