

SUBJECT: First Lien Residential Mortgage Loans Under § 138.052

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INTRODUCTION

This Release applies to all credit unions offering residential real estate (including mobile home) loans secured by a first mortgage or equivalent security interest. The Release describes the requirements of Wis. Stats. § 138.052. Additional requirements, under Wis. Stats. Ch. 428, are noted in this Release as applying to these loans when the amount financed is \$25,000 or less. Wisconsin's qualified loan funds law is also described in this Release, even though not a part of § 138.052.

EXECUTIVE SUMMARY

Wis. Stats. § 138.052 imposes special consumer protection requirements for first mortgage lending which are unique to Wisconsin. These requirements are not necessarily addressed in all forms and compliance materials used by credit unions, especially those developed out of state. Credit unions engaged in secondary market lending should be especially diligent in verifying that their procedures comply with these laws.

Specific topics addressed include:

- Qualified loan funds,
- Escrow payment options,
- Forms,
- Late fees,
- Right to prepay,
- Prompt response to inquiries; prompt crediting of payments,
- Dividends on escrow accounts,
- Refund of unearned interest paid, and
- Notification of sale or release of servicing.

For purposes of this Release, it is assumed that the borrower is a member. However, keep in mind that other non-member consumers, such as co-borrowers or co-mortgagors, may have the same rights under the law as members. Other ii Releases describe additional topics of importance in real estate lending, such as financial strategies for first mortgage lending (*ii Release No. B016*), adjustable rate mortgage lending (*ii Release No. B030*), RESPA (*ii Release No. B014*), and right of rescission (*ii Release No. B036*), and DFI-CU 54 (*ii Release No. B053*).

SCOPE

With certain exceptions, Wis. Stats. § 138.052 applies to any loan secured by a first lien real estate mortgage on (or equivalent security interest in) a one- to four-family dwelling which the member uses as his or her principal residence. This broad definition may include purchase money loans, refinancings, home improvement loans, home equity loans, mobile homes attached to real estate, or R.E.A.P.[®] lines of credit. An “equivalent security interest” is a junior lien where the credit union holds the only senior lien. Thus, a second mortgage where the credit union holds the first is “equivalent” to a first lien and is subject to this law.

While the dollar amount of the loan is immaterial under § 138.052, Chapter 428 applies only to loans with an amount financed of \$25,000 or less.

Exceptions

Neither § 138.052 nor Ch. 428 applies to:

- A mobile home transaction when the structure is not attached to real estate owned by the mobile home owner;
- A loan that is primarily for a business purpose; or
- A loan to a corporation or a limited liability company.

Furthermore, § 138.052 does not apply to:

- A loan that is primarily for an agricultural purpose; or
- A HUD, VA, or FHA insured or guaranteed loan.

LOAN CLOSING

Qualified Loan Funds (§ 708.10)

Credit unions granting a real estate loan must supply “qualified loan funds” to the closing agent. The intent of the law is to guarantee that the funds delivered at closing are good. Other states have had problems with warehouse lenders closing their operations without notice. Qualified loan funds include the following four choices:

- A wire transfer;
- A cashier's check or teller's check;
- A check on which the lender or an affiliate of the credit union is the payer; or
- A transfer of loan funds by the credit union to an account in favor of the closing agent. Explanation of Personal Obligation (§ 428.103(1)(b))

If the amount financed is \$25,000 ([increased to \\$50,000 as of Jan. 1, 2027](#)) or less, the credit union must provide any cosigner, other than a spouse, an Explanation of Personal Obligation notice substantially the same as that required by the Wisconsin Consumer Act (§ 422.305). The League offers forms for this purpose (#82028 for closed-end and #82077 for open-end credit). The cosigner is also entitled to a copy of any document evidencing the obligation to pay the debt.

Escrow Payment Options (§ 138.052(5m))

The escrow payment option applies to the credit union or any “escrow agent” who receives escrow payments on behalf of itself or another party. For simplicity, the Release will refer only to the credit union. Please note that a credit union requiring escrow of funds for taxes, insurance, etc., should address the issue in its mortgage documents. For example, the League's Real Estate Mortgage Note—Non-Consumer (#82042) includes a check box to be marked if the credit union requires an escrow.

Notice of Escrow Payment Options

Except as provided below, if an escrow is required to assure the payment of property taxes, a credit union which originates a loan must, before the loan closing, provide the member with a written notice clearly stating:

- That the borrower may require the credit union to make payments under any of three options, described below, from the amount escrowed to pay property taxes; and
- The responsibilities of the borrower and credit union under this law.

A model form is provided in *Exhibit B* of this Release.

Member's Options

Again, subject to the exceptions below, a member may require the credit union to do any of three options. The member must notify the credit union of his or her choice by November 1 and the loan must be current.

Option #1 Direct the credit union to send the member a check by December 20 in the amount of the funds held in escrow for the payment of property taxes. The check must be made jointly payable to the member and the town, city, or village treasurer authorized to collect the tax. (In its sole discretion, a credit union may send the check made payable only to the member.)

The member choosing this option must annually, by March 31, send a copy of the receipt for paid property taxes to the credit union or other party to whom the member makes his or her loan payments.

A member who fails to do so loses the option of receiving the escrow payout later that year in the manner specified. If that happens, the member may again receive payments under this option by renotifying the credit union in writing by November 1 of the next year. Of course, the member must be current on loan payments.

Option #2 Direct the credit union to pay the property taxes by December 31, if the credit union has received a tax statement for that property by December 20.

Option #3 Direct the credit union to pay the property taxes when due.

Member's Exercise of Options

A member wishing to exercise one of the three options for the first time must send written notice to the credit union by November 1, specifying the choice. Once notified, the credit union must annually make payments in that manner unless:

- The member is not current in his or her loan payments;
- Notified in writing by the member by November 1 to do otherwise; or
- A member who chooses Option 1 fails to provide the credit union with a copy of the tax receipt by March 31.

Exceptions

The credit union is exempt from the escrow payment option rules if its practice is to send the member a check by December 20 payable to the borrower, or to the borrower and the treasurer authorized to collect the tax, in the amount held in escrow for the payment of property taxes. However, the current requirements of RESPA would permit this only if the member voluntarily agrees to the practice. See *ii Release No. B014*.

Member May Establish Escrow Account Elsewhere If Credit Union Fails to Comply

A member may establish an escrow account required for the payment of taxes and insurance in a financial institution of the member's choice if the credit union fails to comply with the escrow payment option law, unless the credit union demonstrates that the other financial institution is incapable of servicing the escrow account.

If the member establishes the account elsewhere, he or she must annually, by March 31, send to the credit union verification of the amounts which the member deposited in the escrow account during the previous 12 months and copies of receipts for taxes and insurance paid during the previous 12 months.

Late Fees

On first lien loans, the parties may agree to imposition of a late payment charge not exceeding 5% of the unpaid amount of any installment not paid on or before the 15th day after its due date. For purposes of this rule, payments are applied first to current installments and then to delinquent installments. A delinquency charge may be imposed only once on any installment. (§ 138.052(6))

For the few loans subject to Chapter 428 but exempt from § 138.052, no delinquency charge may be collected on an installment which is paid in full on or before the 10th day after its scheduled due date even though an earlier maturing installment may not have been paid in full. For purposes of this rule, payments are applied first to current installments and then to delinquent installments. (§ 428.103(1)(a))

Late fees are permitted only if agreed to by the member in the note. The Real Estate Mortgage Note (#82042) and R.E.A.P. Non-Consumer Loan Agreement (#82087) include appropriate language. Truth in Lending disclosures must also include the late fee.

CONTRACT TERMS

Forms

The League offers mortgage, note, and Truth in Lending forms drafted to ease compliance with the many requirements described in this Release. For closed-end loans a credit union may use the following:

- Real Estate Mortgage Note (Non-Consumer) (#82042), and
- Mortgage (Non-Consumer) (#82043).

The credit union must obtain TILA-RESPA Integrated Disclosures (Loan Estimate and Closing Disclosure) from other compliance-oriented form vendors such as TruStage.

For open-end real estate lines of credit, the League offers:

- R.E.A.P.® Non-Consumer Loan Agreement (#82087); and
- R.E.A.P. Non-Consumer Mortgage (#82088).

Right to Prepay (§ 138.052(2)(a))

A loan may be prepaid by the member at any time in whole or in part. Prepayment penalties are limited in amount and often entirely prohibited.

Prepayment penalties may only be imposed if provided for in the contract and then only during the first five years of the loan, notwithstanding any refinancing, renewal, extension, or modification of the loan. The penalty is limited to an amount not exceeding 60 days' interest at the contract rate on the amount by which the aggregate principal prepayments for a 12-month period exceeds 20% of the original amount of the loan.

The League's Real Estate Mortgage Note (#82042) includes a check box for use if the credit union wants the right to impose this prepayment penalty. Be sure to also indicate on the Truth in Lending disclosure that a prepayment penalty may be charged. Also, disclose whether the loan will be subject to a rebate of any finance charge if prepaid, especially as described later under "Refund of Unearned Interest Paid."

When are prepayment penalties prohibited?

No prepayment penalty is allowed five or more years from the date the loan is made. Remember, a refinancing or other modification of a loan does not extend this five year period.

Wis. Stats. § 138.056(3m)(a) provides additional restrictions on ARMs. Lenders may not include a prepayment penalty in a variable rate loan using an approved index unless all of the following are satisfied:

1. The lender also makes variable rate loans without prepayment penalties and the lender provides the borrower with a written statement that the lender also makes variable rate loans without prepayment penalties.
2. At the time of the offer of the variable rate loan, and the borrower acknowledges, in writing, receipt of the statement specified in item 1 above.
3. The penalty is limited to prepayment that is made within 3 years of the date of the loan.
4. The prepayment is not made in connection with the sale of a dwelling or manufactured home securing the loan.

This applies to variable rate loans made, refinanced, renewed, extended, or modified on or after March 25, 2006.

Security Interest in Household Goods (§ 428.103(1)(d))

For loans with an amount financed of \$25,000 or less, no credit union may take a security interest in the household goods or furnishings, other than fixtures, of a member or other borrower.

Attorney Fees (§ 428.103(e))

For loans with an amount financed of \$25,000 or less, the credit union may not contract for or charge its attorney fees to the member except as follows:

- Reasonable fees for opinions of title.
- In foreclosure cases, 5% of the amount adjudged due the credit union; or if the dispute is settled prior to judgment, a reasonable fee based on the time, nature and extent of the work involved, but not to exceed 2.5% of the unpaid principal balance of the loan.

POST-CLOSING

Prompt Response to Inquiries; Prompt Crediting of Payments (§ 138.052(7s))

A credit union which receives loan or escrow payments must:

- Respond to a member's inquiry within 15 days after receiving the inquiry; and
- Consider that a loan payment by check, or other negotiable instrument, is made on the date on which the check is physically received. However the credit union may charge back an uncollected loan payment.

The following additional requirements of § 428.104 apply to loans with an amount financed of \$25,000 or less:

- Any time a payment is made in cash, or any other time the method of payment does not itself provide evidence of payment, the credit union must automatically furnish the member a written receipt, evidencing such payment.

The member is entitled upon request to an annual statement of account showing receipts and disbursements, free of charge.

Satisfaction of Mortgage

Upon payment in full of the member's obligation, the credit union must satisfy any mortgage. See The League's *ii Release No. B078*, which describes additional compliance requirements for mortgage payoff requests, payoff statements, and satisfactions.

Dividends on Escrow Accounts (§ 138.052(5))

A state-chartered credit union that originates a covered first lien mortgage or equivalent loan and requires an escrow to assure the payment of taxes or insurance must pay dividends (interest) on the outstanding principal balance of the escrow at a rate to be established annually by state regulators if the loan was originated on or after January 1, 1994, and before April 18, 2018. For 2026, the mandatory interest rate on certain required escrow accounts originated before April 18, 2018 will be 0.17% (down from 0.20% in 2025).

The annually revised dividend rate also applies to loans originated after January 31, 1983, and before January 1, 1994, if a dividend rate is not specified in the loan agreement. Escrow accounts for loans originated prior to that period were once subject to a 5.25% fixed rate. In the unlikely event that the 5.25% rate was specified in a loan agreement originated after January 31, 1983, and before January 1, 1994, it still applies.

Exceptions

There is no requirement under §138.052 to pay interest on a required escrow account when:

- The escrow funds are held by a 3rd party in a non-interest-bearing account;
- The parties agree to waive payment of all or part of the interest if more than 75% of the credit union's interest in the loan is sold to a 3rd party who is not "related to" the credit union and the escrow funds are held by the 3rd party.

- The credit union operates under a federal (not state) charter. This is because the NCUA General Counsel's office issued an opinion letter in 1991 determining that NCUA rules preempt this Wisconsin provision in regard to federal credit unions.

How the Rate Is Set Each Year

State regulators must annually determine the average of the rates paid on regular passbook accounts by all state financial institutions.

The average rate is rounded to the nearest one-hundredth of a percent and reported to the Revisor of Statutes for publication in the *Wisconsin Administrative Register*. The published interest rate usually takes effect on January 1st and then remains in effect the entire year.

RESPA Imposes Additional Requirements

The Real Estate Settlement Procedures Act (RESPA) imposes initial disclosure and annual statement requirements on both required and voluntary escrows. It also sets forth rules on the amount of money the credit union can require to be escrowed and treatment of shortages and surpluses. See *ii Release No. B014* for details.

Refund of Unearned Interest Paid (§§ 138.052(2)(b), 138.052(3))

As discussed earlier, the member has a right to prepay the loan at any time; sometimes a penalty may be imposed. On the other side of the coin, the member who prepays, whether by cash, renewal or refinancing, is entitled to a refund of “unearned interest” paid. The unearned interest consists of a portion of the prepaid fees and charges on the loan.

All prepaid charges are subject to the rebate, *except* the following:

- Identifiable and separately itemized charges for services incident to the loan if they are bona fide and paid to 3rd parties.
- Fees, discounts or other sums actually imposed by GNMA, FNMA, FHLMC, or other government-sponsored secondary mortgage market purchaser of the loan or any private secondary mortgage market purchaser of the loan who is not a “person related to” the original lender.

This exclusion relates only to fees actually imposed by the secondary market purchaser of the loan. Thus, the exclusion is not available if the particular loan has not been sold. Anticipation of sale is not enough.

A “loan administration” fee charged by a lender, including fees paid to 3rd parties for loan administration services, not exceeding 2% of the principal amount of any construction loan and 2% of the principal amount of any other loan.

- The amount of any prepayment penalty authorized and collected as described earlier.
- Loan commitment fees.
- Amounts paid to the lender by any person other than the borrower.

Two options are provided for the refund computation. An actuarial method is most likely to be used for simple interest loans. Otherwise, a pro rata method is used. See § 138.052(2)(b) for details of the computation methods.

One detail in the law is that the parties may agree that any installment paid within 30 days prior to or after the scheduled due date is paid on the due date for purposes of calculating the refund. The League's Real Estate Mortgage Note (#82042) includes a clause to allow the credit union and member to agree on this option by filling in 30 days.

Interest after Acceleration or Maturity (§ 138.052(7))

The interest imposed on the amount due after acceleration or maturity of a loan may not exceed the contract rate. For purposes of this law, the contract rate means the rate contracted to be paid from time to time on the principal of the loan.

Debt Collection (§ 428.103(1)(c))

Several special rules apply with respect to debt collection for loans with an amount financed of \$25,000 or less:

First, the credit union may not engage in debt collection practices of the type prohibited by the Wisconsin Consumer Act (§ 427.104).

Second, the member is given the benefit of certain exemptions from execution specified in the Wisconsin Consumer Act` (§ 425.106 (1) (a) and (b)), with respect to earnings, personal clothing, and furnishings (except as to fixtures).

Pleadings (§ 428.105))

For loans with an amount financed of \$25,000 or less, a credit union's complaint to enforce a cause of action must set forth the facts constituting the alleged default of the member, the amount to which the credit union is allegedly entitled and a summary of the figures necessary for computation of such amount, and must be accompanied by an accurate copy of the writing evidencing the transaction.

Attorney Fees (§ 428.103(1)(e))

As discussed earlier in this Release, attorney fees are limited if the amount financed is \$25,000 or less.

RELATED II RELEASES

Many other state and federal compliance rules apply to first lien residential mortgage loans. For more information, please see The League's *ii Release No. B053*, which includes an extensive list of compliance requirements for mortgage lending.

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League publications are designed to provide accurate information with regard to the subject matter covered, with the understanding that the League does not render legal services. If you have general questions regarding this release, please call The League at (608) 640-4050 if local or (800) 242-0833. For specific legal advice, please consult your credit union's attorney.

Legal Affairs Department

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EXHIBITS

A. Sample escrow payment option notice

EXHIBIT A - SAMPLE ESCROW PAYMENT OPTION NOTICE

Escrow Payment Option Notice

Wis. Stats. § 138.052(5m)

Your real estate mortgage loan requires an escrow to assure payment of property taxes and insurance. You have your choice of three tax payment options if you remain current in your loan payments and you send notice of your choice in writing by November 1 to *[insert name of credit union or escrow agent.]* The options are:

Option # 1. Check sent to you, payable to you *[Optional: and the tax authority]*.

You will be sent the check by December 20, to be applied to your real estate taxes. You must send *[insert name of credit union or escrow agent]* a copy of the receipt for paid property taxes by March 31 each year. Failure to do so will forfeit your right to this option on the next tax bill.

Option # 2. *[Insert name of credit union or escrow agent]* pays taxes directly by December 31, if provided a tax statement by December 20.

Option # 3. *[Insert name of credit union or escrow agent]* pays taxes when due.

With this option, taxes are paid after January 1.

Your choice will remain in effect for subsequent years as long as your loan payments are current, unless you send written notice of a change to *[insert name of credit union or escrow agent]* by November 1.

Please return this letter indicating your choice below.

I choose Option (☐ # 1) (☐ # 2) (☐ # 3), as described above, as my escrow payment choice.

(Member's signature)

(Date)