HOMEOWNERS PROTECTION ACT OF 1998

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I. INTRODUCTION

A. Homeowners Protection Act of 1998 (Public Law 105-216) enacted in July is effective July 29, 1999.

B. Like many of our consumer protection statutes this Act resulted from a legislator's personal experience; specifically Utah Congressman James Hanson came to Washington, bought a condominium with PMI and then encountered enormous difficulties in terminating the PMI.

C. The legislative response goes beyond providing for disclosure and rights to cancel, but provides for automatic termination.

D. Unfortunately the Act raises as many questions as it answers and Congress saw fit not to appoint a regulator to implement or interpret the statute.

II. COVERAGE AND STATUTORY FRAMEWORK

A. The Act applies to PMI in connection with residential mortgage transactions.

1. Private Mortgage Insurance is defined to mean any insurance (including mortgage guaranty insurance) against non-payment of a mortgage loan and does include lender paid mortgage insurance. The definition specifically excludes mortgage insurance available under the National Housing Act or the Housing Act of 1949 (i.e. excludes FHA and VA insurance).

2. Residential Mortgage Transaction is defined to mean loans consummated on or after July 29, 1999, to purchase, construct or refinance a primary residence. The law applies to owner-occupied condos, cooperatives and mobile homes, but does not apply to 2-4 family dwellings or home equity lines of credit, and could apply to second mortgages.

B. The Act sets out three triggering events and/or times for lender action: borrower cancellation, automatic termination and final termination.

C. The Act also establishes different rules for "high-risk loans"

III. <u>TERMINATION OF PRIVATE MORTGAGE INSURANCE</u>

A. <u>Borrower Cancellation</u> (Cancellation upon Borrower Request)

1. The requirement for private mortgage insurance must be canceled in connection with a residential mortgage on the cancellation date upon the borrower's request.

a. The "cancellation date" is, at the Borrower's option, the date when the LTV either:

(1) is first scheduled to reach 80% of the original value of the property secured, based solely on the initial amortization schedule, regardless of the actual outstanding balance;

(2) reaches 80% of the original value based solely on actual payments; or.

(The original value is the lesser of sales price as reflected in sales contract or the appraised value at the time the RMT was consummated).

b. With regard to adjustable rate mortgages, the cancellation date is based on amortization schedules or actual payments, at the borrower's option.

2. The PMI need only be canceled on the cancellation date if the mortgagor:

a. submits a request for cancellation in writing to the servicer;

b. has good payment history with respect to the mortgage; and

(1) the term “good payment history” means, with respect to a borrower, that the borrower has not:

(a) made a mortgage payment that was 60 days or longer past due during the 12-month period beginning 24 months before the date on which the mortgage reaches the cancellation date; or

(b) made a mortgage payment that was 30 days or longer past due during the 12-month period preceding the date on which the mortgage reaches the cancellation date.

c. has satisfied any requirements of the holder of the mortgage for:

(1) evidence that the value of property securing the mortgage has not declined below the original value; and

(2) certification that the mortgagor’s equity is not encumbered by a subordinate lien.

B. <u>Automatic Termination</u>

1. A requirement for PMI must terminate with respect to payments made by the mortgagor:

a. on the termination date if mortgagor is current on the mortgage payments; or

b. on the date after the termination date on which the mortgagor becomes current on mortgage payments.

2. The “termination date” is:

a. with regard to fixed rate mortgages the date when the LTV is first scheduled to reach 78% of the original value of the property based solely on the <u>initial</u> amortization schedule, regardless of the actual outstanding balance;

b. with regard to adjustable rate mortgages, the date when the LTV is first scheduled to reach 78% of the original value of the property based on amortization schedules.

C. Final Termination -- If a requirement for PMI is not otherwise canceled or terminated, PMI must not be imposed beyond the first day of the month immediately following the midpoint of the amortization period of the loan if the mortgagor is current on payments.

D. No Further Payments -- No payments may be required for terminated or canceled PMI under this section:

1. in case of borrower cancellation, more than 30 days after the later of;

a. the date on which a request is received; or

b. the date on which the mortgagor satisfies any evidence and certification requirements.

2. in case of automatic termination, more than;

a. 30 days after the termination date, or

b. the date which the mortgagor becomes current on payments required by the mortgage.

3. in case of final termination, more than 30 days after the final termination date.

E. Return of Unearned Premiums

1. In General -- the servicer must return all unearned PMI premiums to the mortgagor not later than 45 days after the termination or cancellation of PMI.

2. Transfer of Funds to Servicer -- the mortgage insurer must transfer any unearned premiums to the servicer not later than 30 days after notification of termination by the servicer.

F. Exceptions for High Risk Loans

1. In General -- The Borrower Cancellation and Automatic Termination provisions do not apply to PMI when at time the mortgage was consummated, the loan is considered "high risk."

    a. In connection with conforming loans ($240,000 or less), high risk loans are to be determined in accordance with guidelines published by Fannie Mae and Freddie Mac.

    b. as determined by the mortgagee in the case of any other mortgage, except that termination must occur:

        (1) Fixed Rate Loan - date on which the LTV is first scheduled to reach 77% of the original value of the Property, regardless of the outstanding balance.

        (2) ARMs - based on amortization schedule when LTV is scheduled to reach 77%.

    c. no good payment history requirement.

2. Termination at Midpoint of the Amortization -- PMI must terminate by the first day of the month immediately following the date that is the midpoint of the amortization period (if the borrower is current on his payments)

3. Rule of Construction -- mortgages need not be purchased by Fannie Mae or Freddie Mac.

IV. DISCLOSURE REQUIREMENTS

Note: These disclosure requirements apply to residential mortgages consummated on or after a date that is 1 year after the enactment of this Act (July 29, 1999).

A. Disclosures for New Mortgages at Time of Transaction -- Disclosure for Non-Exempt Transaction -- In cases where PMI is required for a mortgage (other than a high risk mortgage), at the time at which the transaction is consummated, the lender must provide to the borrower:

1. for a fixed rate mortgage

    a. a written initial amortization schedule; and

b. a written notice;

(1) that the mortgagor may request to cancel PMI on the cancellation date based on the initial amortization schedule

(2) that mortgagor may request cancellation earlier than provided for in the initial amortization schedule, based on actual payments;

(3) that the PMI requirement will automatically terminate on the termination date (and what that date is);

(4) that there are exemptions to the right to cancellation and automatic termination of PMI for high risk loans and whether those exemptions apply.

c. if the transaction relates to any adjustable rate mortgage, a written notice that;

(1) that mortgagor may cancel the requirement for PMI on the cancellation date and that the servicer will notify the borrower when the cancellation date is reached;

(2) PMI will automatically terminate on the termination date, and on that date, the borrower will be notified of the termination or that the requirement will be terminated as soon as the mortgagor is current on loan payments;

(3) that there are exemptions to the right of cancellation and automatic termination of PMI and whether such exemptions apply at that time.

2. <u>Disclosures for Exempt Transactions</u> (High Risk Loans) -- The mortgagee must provide written notice to the mortgagor at consummation that in no case will PMI be required passed the midpoint of the amortization period of the loan, if the mortgagor is current on payments for the mortgage.

3. <u>Annual Disclosures</u> -- If PMI is required in connection with the mortgage transaction, the servicer must disclose to the mortgagor in each such transaction in an annual written statement --

a. the rights of mortgagor to cancellation or termination under the Act; and

b. an address and telephone number that the mortgagor may use to contact the servicer to determine whether the borrower may cancel.

B. Disclosures for Existing Mortgages -- If PMI was required in connection with a residential mortgage entered into at any time before July 29, 1999, the servicer must disclose to the mortgagor in an annual written statement—

1. that PMI may, under certain circumstances, be canceled by the mortgagor (with the consent of the mortgagee and in accordance with applicable State law; and

2. an address and telephone number that the mortgagor may use to contact the servicer to determine if they may cancel PMI.

C. Inclusion in Annual Notices -- Disclosure information may be provided in an annual statement concerning escrow accounts required under the Real Estate Settlement Procedures Act or as part of annual disclosures of interest required by the IRS.

D. Standard Forms -- The mortgagee or servicer may use standard forms for these disclosures.

V. NOTIFICATION UPON CANCELLATION OR TERMINATION

A. In General -- not later than 30 days after the date of cancellation or termination of PMI, servicer must notify the mortgagor in writing:

1. that the PMI has terminated;

2. that no other premiums, payments or fees are due.

B. Notice of Grounds --

1. In General -- if the servicer determines that the borrower did not meet the requirements for termination or cancellation, it must provide written notice of the grounds relied on to make the determination that PMI should not be canceled (e.g. appraisal).

2. Timing -- generally notice of grounds must be provided with respect to:

a. cancellation of PMI, not later than 30 days after the later of the date on which the borrower's request was received or the date on which the mortgagor satisfies any evidence and certification requirements with respect to termination of PMI;

b. termination of PMI, not later than 30 days after the scheduled termination date.

VI. DISCLOSURE REQUIREMENTS FOR LENDER-PAID MORTGAGE INSURANCE

A. Notice to Mortgagor -- In case of lender-paid mortgage insurance that is required in connection with a residential mortgage transaction not later than the date on which a loan commitment is made, the prospective mortgagee must provide to the prospective mortgagor a written notice that:

1. lender-paid mortgage insurance differs from borrower-paid mortgage insurance because the former may not be canceled by the mortgagor, while borrower-paid mortgage insurance is cancelable by the mortgagor and could automatically terminate;

2. lender-paid mortgage insurance:

a. usually results in a residential mortgage having higher interest rate than it would in the case of borrower-paid mortgage insurance; and

b. terminates only when the residential mortgage is refinanced, paid off, or otherwise terminated; and

3. that lender-paid PMI and borrower-paid PMI both have benefits and disadvantages, including:

a. a generic analysis of the differing costs and benefits of a residential mortgage transaction with lender-paid vs. borrower-paid PMI over a 10-year period assuming prevailing interest and property appreciation rates; and

b. that lender-paid PMI may be tax deductible (Federal taxes)

B. Not later than 30 days after the termination date that would apply in case of borrower-paid PMI, the servicer must provide a written notice indicating mortgagor financing options that may eliminate the need for PMI.

C. PMI Standard Forms-the servicer may develop and use standard forms for notices to the mortgagor.

VII. FEES FOR DISCLOSURE

No fee or other cost may be imposed on the mortgagor for information or notice with respect to the Act.

VIII. CIVIL LIABILITY

A. In General -- any servicer, mortgagee, or mortgage insurer that violates this Act is liable to the mortgagor to whom the violation relates:

1. in an action by an individual or a class action in which liableparty is not subject to enforcement, any damages sustained, including interest rate, on the amount of the actual damages, accruing from the date on which the violation commences;

2. in the case of:

a. an action by an individual, such statutory damages as the court may allow, not to exceed $2000; and

b. in the case of a class action:

(1) in which the liable party is subject to enforcement, such amount the court may allow, except the total recovery in any class action or series of class actions arising out of the same violation must not exceed the lesser of $5000,000 or one percent of the net worth of the liable party; and

(2) In which the liable party is not subject to enforcement, such amount as court may allow must not exceed $1000 as to

each member of the class, except the total recovery in any class action or series of class actions arising out of the same violation must not exceed the lesser of $5000,000 or 1 percent of the gross revenues of the liable party.

c. Plus costs of the action and reasonable attorney fees.

B. Timing of Actions -- no action may be brought by the mortgagor for civil liability later than 2 years after the date of discovery.

C. Limitation on Liability - failure of servicer to comply because of:

1. failure by mortgage insurer or mortgagee will not be construed as a violation by servicer.

2. Rule of Construction -- no additional requirements will be construed to impose civil liability.

IX. EFFECT ON OTHER LAWS AND AGREEMENTS

A. Effect on State Law -

1. In General -- With respect to any residential mortgage or residential mortgage transaction consummated after July 29, 1998, the provisions of this Act will supersede any provisions of law of any State relating to requirements for obtaining residential mortgage transactions, cancellation or automatic termination of PMI, any disclosure of information addressed by this Act, and any other matter specifically addressed by this Act.

2. Protection of existing state laws

a. In General -- The provisions of this Act do not supersede protected state laws, except to the extent that the protected state laws are inconsistent with any provision of this Act, and then only to the extent of the inconsistency.

b. Inconsistencies -- A protected State law must not be considered to be inconsistent with a provision of this Act if the protected State law-

(1) requires termination of PMI at a date earlier than as provided in this Act or when a mortgage principal balance is achieved that is higher than as provided in this Act.

(2) requires disclosure of information that provides more information required by this Act or more often or at a date earlier than is required by this Act.

3. Protected State Laws -- The term "protected state law" means a State law-

a. regarding any requirements relating to PMI in connection with residential mortgage transactions;

b. that was enacted not later than 2 years after the date of the enactment of this Act; and

c. that such state law was in effect on or before January 2, 1998 concerned residential mortgages.

X. ENFORCEMENT

A. In General -- Compliance with the requirements imposed under this Act must be enforced under the Federal Deposit Insurance Act, the Federal Deposit Insurance Corporation, by the Director of the Office of Thrift Supervision, the Federal Credit Union Act, and part C of Title V of the Farm Credit Act, or any other applicable act.

B. Enforcement and Reimbursement

In carrying out the enforcement activities each agency will notify mortgagee of any failure to comply, require that correction is made with respect to the failure to comply, and require reimbursement with respect to that failure to comply.

Note: GOA Report -- not later than 2 years after the enactment of this act, the Comptroller General of the United States will submit to Congress a report describing the volume and characteristics of residential mortgages.