When You Need Private Mortgage Insurance

One of the biggest loans that most people in the United States take on during their lifetime is a mortgage for their house. Our system generally calls for a down payment of some type followed by a loan to cover the remainder of the house cost. Private mortgage insurance is usually required by the lender when the buyer puts down less than 20% of the sale price of the home he or she may wish to buy.

This insurance protects the lender in the event that the buyer is not able to finish paying off the loan. Once the mortgage is paid down to at least 80% of the home's value, or possibly when the home's value appreciates, the Private Mortgage insurance is usually no longer needed.

The sales price of the home is determined by the market value of the home, the area in which the home is located, and the size of the home. These dynamics are factored in when the home's value is set by the appraiser.

There are several different ways that the Private Mortgage Insurance might be paid. The first option would be for the insurance policy to be paid as escrow is closed on the purchase of the house. This insurance would be for a fixed amount of time. This time frame is determined by when the 80% value will be reached according to the mortgage amortization schedule.

A second option might be that the private mortgage insurance policy payment amount would be combined with the mortgage payment itself, much like property taxes are included with some mortgage payments. Again, this payment would stop at the time when the 80% value is reached and would no longer be part of the mortgage payment.

A third option exists, as well, and many times the buyer may not even know that mortgage insurance exists in their mortgage. Some of the higher interest rates might specify that no mortgage insurance is needed. in actuality, however, the insurance payment has been added to the interest rate quoted on the prepared mortgage payment.

The private mortgage insurance premium is determined by several factors. One important issue is whether or not the home is investment property or whether it is a primary or secondary residence for the borrower. Another item that would be considered is the loan amount against the current appraisal value of the home. Of primary importance would be the borrower's credit score.

Until 2007, private mortgage insurance premiums were not deductible on the home buyer's income taxes. It was for this reason that many people who did not have the full 20% down payment would consider a second mortgage. The second mortgage would provide the money for 10 or 15% of the down payment, depending on the need of the borrower.

Now, however, a borrower may deduct premiums for the private mortgage insurance for up to three years on their tax returns. In many cases, this deduction has made it more cost effective to purchase the insurance than to obtain a second mortgage.

According to the Homeowners Protection Act passed in 1998, most private mortgage insurance policies automatically cancel when the 78% loan-to-value is reached. Defaulting on the payments or making late payments will, however, allow the lender to continue to require this insurance. This requires less of the home buyer because of the automatic percentage built into the policy. The savvy home buyer will, of course, want to mark this date on a calendar and check to make sure this is taken care of promptly.

Legally, the lender can hold the borrower liable for the premium on the private mortgage insurance policy until the value of the home reaches 78% of the loan-to-ratio value. Once that obligation has been met, the lender will probably require that the home be appraised again to make sure the insurance is no longer needed.

However, if the home buyer's credit score is good and all the payments are current, there is another option. He or she may be able to petition to have the private mortgage insurance removed when 20% of the home's value has been paid by the borrower.

Exceptions to these two allowances for termination of the private mortgage insurance may not be allowed on loans that are considered to be high risk by the lender. Another situation which may influence whether the lender allows for termination of the policy may be the presence of other liens on the land and/or the home.

Many considerations go into the buying of a home. If the home buyer has less than 20% down payment, he or she needs to be prepared for this to be one of those considerations. Just as property taxes and home owner's insurance are part of the home owner's future, so private mortgage insurance is part of the home buyer's assortment of tasks to be dealt with as they look into the details of their new purchase.

About the Author

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