

INTERPRETIVE LETTER 96-1 (JANUARY 24, 1996)

State bank's home equity line of credit is a revolving credit plan pursuant to the Financial Services Development Act (IFSDA). Early Cancellation Fee is a "charge which may be provided in the agreement between the Bank and customer. Interest Act provisions do not limit revolving credit plans pursuant to IFSDA.

This letter responds to your inquiry made to the Commissioner of Banks and Trust Companies ("Commissioner") on behalf of an Illinois state-chartered bank ("Bank"). The issues you raise are: 1) whether Bank's home equity line of credit is a "revolving credit plan" as defined by the Illinois Financial Services Development Act ("IFSDA"), 205 ILCS 675/1 et. seq. (1994); and if so, 2) whether the "Early Cancellation Fee" (described below) included in the line of credit agreement is prohibited under either the IFSDA or the Interest Act, 815 ILCS 205/1 et. seq. (1994). It is the position of the Commissioner that Bank's home equity line of credit is a "revolving credit plan" under the IFSDA and the Early Cancellation Fee is not prohibited by either the IFSDA or the Interest Act.

Bank uses the "Home Equity Agreement and Disclosure" form ("Agreement") purchased from the commercial forms vendor CFI, ProService to document home equity loans or home equity lines of credit. The Agreement is sold under the registered trademark name Laser Pro. The Agreement terms provide a borrower a revolving line of credit requiring minimum monthly payments of accrued interest on any outstanding principal balance. Any outstanding principal balance becomes payable in full upon the expiration of the line of credit term or upon cancellation or termination of the line of credit. The borrower may make payments to reduce the outstanding principal balance, in full or in part, or any other amount owing at any time without penalty. However, if the line of credit account is cancelled or terminated during the first 24 months of the term of the Agreement, the Agreement provides that Bank may charge the borrower an "Early Cancellation Fee." The Early Cancellation Fee is listed under the heading "Conditions Under Which Other Charges May be Imposed" as a part of "Other Charges." The amount of the charge is \$300 if the maximum line balance is \$100,000 or less, otherwise the charge is \$500. The borrower may unconditionally cancel the line of credit according to the Agreement, at which time all principal, accrued interest and charges become due, including the Early Cancellation Fee if the borrower closes the account within the first 24 months. The Early Cancellation Fee will not be assessed if Bank exercises its rights under the Agreement and cancels or terminates the line of credit within the first 24 months.

Home Equity Lines of Credit Qualify as a Revolving Credit Plan under the IFSDA
Section 3 of the IFSDA defines a revolving credit plan as: a plan contemplating the extension of credit under an account governed by an agreement between a financial institution and a borrower who is a natural person pursuant to which:

(1) The financial institution permits the borrower . . . from time to time . . . to obtain loans by any means whatsoever . . .;

(2) the amounts of such . . . loans are charged to the borrower's account under the revolving credit plan;

(3) the borrower is required to pay the financial institution the amounts of all . . . loans charged to such borrower's account under the plan but has the privilege of paying such amounts outstanding from time to time in full or installments; and

(4) interest may be charged and collected by the financial institution from time to time on the outstanding unpaid indebtedness under such plan. (205 ILCS 675/3(b)).

The Agreement used by Bank in documenting home equity lines of credit provides a borrower the rights and obligations described above in a revolving credit plan. The Agreement allows a borrower to obtain loans and pay these loans down in installments or in full without penalty. Bank issues home equity lines of credit possessing the same characteristics as a revolving credit plan defined above. Therefore, a home equity line of credit will be considered a revolving credit plan when the home equity line of credit, by the terms of the agreement between the bank and the borrower, comply with the definition in Section 3 of IFSDA.

The Early Cancellation Fee is Not Prohibited by the IFSDA or the Interest Act Section 4 of the IFSDA states that: Notwithstanding the provisions of any other laws in connection with revolving credit plans, any financial institution may . . . offer and extend credit under a revolving credit plan to a borrower and in connection therewith may charge and collect interest and other charges, may take real and personal property as security therefore and may provide in the agreement governing the revolving credit plan for such other terms and conditions as the financial institution and the borrower may agree upon from time to time. . . . (205 ILCS 675/4).

The term "other charges" is not defined or limited in Section 4. Section 6 of the IFSDA provides examples of possible charges included in a revolving credit plan, stating that: In addition to or in lieu of interest . . . and without limitation of the foregoing Section 4, a financial institution may, if the agreement governing the revolving credit plan so provides, charge and collect as interest, in such manner or form as the plan may provide, an annual or other periodic fee for the privileges made available to the borrower under the plan, a transaction charge or charges, late fees or delinquency charges, returned payment charges or over limit charges and fees for services rendered. 205 ILCS 675/6 (1994).

The charges included in Section 6 of the IFSDA represent examples of allowable charges, but the list is not exclusive. Section 6 of the IFSDA expressly refuses to limit the language in Section 4, thus not restricting the possible "other charges" which a financial institution may collect under a revolving credit plan. Section 4 also makes clear that additional terms of the agreement are allowed if agreed upon by the bank and borrower. The remaining sections of the IFSDA do not address or exclude an Early Cancellation

Charge or similar type of charge. Thus, the IFSDA does not prohibit Bank from charging the Early Cancellation Fee.

The Interest Act does not prohibit the Early Cancellation Fee charged by Bank under the Agreement. Section 4.1 of the Interest Act defines "revolving credit" and states that a revolving credit plan operated in accordance with the IFSDA also qualifies as "revolving credit," but exempts revolving credit plans under the IFSDA from the remaining sections of the Interest Act that govern the terms and conditions of "revolving credit." No other provisions in the Interest Act address either revolving credit plans, Early Cancellation Fees or a similar type of charge, or limit or prohibit an Early Cancellation Fee or similar type of charge.

This interpretation assumes that Bank complies with Section 7 of the IFSDA and the requirements of the federal Truth-in-Lending Act, 15 U.S.C. sec 1601 et seq., in disclosing the Early Cancellation Fee, and how it may apply to a potential borrower.