MGIC

How Mortgage Insurance Works

What Is Mortgage Insurance?

- It’s a financial guaranty that reduces the loss to the lender or investor in the event the borrowers do not repay their mortgage
- It’s also called MI, private MI or PMI

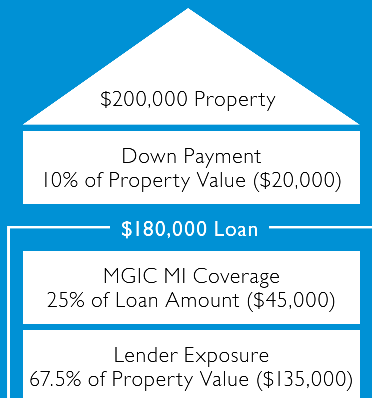
By using MI to reduce risk, the quality of the mortgage as an asset is enhanced. It becomes a safer investment for lenders who keep their loans in portfolio and for investors looking for secure purchases. Even if the borrowers fail to repay, the lender/investor will not suffer a complete loss, but rather, share the loss with the mortgage insurer.

How Does MI Work?

For example:

Consider borrowers who purchase a $200,000 property with a fixed-rate mortgage.

They make a 10% down payment and are required to use MI to finance a $180,000 mortgage.



Typically on a 90% LTV, fixed-rate mortgage, investors require 25% MI coverage. This means that, in the event of a claim, MGIC is responsible for paying 25% of the outstanding balance, leaving the lender at risk for 67.5% of the original property value. (Original property value is the lesser of the property sales price and the appraised value. For a refinance transaction, original value is the appraised value.)

On an uninsured loan, the lender is at risk for the entire loan balance.

If, down the road, these borrowers fail to repay their mortgage, the lender or investor files a claim based on the unpaid loan balance, delinquent interest and foreclosure costs.

There are several settlement options MGIC can elect when paying a claim:

- Percentage Option
- Loss on Property Sale Option
- Acquisition Option
- Anticipated Loss Option

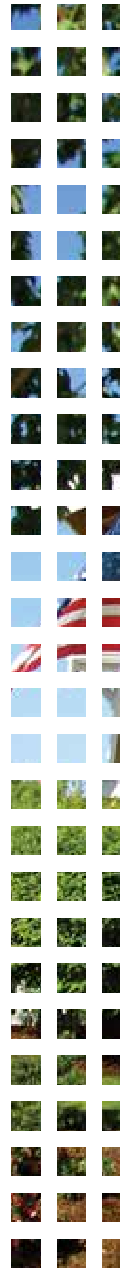
See MGIC's Servicing Guide for details.

RESOURCES

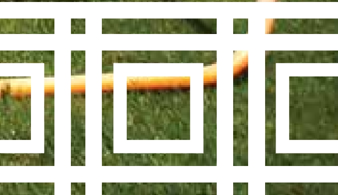
Calculate MGIC MI premiums online at mgic.com/ratefinder; access rate cards at mgic.com/mgicrates.

Compare MGIC MI premium programs and non-MI programs for your borrowers at mgic.com/micalculator.

See MGIC's Servicing Guide at mgic.com/servicing-guide.



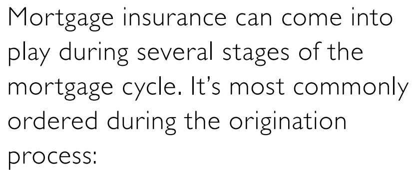
How Does MI Fit Into the Big Picture?



Investors like Fannie Mae and Freddie Mac purchase mortgages from lenders, who in turn use those funds to originate more mortgages.

Investors have set parameters that loans must meet before they are purchased. One such parameter is that the mortgage has a loan-to-value ratio of at least 80%, meaning that the borrowers have made a 20% down payment.

Historically, that 20% down payment has been a difficult hurdle to clear for many consumers. MI was created to help more consumers afford homeownership — to lift them over that hurdle. →



Mortgage insurance can come into play during several stages of the mortgage cycle. It's most commonly ordered during the origination process:

- By the loan originator while taking the loan application
- By the processor while completing the loan file or
- By an investor on warehoused loans

Later on in the cycle, MI serves as the passkey for low-down-payment loans for delivery into the Secondary Market, where the funds from their sale become available to fund new mortgages.

From origination through Secondary Market delivery, MI helps keep the mortgage cycle rolling along.

How Can My Borrowers Benefit From MI?

Borrowers probably do not consider themselves a potential default risk, so they may be skeptical or reluctant about MI. By offering MI as a finance option, you can overcome their doubts by showing them the opportunities that financing with MI can create for them. →

Increased buying power.

Say your borrowers have saved $20,000. They could use that cash to put 20% down on a $100,000 home OR they could make a smaller down payment on a more expensive home — for example, 10% down on a $200,000 home.

Expanded cash-flow options.

Using MI to finance their mortgage, your borrowers could elect to put less money down and still have funds for home-related purchases and repairs or investments. For example, rather than putting 20% down ($40,000) on a $200,000 home, they may decide to put down 10% ($20,000) and use the other $20,000 to remodel. →

Lower monthly payments.

MGIC rewards borrowers with credit scores of 760-plus with our lowest borrower-paid monthly MI rates. That translates to monthly MI costs and monthly mortgage payments that are significantly less than FHA financing.

Secure, competitive, predictable monthly payments.

A fixed-rate mortgage with MI provides borrowers with a locked-in monthly payment that will not increase and that will be reduced when MI coverage is cancelled.

Private mortgage insurance may be cancelled.

The Homeowners Protection Act of 1998 (HPA) provides conditions for homeowners to request MI cancellation when their mortgage balance reaches 80% of the original property value – because they've made all scheduled payments or extra payments ahead of schedule.

If they don't request cancellation, their lender must automatically cancel the MI policy when their mortgage balance reaches 78% of original value, and their mortgage payments are current.

Outside of HPA, they can ask their lender to cancel MI based on an increase in their property's appraised value.

In all scenarios, other requirements may apply. Homeowners should ask their lender for details.

Once mortgage insurance is cancelled, the borrowers' monthly mortgage payment is reduced by the amount of their monthly MI payment.

RESOURCES

Prepare your borrowers for homeownership with MGIC's Homebuyer Education, a free online certification program. Register for your Homebuyer Education code at mgic.com/homebuyereducation.

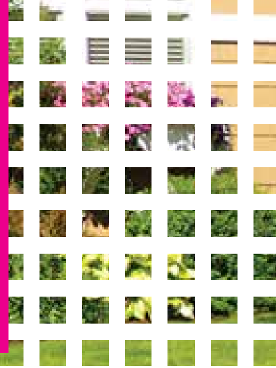
For detailed information about cancelling MI, go to mgic.com/servicing/cancelling-mortgage-insurance.

How Do My Borrowers Qualify for MI?

Loan files are underwritten for MI just as they are for lender or investor compliance.

- Underwriting for MI can occur simultaneously with the lender's evaluation or independently of it
- Files can be underwritten manually by the mortgage insurer's underwriting staff or electronically by the insurer's own automated underwriting system ➔

Generally, the principles of the mortgage industry's Four Cs apply: The borrowers' Credit, Capacity, Capital and Collateral are evaluated, as represented by the information on their loan application and on the documentation gathered to measure, support and substantiate their financial standing and the property's value.



The Four Cs

Credit

The borrowers' willingness to repay the loan, based on their prior use of credit

Capacity

The borrowers' ability to repay, based on the amount and stability of income

Capital

The amount of the investment in the property from savings and other sources

Collateral

Whether the property's value and marketability provide adequate security for the loan

Qualifying With Quality in Mind

As mortgage professionals, our shared goal is to qualify as many borrowers as possible without compromising the assets of the lender or the investor and, above all, without compromising the borrowers' ability to successfully maintain homeownership.

By carefully reviewing the borrowers' Credit, Capacity, Capital and Collateral, MGIC can piece together a comprehensive picture of risk.

The presence of a high-risk factor in any one of these categories doesn't necessarily threaten successful homeownership. But when a number of interrelated high-risk characteristics are present without sufficient offsets or compensating factors, their cumulative effect increases the likelihood of default.

RESOURCES

See our Underwriting Guide and guideline summaries at mgic.com/guides.

Order MGIC MI online via the Loan Center: Login at mgic.com; details at mgic.com/loancenter.

How Is MI Paid For?

MGIC offers both lender-paid and borrower-paid MI premium plans.

Borrower-Paid MI

MGIC borrower-paid premium plans incorporate credit scores to tier premiums. Under these plans:

- Borrowers with better credit ratings receive lower MI premium rates
- Those with weaker credit ratings receive higher rates

Monthly Premiums

Borrower-paid monthly MI remains the mortgage industry's preferred MI product because it's easy to execute.

MGIC borrower-paid monthly MI most often works out to be the best option for borrowers with high-quality credit — even over FHA financing. →

Advantages of conventional financing with MGIC monthly borrower-paid MI over FHA include:

- No upfront premium
- Lower loan amount (because there is no upfront premium to finance)
- A lower monthly mortgage payment
- Greater equity
- The chance to cancel MI sooner

A no-premium-due-at-closing option reduces closing costs. Borrowers pay the premiums as part of their monthly mortgage payment.

Monthly premiums are cancellable after an acceptable LTV level has been reached. When they are cancelled, the monthly mortgage payment is reduced by the amount of the MI premium.

Single Premiums

Borrowers pay a one-time, single payment up front at closing or finance it into the loan amount (check investor guidelines). A third party, such as a builder or a seller, can also pay Single Premiums.

Split Premiums

MGIC Split Premiums give your borrowers the option of paying part of the MI premium up front in order to reduce the monthly MI premium paid along with their mortgage payment. Borrowers can choose the upfront premium rate, which is a percentage of the loan amount.

A third party, such as a builder or a seller, may be eligible to pay the upfront premium.

Lender-Paid MI

MGIC lender-paid MI rate programs provide a "no MI" option for borrowers.

Lender-paid premiums are usually built into the mortgage interest rate or the origination fee.

For example, in exchange for paying the mortgage insurance premium, the lender may charge the borrowers a mortgage interest rate of 4.5% rather than 4.25%. Or the lender may recoup MI costs by charging an origination fee.

The Cost of MI

The cost of MI is based on

- The MI premium plan
- The mortgage loan program (fixed, adjustable, etc.)
- Loan term
- Whether the MI premium is refundable or nonrefundable
- Loan-to-value (LTV) ratio
- The amount of MI coverage, as determined by the lender or investor
- Loan amount
- The borrowers' credit scores
- Whether there are any adjustments to the premium to compensate for additional risk, such as a loan for a refinance

Your company will guide you regarding the premium plans you may use, as well as any other criteria that will need to be met.

RESOURCES

Calculate MGIC MI premiums online at mgic.com/ratefinder; access rate cards at mgic.com/mgicrates.

Compare MGIC MI premium programs and non-MI programs for your borrowers at mgic.com/micalculator.

MI Gives You an Extra Advantage

By understanding how MI works and offering it as a mortgage finance option, you create opportunities for your borrowers and yourself. With MI you can:

- Structure safe, high-LTV loans
- Possibly save your borrowers thousands in MI costs, compared to financing with FHA
- Broaden your customer base
- Enhance your role as Trusted Advisor and differentiate yourself from your competition by:
  + Broadening the options you provide your borrowers
  + Notifying them when they may be able to cancel MI and reduce their monthly mortgage payment

RESOURCES

For more information about mortgage insurance:

- Contact your MGIC representative, mgic.com/contact
- Sign up for our free, online MI Basics class at mgic.com/training

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MGIC Plaza, Milwaukee, Wisconsin 53202 • mgic.com
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