

Legal Opinion: CIS-0090

Index: 4.130, 4.155
Subject: Excessive 1% Origination Fees in Puerto Rico

September 10, 1996

MEMORANDUM FOR: Raymond C. Buday, Jr., Assistant General Counsel
Southeast/Caribbean, 4AC

FROM: John J. Daly, Associate General Counsel for Insured
Housing, CI

SUBJECT: Origination Fees in Puerto Rico

The OGC Weekly Activity Report dated July 12, 1996 contains the following item:

Southeast. OC Finds that Commonwealth Law Permits Higher Lending Fees. OC issued an opinion to MBA-PR regarding non-applicability to Puerto Rico of preemption of Section 501(a)(1) of Public Law 96-221. A review of the local statute codified at 10 LPRA Section 998(1) evidences that Puerto Rico exercised the right granted by the cited federal statute not to be subject to the federal preemption with respect to interest rates, discount points, origination fees and other finance charges. Given Puerto Rico's exercise of such right, mortgage lenders in Puerto Rico will be able to charge, once a local regulation is amended, origination fees in excess of the 1 percent fee limitation established by 24 CFR Section 203.27.

In response to our inquiry about this item, Maria Teresa Pombo, Chief Counsel, HUD Caribbean Office, furnished this Office with copies of a June 28, 1996 letter to Ms. Pombo from Norberto Medina Zunaga, Ms. Pombo's July 10, 1996 reply to Mr. Medina, and Mr. Medina's July 24, 1996 letter to the Financial Institutions Commissioner of Puerto Rico concerning origination fees in excess of 1% on FHA-insured single family mortgages in Puerto Rico.

Mr. Medina had taken the position that Section 501 of Public Law 96-221, the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA), 12 USC 1735f-7a, permitted Puerto Rico "to override the preemption provided by [that] statute in regard to the interest rates, discount points, origination fees and other finance charges," and that Puerto Rico exercised its option to override the preemption. Therefore, according to Mr. Medina, mortgage lenders in Puerto Rico may charge origination fees in excess of the 1% limitation in 24 CFR 203.27.

Ms. Pombo stated in her letter that she agreed with the foregoing position.

Section 501(a) of DIDMCA provides that state laws and constitutional provisions limiting the rates or amounts of interest, discount points, finance charges, and other charges imposed by mortgage lenders are inapplicable to certain loans, including but not limited to, single family mortgages insured by FHA. Section 501(b) of DIDMCA authorized states to override this preemption of their laws and constitutional provisions during the three-year period from April 1, 1980 until March 31, 1983. Puerto Rico enacted such legislation on June 14, 1980. See 10 LPRA 9981-998q.

Mr. Medina's interpretation of the affect of the preemption and the override authorized by Section 501 of DIDMCA is incorrect with regard to the origination fee limitation in Section 203.27 of the regulations. This limitation was promulgated by FHA many years prior to enactment of DIDMCA, and is a condition for insurance by FHA of a mortgage. Thus, if a state law authorized an origination fee in excess of 1%, the mortgage lender could not charge the full amount authorized by state law if the mortgage was insured by FHA. The DIDMCA preemption had no effect on this limitation, because it was not a state limitation. Consequently, the override of the preemption afforded by DIDMCA could have no affect on Section 203.27's limitation.

Please request Ms. Pombo to advise Mr. Medina and the Financial Institutions Commissioner of Puerto Rico that mortgagees cannot charge origination fees in excess of 1% for FHA-insured mortgages in Puerto Rico. FHA-approved mortgagees should also be notified of the foregoing.