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DEPARTMENT OF BUSINESS REGULATION
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ADVISORY RULING #60
OCTOBER 30, 1981

(Repealed - See AR #60-A)

October 30, 1981

Dear

You have asked me to clarify the exemption for first mortgage loans in Section 1-202(8) of The Maine Consumer Credit Code. You are correct in your understanding that the exemption in the Code is not limited to "purchase money" first mortgage loans. The exemption is for any first lien mortgage secured by an interest in land (other than a mobile home loan) granted by a supervised financial organization, but note the "circumvention or evasion" language. You described three examples in your letter and ask whether or not they are exempt from the Code.

In the first example, the applicant applies for a loan to pay college tuition and offers as security for the loan a first lien mortgage on his or her personal residence. In this transaction, assuming it is granted by a supervised financial organization, the first lien mortgage would be exempt from the Code. The purpose for the loan is not controlling.

In example two, the applicant applies for a loan in part for personal debt consolidation and in part for home improvement. You propose that as security for this loan, the bank would utilize the existing first mortgage, which contains an "open-end feature or what is also referred to as a future advance clause." The Bureau does not believe that the transaction that you describe in this example is exempt from the Code. A transaction subsequent to a purchase money first mortgage loan, and which subsequent transaction merely references the previous first mortgage as a security interest, does not qualify in our opinion. There are two reasons for this position.

The first reason is that we believe that the "circumvention or evasion" language of Section 1-202(8) is applicable to this type of transaction. We believe that the real estate exemption in the Code should not be available for a transaction which is primarily a consumer loan and secured by real estate for the purpose of evading the Code's regulation. In this situation, the first mortgage has already been granted and the Code's exemption stops at that point.

The second reason is derived from an analysis of a recent decision by the Maine Supreme Court, Becker v. Canal National Bank, (July 3, 1981). In that case, the Court analyzed the use of a future advance clause by a bank in a commercial transaction. The Court suggested serious concerns with the use of the so-called "dragnet" clause. The Court observed:

"Furthermore, while a dragnet clause in a mortgage can properly serve purposes of commercial convenience, it may also be a trap for the unwary. A dragnet clause often, as in the instant case, is included in standard mortgage forms drafted by the mortgagee. The mortgagor may well be unaware of either its presence or its implications. See First Security Bank of Utah v. Shiew, 609 P. 2nd 952, 954 (Utah, 1980). Mortgages containing future advances clauses 'have been denominated anaconda mortgages and are well named thus, as by their broad and general terms they enwrap the unsuspecting debtor in the folds of indebtedness embraced and secured in the mortgage which he did not contemplate...' Berger v. Fuller, 180 Ark, 372, 377, 21 S. W. 2nd 419, 421 (1929). A literal interpretation of the clause would allow the bank to turn to the real estate subject to the mortgage any time the mortgagor falls behind on a personal loan, misses a payment on an automobile loan, or overdraws his checking account at the bank. Wong v. Beneficial Savings & Loan Association, 56 Cal. App. 3rd 286, 128 Cal. Rptr. 338, 342 (1976)." (Footnotes deleted.)

Because of the circumvention or evasion language of the Code and the reasoning in the Becker case, the Bureau will treat the exemption in 1-202(8) of the Code as applying to future advances in an existing first mortgage only in the following situation: when the amount of the future advance is added to the balance owed on the first mortgage and the terms and conditions of the first mortgage are thereby applied to this future advance.

The third example you give is for an individual who desires to apply for a loan to consolidate personal debts. The individual offers as security a first mortgage on a piece of land which contains no buildings. Again, the exemption in the Code is applicable. A first mortgage on real estate does not require a personal residence in order to qualify.

Certain other provisions of the Code should be highlighted with respect to the regulation of real estate transactions:

- (1) 9-A M.R.S.A. § 1-301(14)(B)(ii) exempts transactions, no matter the lien status, secured by an interest in real estate if the finance charge does not exceed 12¼%;
- (2) The dollar amount which currently defines a consumer loan or credit sale (\$45,000) is not applicable to a real estate transaction. See 9-A M.R.S.A. § 1-301 (11)(A)(v) and (14)(A)(iv).

(3) Article VIII - Truth in Lending is applicable to all the consumer transactions which may be exempt from the Code by virtue of its lien status or interest rate. Note, as well, that the right of rescission is applicable to any real estate transaction secured by the principal residence of the consumer and not made for purchase or acquisition. The lien status is not controlling. See 9-A M.R.S.A. § 8-204.

We appreciate your consultation with us on this important issue. Should you have any further questions, please do not hesitate to contact me.

Sincerely,

/s/ Barbara R. Alexander

Barbara R. Alexander
Superintendent

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