



Mortgage Bankers Association of Hawaii
P.O. Box 4129, Honolulu, Hawaii 96812

October 16, 2024

Member of the Insurance Stabilization Task Force

Re: Insurance Stabilization proposed legislation and funding of the HHRF.

Before making additional recommendations to the legislature for funding of the HHRF, a review of what was already in place from 1993 through 2001 is relevant. Since passage in 1993, there have been nine subsequent bills passed to amend operations, funding, and disposition of the HHRF. We strongly recommend that all parties review the original HRS as well as the subsequent amendments to understand the challenges that were faced when a previous generation of legislators and insurance professionals tried to implement something as complex as the HHRF. We also recommend that the various operational departments with the state government which will need to implement proposed legislation be consulted so that appropriate funding for any needed additional staff to operationalize the HHRF can be appropriated as part of any proposed bill. Review by the newly resurrected HHRF board to assure alignment in direction would also be prudent.

The Mortgage Bankers Association of Hawaii (“MBAH”) understands that considerations for funding of the HHRF are public policy issues that ultimately are best left to legislators to balance the needs of various constituents. Should the legislature determine that per-transaction fees assessed on real estate transfers are part of the optimal solution, the MBAH believes that sources to fund the HHRF should be “diversified” and be assessed on both cash-only transactions as well as those for which the buyer needs to obtain a mortgage loan to complete the purchase. With the existing Special Mortgage Recording Fee (“SMRF”), only certain non-cash buyers are contributing to this fund. In Hawaii, it is the legal obligation of the seller to pay the conveyance tax, unless otherwise negotiated. Thus, with the originally proposed addition of a conveyance tax surcharge in the 2024 SB 3234, sellers would also be contributing to funding, but all-cash buyers would not be. The imposition of a more broad-based nominal fee assessed to and shared by all buyers and sellers would be more equitable.

We do not support any increase to the Special Mortgage Recording Fee (“SMRF”). The SMRF is a regressive fee, in that homebuyers who need to finance more of their purchase price are assessed proportionally more than other buyers who need to finance less or who can purchase with all cash. The SMRF most adversely impacts first-time and low/moderate income homebuyers who need to finance a larger portion or all of their purchase price. Any increase would make the hurdle of having sufficient cash for down

payment, closing costs, and fees that much harder for hopeful buyers to overcome in an already high housing cost state.

With respect to determination of the amount and assessment of the Special Mortgage Recording Fee (“SMRF”), there are conflicting written instructions about how this fee would be applied to refinance transactions that create concerns for mortgage lenders in 2024. Prior to 2010, mortgage lenders were not accountable to pay fees for borrowers that were disclosed incorrectly in the up-front “Good Faith Estimate”. Regulations subsequently introduced in 2010 and in 2015, that affect the up-front disclosures provided to loan applicants within 3 business days of application, specify that any incorrectly disclosed amount must be paid by the mortgage lender. **Hence, clarification of how the SMRF would be assessed, if reactivated, is critical so that there is a clear bright-line process that can be known at time of loan application.**

History of SMRF

The need to clarify how the SMRF would be assessed on refinance transactions led to review of the original bill HHRF bill, subsequent amendments, and other documents.

1. The original 1993 Act 339 instituted the fee at 0.1% on the “stated principal amount of the debt secured by the mortgage or, in the case of an amendment of mortgage”, an amount equal to 0.10% of the amount of “the increase of the stated principal debt.” It was silent on specific treatment for refinances and undrawn home equity lines of credit.

the stated principal amount of the debt secured by the mortgage or, in the case of an amendment of a mortgage, an amount equal to one-tenth of one per cent of the amount of the increase of the stated principal debt.

2. This original bill was subsequently amended in the 1995 special session, Act 17, to provide a specific definition of a “mortgage” and to amend this section to specify that the SMRF would apply only to the amount of “increase of the stated principal amount of the debt, if any” in the case of a “refinancing”. Unfortunately, no definition of “refinancing” was also provided.

The special mortgage recording fee shall be [in] an amount equal to one-tenth of one per cent of the stated principal amount of the debt secured by the mortgage or, in the case of an amendment of refinancing of a mortgage, an amount equal to one-tenth of one per cent of the amount of the increase of the stated principal amount of the debt[.], if any.

3. It was not until June 3, 1998 with Act 106 when the assessment for the full amount of an undrawn or partially drawn “open end revolving” home equity line of credit was addressed, with a correction from “of” to “or” in front of the word “refinancing”.

The special mortgage recording fee shall be an amount equal to one-tenth of one per cent of the stated principal amount of the debt secured by the mortgage or, in the case of an amendment [of] or refinancing of a mortgage, an amount equal to one-tenth of one per cent of the amount of the increase of the stated principal amount of the secured debt[, if any.]; provided that the board may establish a lower special mortgage recording fee amount pursuant to section 431P-5(b)(14). With respect to an open end revolving loan, the principal amount of the debt on which the special mortgage recording fee is calculated shall be the maximum amount which may be outstanding under the loan at any one time. With respect to a mortgage securing a

4. The Administrative Rules 16-178-2, that describe the process to assess and collect the SMRF were not published until February 3, 1998, following a public hearing in December 1997 and prior to passage of the June 3, 1998 Act 106 previously mentioned. They specify that the SMRF “shall be calculated on the entire amount of the debt secured by the new mortgage” and do not specify something less. Those Administrative Rules include the guidelines on assessment of the SMRF on the full amount of an undrawn or partially drawn open-end revolving line of credit even though the law that clarified their treatment was not passed until 4 months after the rules were published, which is mysterious. I contacted the Hawaii State Archives to locate an earlier version, but they were unable to locate anything. So, **it appears that the rules were not published until 1998 even though the law was passed in 1993, five years earlier, but incorporated changes that were not approved to revise the HRS until 4 months after publication!**

(d) A refinancing occurs when an existing debt is extinguished and a new loan is made. When a loan is refinanced, the new mortgage shall be subject to the SMRF. The SMRF shall be calculated on the entire amount of the debt secured by the new mortgage.

5. The purple “SMRF” form, completed and provided to the Bureau for recording, dated April 1, 1999, conflicts with the Administrative Rules and specifies that the SMRF is collected only on the “increase in the stated principal amount of debt” for a “refinanced mortgage”.

Increase in the stated principal amount of debt secured by an amended or refinanced mortgage.

In summary, **there is a conflict between the Administrative Rules and the statute**, with further confusion created by the “SMRF” form with respect to assessment of the SMRF on refinances.

SMRF for refinances

I visited the Bureau of Conveyances to attempt to clarify how the SMRF was assessed for refinances. I was advised that administration and collection of SMRF was handled by a separate department at the Bureau, which was dismantled after the SMRF was no longer being assessed. The employees at the Bureau remembered receiving and forwarding the form and checks to that separate department, but were unable to clarify how the fee was assessed on refinances.

I consulted with an escrow company officer who remembers the SMRF assessment in the 1990s, who said that she is fairly certain that the SMRF was assessed on the full amount of refinance transactions, not just on the increased amount.

When the SMRF is assessed on the full amount of the refinance as described in the Administrative Rules, homeowners may end up paying the fee twice on the same balances solely because they want to reduce their interest rate and lower their monthly payments with a refinance.

Whether the SMRF is assessed on the full amount of a refinance transaction or only on the increased amount is critical to determination of how much revenue would be raised with a reinstated SMRF. Our internal reports show that for refinances, the percentage of the balance that was an increase vary from 5% to 15%, with lower percentages occurring in years with higher levels of refinance activity and very low interest rates. This lower percentage is because more borrowers would be motivated to refinance only to lower their rate and payment without additional cash in hand in a very low-rate environment, whereas receipt of cash out with an increase in balance is more likely to motivate borrowers in a higher rate environment. For example, our data shows in 2021, with extraordinarily low interest rates, only 52% of all refinances received cash out, which increased to 71% in 2022 and 79% in 2023 as interest rates rose.

The HHRF will need to count on reliable consistent amounts of funding. The SMRF is not reliable and consistent when assessed on refinances. The table below* shows the amount of SMRF that would have been collected in 2021, at the height of the refinance boom, and in 2023, in a high interest rate environment, if collected on the full amount of the refinance. With changes in interest rates, the revenue generated would have swung dramatically, to \$9.2MM from \$31.1 MM as interest rate changed if refinances were included. But revenue variances due to changes in purchase transactions only are smaller, to \$5.4MM from \$10.4MM. The decrease in revenues from eliminating refinances could be offset by assessing a fee on the full purchase price, instead of only the amount financed, and on all-cash transactions.

<u>High REFINANCE year 2021</u>	<u>Total Mortgages</u>	percent	<u>SMRF revenue</u>
TOTAL HOME EQUITY	\$2,963,033,912	0.1%	\$2,963,034
FIRST MORTGAGE PURCHASE	\$10,448,998,777	0.1%	\$10,448,999
FIRST MORTGAGE REFINANCE	\$17,753,218,591	0.1%	\$17,753,219
TOTAL SPECIAL MORTGAGE RECORDING FEE HIGH VOLUME YEAR			\$31,165,251
<u>Low REFINANCE year 2023</u>	<u>Total Mortgages</u>	percent	<u>SMRF revenue</u>
TOTAL HOME EQUITY	\$1,914,423,040	0.1%	\$1,914,423
FIRST MORTGAGE PURCHASE	\$5,414,676,790	0.1%	\$5,414,677
FIRST MORTGAGE REFINANCE	\$1,962,489,466	0.1%	\$1,962,489
TOTAL SPECIAL MORTGAGE RECORDING FEE LOW VOLUME YEAR			\$9,291,589

* Based on data provided in Title Guaranty monthly Hawaii Market Share report.

With respect to reverse mortgages, the SMRF is assessed on the full amount of the recorded mortgage lien but the proceeds of the refinance will not be disbursed to the borrower immediately. Thus, kapuna will have to draw an additional amount at loan origination to pay the SMRF assessment and receive less cash out of their reverse mortgage over time.

Summary

It should be noted that the existing HRS 431P-5 states that the HHRF already has the power to “Suspend or reactivate the special mortgage recording fee pursuant to resolution of the board”. Hence, legislative action is not needed to reactivate assessment of this fee, but **legislative action is needed to repeal the SMRF altogether.**

The Special Mortgage Recording Fee has the following flaws:

1. It is regressive, adversely impacting low/moderate income and first-time homebuyers disproportionately.
2. It is particularly detrimental to kapuna who must pay the fee now to receive future cash proceeds from reverse mortgage transactions.
3. It is highly variable and unreliable as a funding source, particularly when the fee is assessed on refinances.
4. Assessment of this fee on refinances may be double taxation for certain homeowners who paid the fee on a purchase-money mortgage and then refinance.
5. It creates complications for mortgage lenders and possible non-compliance with regulations imposed since the original HHRF law was passed.
6. There are conflicting published government documents as to how the fee should be applied to refinance transactions.

Based on the above, the MBAH believes that the Special Mortgage Recording Fee should be repealed altogether. If our legislature determines that real estate per-transaction fees are necessary to support start-up or ongoing funding of the HHRF, we recommend replacement of the SMRF with a nominal fee that is assessed on both buyers and sellers of real estate and that is not assessed to existing homeowners who want to refinance existing balances, whether or not the original balance is increased, or who want to access the equity in their home. Replacement with some other per-transfer assessment will be a more reliable and consistent funding source.

Thank you for the opportunity to present our suggestions.

Victor Brock
Mortgage Bankers Association of Hawaii