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Buying and Owning a Home

PREPAYMENT PENALTY MORTGAGES

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What is a Prepayment Penalty Mortgage?

A Prepayment Penalty Mortgage, or PPM, requires borrowers to pay a prepayment penalty or fee if the borrower prepays their entire loan or a substantial portion of it within a certain time period. This time period commonly applies to the first 5 years of the mortgage. Because of the many different types of mortgage products, a PPM is *always an option*, *never* a requirement. Borrowers may choose a PPM on a 15- or 30-year fixed-rate loan or Adjustable-Rate Mortgages.

What do borrowers receive in return for a PPM?

Depending on the lender, borrowers may receive reduced fees or a lower mortgage rate.

What exactly does "prepayment" mean?

Prepayment simply means paying all or part of a mortgage debt before it is due, i.e., the mortgage's original maturity date. Prepayment of a mortgage may include refinancing or making substantial payments against the principal (substantial payment is generally defined as more than 20% of the original principal balance).

What if a borrower sells their home within the specified prepayment time period?

If a borrower has chosen a PPM and sells their home within the specified period of time, they ***do not*** have to pay a penalty fee. Borrowers are required to pay a penalty fee ***only*** if they refinance or make a substantial payment against the mortgage principal.

How can a borrower determine if a prepayment mortgage makes sense for them?

Before choosing a prepayment penalty mortgage, borrowers should assess their current financial situation and think about how long they think they will keep the mortgage before refinancing or making a large payment against it.

How can borrowers determine how much the penalty fee will be if the mortgage is prepaid?

Lenders must provide the following information in writing:

- The amount of the penalty
- The time period in which the penalty will be charged if a borrower prepays or makes a substantial payment on a loan, and
- Any other conditions under which the lender may charge a prepayment penalty

What questions should borrowers ask their lender?

- How much will I save on my closing costs or fees?
- Will my interest rate be lower if I accept a PPM?
- Under what conditions will the lender enforce the prepayment penalty?
- How is the prepayment penalty calculated, and how much would it be?
- When can I prepay the loan without incurring a penalty?

Important information to remember:

- A PPM is always a borrower's choice, ***never*** a requirement.
- Prepaying means paying off the entire mortgage or a large portion of the principal within a specified period of time.
- Borrowers will ***not*** be charged a penalty fee when a house is sold.

Research all of your options when looking for the right type of mortgage. If you need assistance, you can talk to a homeowner education or housing counseling agency in your area.