## Homeowners Protection Act[1]

### Introduction

The Homeowners Protection Act of 1998 (the Act) was signed into law on July 29, 1998, and became effective on July 29, 1999. The Act was amended on December 27, 2000, to provide technical corrections and clarification. The Act, also known as the "PMI Cancellation Act," addresses homeowners' difficulties in canceling private mortgage insurance (PMI)[2] coverage. It establishes provisions for canceling and terminating PMI, establishes disclosure and notification requirements, and requires the return of unearned premiums.

PMI is insurance that protects lenders from the risk of default and foreclosure. PMI allows prospective buyers who cannot, or choose not to, provide significant down payments to obtain mortgage financing at affordable rates. It is used extensively to facilitate "high-ratio" loans (generally, loans in which the loan to value (LTV) ratio exceeds 80 percent). With PMI, the lender can recover costs associated with the resale of foreclosed property, and accrued interest payments or fixed costs, such as taxes or insurance policies, paid prior to resale.

Excessive PMI coverage provides little extra protection for a lender and does not benefit the borrower. In some instances, homeowners have experienced problems in canceling PMI. At other times, lenders may have agreed to terminate coverage when the borrower's equity reached 20 percent, but the policies and procedures used for canceling or terminating PMI coverage varied widely among lenders. Prior to the Act, homeowners had limited recourse when lenders refused to cancel their PMI coverage. Even homeowners in the few states that had laws pertaining to PMI cancellation or termination noted difficulties in canceling or terminating their PMI policies. The Act now protects homeowners by prohibiting life of loan PMI coverage for borrower-paid PMI products and establishing uniform procedures for the cancellation and termination of PMI policies.

### Regulation Overview

#### Scope and Effective Date

The Act applies primarily to "residential mortgage transactions," defined as mortgage loan transactions consummated on or after July 29, 1999, to finance the acquisition, initial construction, or refinancing[3] of a single-family dwelling that serves as a borrower's principal residence.[4] The Act also includes provisions for annual written disclosures for "residential mortgages," defined as mortgages, loans or other evidences of a security interest created for a single-family dwelling that is the principal residence of the borrower (12 USC §4901(14) and (15)). A condominium, townhouse, cooperative, or mobile home is considered to be a single-family dwelling covered by the Act.

The Act's requirements vary depending on whether a mortgage is:

- A "residential mortgage" or a "residential mortgage transaction";
- Defined as high risk (either by the lender in the case of non-conforming loans, or Fannie Mae and Freddie Mac in the case of conforming loans);
- Financed under a fixed or an adjustable rate; or
- Covered by borrower-paid private mortgage insurance (BPMI) or lender-paid private mortgage insurance (LPMI).[5]

### Cancellation and Termination of PMI for Non High Risk Residential Mortgage Transactions

#### Borrower Requested Cancellation

A borrower may initiate cancellation of PMI coverage by submitting a written request to the servicer. The servicer must take action to cancel PMI when the cancellation date occurs, which is when the principal balance of the loan reaches (based on actual payments) or is first scheduled to reach 80 percent of the "original value,"[6] irrespective of the outstanding balance, based upon the initial amortization schedule (in the case of a fixed rate loan) or amortization schedule then in effect (in the case of an adjustable rate loan[7]), or any date thereafter that:

1 This section fully incorporates the examination procedures issued under DSC RD Memo 03-049: Revised Interagency Examination Procedures for the Homeowners Protection Act.

2 The Act does not apply to mortgage insurance made available under the National Housing Act, title 38 of the United States Code, or title V of the Housing Act of 1949. This includes mortgage insurance on loans made the Federal Housing Administration and guarantees on mortgage loans made by the Veterans Administration.

3 For purposes to these procedures, "refinancing" means the refinancing of loans any portion of which was to provide financing for the acquisition or initial construction of a single-family dwelling that serves as a borrower's principal residence. ***See*** 15 USC §1601 *et seq*. and 12 CFR §226.20.

4 For purposes of these procedures, junior mortgages that provide financing for the acquisition, initial construction or refinancing of a single-family dwelling that serves as a borrower's principal residence are covered.

5 All sections of these procedures and Handbook apply to BPMI. For LPMI, relevant sections begin under that heading and follow thereafter.

6 "Original value" is defined as the lesser of the sales price of the secured property as reflected in the purchase contract or, the appraised value at the time of loan consummation. In the case of a refinancing, the term means the appraised value relied upon by the lender to approve the refinance transaction.

7 The Act includes as an adjustable rate mortgage, a balloon loan that "contains a conditional right to refinance or modify the unamortized principal at the maturity date." Therefore, if a balloon loan contains a conditional right to refinance, the initial disclosure for an adjustable rate mortgage would be used even if the interest rate is fixed.