CP 2013-01

HIGHER-PRICED MORTGAGE LOANS (HPMLs)

HIGHER-PRICED COVERED TRANSACTIONS (HPCTs)

Truth in Lending/CFPB Regulation Z [12 C.F.R. 1026.35]

Definition of HPML

A "Higher-priced Mortgage Loan" (HPML or Section 35 Loan) is a mortgage loan that is:

- Secured by the borrower's principal dwelling, *and*

- In the case of a **first-lien** loan that is within the maximum limit eligible for purchase by FreddieMac (*i.e.,* conforming loan limit), the **APR exceeds the Average Prime Offer Rate (APOR) for a comparable transaction by 1.5% or more as of the date the interest rate is locked,** *or*

- In the case of a **first-lien** loan that **exceeds the maximum limit eligible for purchase by FreddieMac** (*i.e.*, "jumbo" loan**)**, the APR exceeds the APOR by **2.5%** or more on the interest rate lock date, *or*

- In the case of a **subordinate-lien** loan, the APR exceeds the APOR by 3.5% or more as of the interest rate lock date

The Average Prime Offer Rates compile mortgages rates on loans with low-risk pricing characteristics from a representative sample of lenders. This calculation differs significantly from Section 32, FannieMae or other State high cost tests in that it evaluates only the APR, and there is no separate points-and-fees limit. The CFPB publishes the APOR tables weekly.

The lock confirmation must be in the file for the investor to verify the interest rate lock date, as the APR is compared to the APOR in effect on the lock date to determine whether or not the loan falls under Section 35. Our failure to include the lock confirmation in the file will delay the loan purchase.

Exemptions

The following loan types are **exempt** from coverage under Section 35:

- Second homes
- NOO rental properties

General HPML Restrictions and Requirements

HPMLs are subject to the following limitations and requirements:

- The monthly P&I payment cannot change during the first four years of the loan,
- Prepayment penalties after the first two years of the loan are prohibited (01-09-14),
- The borrower's ability to repay the HPML must be documented in the file (01-09-14), *and*
- Impounds for property taxes and insurance (including PMI, if required) are required

PRMG HPML Policy and Exceptions

PRMG **will** accept loans meeting the HPML criteria within the parameters of Section 35 of CFPB Regulation Z.

Exceptions

The following loan types **CANNOT** go forward if they hit the Section 35 test threshold:

- **One-year, 3/1 and 5/1 ARMs,** including FHA ARMs
- **Interest-only loan programs**
- **FHA streamline (non-credit-qualifying) refinances**
- **VA IRRRLs (non-credit-qualifying refinances)**
- **Any loan program that does not require or that waives income documentation**
- **Any jumbo loans**

Important Note: A violation of the Section 35 regulations is not curable.

HPML Underwriting/Ability-to-Repay Requirements (01-09-14)

Income/Asset Documentation

1. The borrower's ability to repay the mortgage must be documented in the file, including:
   - Current and reasonably-expected income
   - Employment
   - Assets -- other than the collateral
   - Current obligations and mortgage-related obligations, including property taxes, homeowner's insurance and similar mortgage-related expenses (such as homeowner's association dues)

2. Income or assets that used to determine the borrower's ability to repay must be verified by:
   - W2's
   - Tax returns
   - Payroll receipts
   - Financial institution records, or
   - Other third-party documents that provide reasonably reliable evidence of income or assets

3. Current obligations must be verified.

At the present time, the FullDoc loan programs offered by PRMG should satisfy the HPML/ Section 35 income and asset documentation requirements.

Escrow Accounts

First-lien HPMLs **must** have escrow accounts established at closing for the payment of property taxes and insurance, including hazard, flood and PMI, if applicable.

The mandatory escrow accounts are required on the loan until **all** of the following conditions are met:

- At least five years after consummation of the loan, *and*
- The LTV reaches 80% of the original value of the property, *and*
- The loan is not delinquent or in default

The escrow account provision applies to both Conventional and Government loans. The mandatory insurance escrow requirement does not apply to voluntary insurance premiums elected by the borrower, such as earthquake insurance. Condominium properties that are covered by a master policy are exempt from the insurance escrow requirement; however, property tax impounds must be set up on condo loans.

Residual Income Evaluation Worksheet

All loans that are Higher-priced Mortgage Loans (HPMLs) or Higher-priced Covered Transactions (HPCTs) require the underwriter's completion of a Residual Income Evaluation (RIE) Worksheet demonstrating that the minimum residual income requirements are met.

***A Higher-priced Covered Transaction is a second home or investment property loan that meets the HPML criteria.**

DU Refi Plus

Additional credit score and DTI requirements apply to HPMLs and HPCTs under the DU Refi Plus product:

- Credit score of 620 or more, and
- Debt-to-income ratio of 45% or less

A second level review/signature is required by a Corporate Underwriter or Operations Manager for:

- Owner-occupied credit scores between 620 – 659
- Second home credit scores between 660 – 699
- Non-owner-occupied credit scores between 680 - 699

HPML/Section 35 Test

DocMagic runs the Section 35 calculation at initial disclosure, redisclosure and closing docs. If a loan hits/exceeds the Section 35 ceiling, we will get a [non-fatal] WARNING. It is **critical** that the user verify **two loan terms** in order to proceed with the loan as an HPML because, again, a violation of the Section 35 rules is not curable (*e.g.,* allowing an FHA Streamline or a VA IRRRL or a one-year ARM that qualifies as an HPML escape detection and fund):

1. That the loan is **NOT** done under one of the prohibited programs:
    - **One-year, 3/1 or 5/1 ARM,**
    - **Interest-only product**
    - **FHA streamline refinance,**
    - **VA IRRRL, or**
    - **Jumbo loan**

    If the loan falls under a prohibited program, **we will need to take it out of Section 35**. The interest rate may need to be lowered, since Section 35 evaluates the APR only and does not contain a points-and-fees test. Therefore, we may not be able to get the loan out of Section 35 simply by lowering APR fees.

    Note: Under HUD's Mortgagee Letter 2013-04 effective with FHA case numbers assigned on or after June 3, 2013, the extended annual mortgage insurance premium terms, particularly on smaller purchase prices/loan amounts with LTVs exceeding 90%, will significantly impact the APR.

2. That property tax and insurance impounds are required on the loan.
    - If the loan qualifies under Section 35 and an impound account has not been required or requested, we need to alert the originator/brokers that impounds will be set up.
    - The originator should explain the HPML impound cancellation requirements described above to the borrower.