

Insights

September/October Hoosier Banker: Waiving HELOC Closing Costs ‐ While keeping line of credit open

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Question: *Our chief lending officer wants to run a new promotion waiving all closing costs on home equity lines of credit, but is concerned that borrowers will pre-pay the loan before the bank recoups the cost of origination. Does Indiana law permit us to waive closing costs, conditioned upon keeping the line open for a certain period of time?*

Answer: Yes, although until very recently this practice was not allowed under Indiana law. While banks may waive fees at their discretion, conditioning the waiver on a borrower's keeping the line of credit open for a time certain fell within the scope of a "prepayment penalty" under the Indiana Uniform Consumer Credit Code.¹ Specifically, Ind. Code § 24-4.5-3-209(1) provided: "Subject to the provisions on rebate upon prepayment (section 210 of this chapter), the debtor may prepay in full the unpaid balance of a consumer loan, refinancing, or consolidation at any time without penalty. With respect to a consumer loan that is primarily secured by an interest in land, a lender may contract for a penalty for prepayment of the loan in full, not to exceed two percent (2%) of any amount prepaid within sixty (60) days of the date of the prepayment in full, after deducting all refunds and rebates as of the date of the prepayment. However, the penalty may not be imposed: (a) if the loan is refinanced or consolidated with the same creditor; (b) for prepayment by proceeds of any insurance or acceleration after default; or (c) after three (3) years from the contract date." The charging of closing costs only when a borrower prepaid a loan would fall within the scope of the prior statute.

House Enrolled Act 1539 became effective on July 1. Among other provisions, it added new language to Ind. Code § 24-4.5-3-209(1) that provides: "For purposes of this section, the collection of the amount of any conditionally waived closing costs (as allowed under section 202(d) of this chapter) by a creditor, as stipulated in the loan agreement, at the time of prepayment in full does not constitute a prepayment penalty and is not subject to the limitations set forth in this subsection."

While this practice is no longer considered a prepayment penalty under Indiana law, be careful to ensure that the conditional nature of this fee waiver is clearly disclosed to the borrower. Clear disclosure can help avoid potential liability for violations of Section 5(a) of the Federal Trade Commission Act,² or of the Unfair, Deceptive, or Abusive Act or Practice under Section 1031 of the Dodd-Frank Act.

¹ Ind. Code § 24-4.5

² 15 USC §45