Government of the District of Columbia

OFFICE OF THE CORPORATION COUNSEL
DISTRICT BUILDING
WASHINGTON, D. C. 20004

IN REPLY REFER TO:

LCD:L&O:IAP
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May 5, 1988

OPINION OF THE CORPORATION COUNSEL

SUBJECT: Does the Interest Rate Ceiling Amendment Act apply to a commercial or investment loan secured by real property, if the borrower moves into the property after the loan is closed?

Ms. Maud Mater
Senior Vice President
General Counsel and Secretary
Federal Home Loan Mortgage Corporation
1759 Business Center Drive
P.O. Box 4115
Reston, Virginia 22090

Dear Ms. Mater:

This is in response to your request, dated June 30, 1987, for the opinion of the Corporation Counsel as to the applicability of § 2(f)(1) of the Interest Rate Ceiling Amendment Act of 1983, D.C. Law 5-62, as amended, D.C. Code § 28-3301(f)(1) (1987 Supp.) ("the act") to certain circumstances arising in connection with the Plan B Mortgage Program ("Plan B") of the Federal Home Loan Mortgage Corporation ("Freddie Mac") under which Freddie Mac purchases loans secured by property containing 5 or more dwelling units.

You have questioned whether the act is applicable to a Plan B loan when a borrower (1) has obtained a Plan B loan for investment purposes, (2) has provided a written statement to the lender that the borrower does not reside at the property used to secure the loan ("secured property") and will not reside at the secured property before the fifth anniversary of the loan closing, and (3) later takes up residence at the secured property

before the fifth anniversary of the loan closing.

It is my understanding that Freddie Mac is concerned about whether in the District a borrower under a Plan B loan can unilaterally negate Freddie Mac's prepayment prohibitions by changing the character of that loan by establishing residence in the secured property after the loan closing but before the fifth anniversary of the loan closing. This concern results from the apparent difference in prepayment provisions of Plan B loans and D.C. Code § 28-3301(f)(1). Prepayment of a Plan B loan is prohibited by the terms of the loan before the fifth anniversary of the loan closing; D.C. Code § 28-3301(f)(1) requires that a loan which is secured by a mortgage on residential property in which the borrower resides permit prepayment after the third anniversary of the loan closing. This concern has resulted in Freddie Mac's ceasing to purchase Plan B loans originating in the District.

Whether a mortgage loan is subject to the provisions of D.C. Code § 28-3301(f) depends on whether the loan falls within the exceptions set forth in D.C. Code § 28-3301(d). That provision reads in relevant part:

> Notwithstanding any other provision of this chapter:
>
> any loan, except a loan which is secured ... by a mortgage or deed of trust on residential real property ... and the residential real property ... is the place of residence of the borrower ... shall not be subject to the provisions of this chapter ... if any of the following conditions are satisfied:
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> ***
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> (B) ... the loan is made for the purpose of acquiring or carrying on a ... commercial activity; or
>
> (C) ... the loan is made for the purpose of acquiring any real property as an investment or for carrying on an investment activity; (Emphasis added.)

D.C. Code § 28-3301(d). This provision was interpreted in an opinion from this Office, dated March 19, 1987, as exempting from the requirements of D.C. Code § 28-3301(f)(1) loans for multifamily properties, such as Plan B loans, which are made for the purpose of carrying on commercial or investment activity unless the borrower resides in the secured property. Moreover, the legislative history of the act indicates that the act was not intended to apply to large commercial purpose loans as are involved here. In particular, the Report of the Committee on Finance and Revenue on Bill 5-193, "Interest Rate Ceiling Amendment Act of 1983" offered the following comments on the exception provisions:

> The committee believes that this treatment will maintain the flexibility needed to negotiate large commercial loans in a changing market place, while offering additional protections to the small businessman who may have to use his home as collateral for the loan.

Report of the Committee on Finance and Revenue, October 20, 1983, p. 5.

Whether a loan falls within the commercial purpose or investment exception of the act is fixed at the time of closing. See In re Jackson, 42 Bankr. 76 (Bankr. D. D.C. 1984) in which the court considered whether a loan was made for a business purpose under the federal Truth-in-Lending Act, 15 U.S.C. §§ 1601, et seq., citing Toy National Bank v. McGarr, 286 N.W. 2d 376, 378 (Iowa 1979):

> The only workable approach is to characterize a loan transaction by the use to which the proceeds are originally placed and maintain the same characterization throughout the life of the loan.*/

Therefore, it is my opinion that a borrower may not avail himself of the prepayment provisions of the District of Columbia Interest Rate Ceiling Amendment Act by moving into the property secured by the loan after the loan is made where the loan is for the purchase or refinancing of a building with five or more dwelling units i.e. commercial or investment property and not a single family home, and the borrower provides written assurances that the secured property is not the borrower's place of residence and is not intended to be his or her place of residence prior to the fifth anniversary of loan closing.

Sincerely,

Frederick D. Cooke, Jr.
Corporation Counsel, D.C.

*/ The Jackson court went on to say that the lender has a heavy burden of proof in establishing an exception from the District's Interest Rate Ceiling Amendment Act, namely: that he relied on a specific exception at the time of making the loan and that he had a basis for such reliance. In re Jackson, supra at 81.