Sell More Homes
With Government Loans

FHA/ VA loans can help consumers qualify

by
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This 3 clock hour course will cover opportunities and challenges
that FHA/VA loans solve for today's borrower.

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Session	Topic		
1 30 min	History of the FHA Advantages of an FHA loan		
2 1 hour	Underwriting Guidelines Risk based pricing		
3 45 min	Qualifying standards Loan programs		
4 45 min	VA loan program and qualifying		

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Why FHA is a great alternative in today's market

This 3 clockhour course will cover the uses and some non-uses for FHA Government Insured Financing.

Mortgage lending has gotten tougher on guidelines, qualifying, and loan products in response to the difficult mortgage market. Government insured loans through the FHA have come back into favor as the government tries to respond to the needs of consumers in the mortgage industry.

To help generate more mortgage money in the market without the dangerous loans of the past FHA has responded with higher loan limits, risk based pricing and better products to serve the consumer.

Contemporary Topics like Risk Based Upfront Mortgage Insurance Premiums, Monthly MI Pricing, and How FHA is affected by FICO Scoring are real concerns in today's lending climate.

This course will discuss the do's and don'ts of FHA - when it can be used in cases of damaged or bruised credit AND when it can't be used in the case of the Classic Credit Criminal borrowers.

HUD is actively expanding its powers to help more homeowners to afford home ownership.

Course Objectives

As a result of taking this class the real estate licensee shall be able to:

- Know the history of FHA
- Know the advantage of using FHA
- Know what FHA insures
- Define occupancy status
- Identify maximum loan amounts
- Understand the basics of underwriting
- Understand qualifying guidelines

- Go over VA Qualifying
- Discuss questions that borrowers and brokers might have

Sell more Homes with Government Loans

History of FHA

The Federal Housing Administration (FHA) was created during the Great Depression to provide liquidity to the financial market while promoting homeownership. The FHA of 1934 was the leader in the industry, providing innovative programs during a time of great financial hardship that strengthened our communities and families. Over the last 74 years, the FHA has enabled over 34 million families to become homeowners, providing a safe and secure environment for children to learn and grow and the means for families to grow wealth.

In today's uncertain housing market many families are once again turning to the FHA. The FHA is not just concerned with getting families in a home but keeping them in their home. The FHA is committed to providing a means to a stronger and more secure future. Uncertain economic conditions and instability do not have to result in foreclosure. Foreclosures have alternatives and the FHA is helping struggling homeowners find alternatives.

What FHA Insures

FHA is an insurance program and not a lender. It is a governmental agency that insures lenders against borrower default. It is a department of HUD and insures the lender for loss.

The FHA insures mortgage on properties that consists of single family detached or semi detached dwellings, town houses or row houses, and individual units within FHA approved condominium projects.

FHA single family programs are limited to owner occupied residences for a minimum of one year only. FHA has strict guidelines to define principle residence. The FHA will NOT insure mortgages on commercial, boarding houses, hotels and motels, tourist houses, private clubs, bed and breakfast establishments, and fraternity and sorority houses.

FHA will not insure more than one mortgage for a borrower with a few exceptions including divorce, relocation, increase in family size, and non occupant co-borrowe

Benefits to an FHA Mortgage

- 3% down payment, as opposed to a 5% down payment on traditional loans
- Low monthly mortgage insurance
- Low closing costs, which are regulated by HUD
- Relaxed credit score requirements
- Qualify for a loan two years after a bankruptcy
- Qualify for a loan three years after a foreclosure
- Allows for a non occupant co-borrower
- Loans are assumable to qualified borrowers
- Competitive interest rates even with moderate credit scores
- Will still insure loans on manufactured loans
- Will insure large parcel properties
- FHA will use non traditional credit
- Can use a down payment assistance program for 100% financing

Maximum Loan Amounts

The maximum loan amount for an FHA loan is defined by county or Metropolitan Statistical Area (MSA). The Maximum insured mortgage is the lesser of:

a. The statutory loan limit for the area is typically based on a county or metropolitan statistical area (MSA)

b. The applicable loan to value limit varies by county.

Cash Investment Requirements

Typically, the borrower must contribute 3% of their own funds.

Gifts from a relative or very close family member
Trade equity
Sale of personal property
Gift funds
Employers Guarantee plan
Employers assistance plans
Savings bonds
IRA and qualified retirement accounts
Stocks
In some cases, cash that has been saved
Rent Credit
Commission from sale from a relative
Grants from Down Payment assistance programs
Private savings clubs
A bridal registry (people don't have to be married)

Gifts for the down payment from a relative can be up to 100% of the home buyers required cash investment. The gift may include the down payment, closing costs, pre-paids and discount points.

Down payment assistance programs may contribute the down payment if they are a appropriately qualified 501 (C) (3) non profit organization such as HART™, Ameridream™, Nehemiah™. Typically sellers assign up to 3-10% of the purchase price plus a service fee to the non profit at closing. In exchange for the service fee, the non profit, gifts a sum equal to the assigned funds by seller to the buyer at closing for the down payment.

Seller Concessions and Contributions

The seller can contribute up to 6% of the sales price towards buyers closing costs, prepaid expenses, discount points and other financing concessions. Contributions in excess of 6% of the sales price or exceeding the actual cost of prepaid expenses, discount points and other financing concessions will be treated as inducements to purchase thereby reducing the mortgage.

Inducements to purchase

Certain expenses paid on behalf of the borrower as well as other inducements to purchase result in dollar for dollar reduction to the sales price before applying the appropriate loan to value ratios in some cases.
Examples of these inducements include:

Decorating allowances
Repair allowances
Moving costs
And other costs to be determined by the local FHA office

Personal property given by sellers to consummate a sale including boats, cars, riding lawnmowers, furniture etc, result in a reduction to the mortgage. Certain items may be considered normal and customary as part of the transaction like ranges, refrigerators, dishwashers, washers dryers, window treatments are considered part of the transaction with no adjustments to the sales price.

Repairs and improvements

If the appraiser requires certain repairs as essential for property eligibility and to be paid for by the borrower may be added to the sales price before calculating the mortgage amount. The revised appraisal will reflect these improvements and repairs

For the cost of the repairs to be eligible for inclusion in the mortgage amount, the sales contract and addendum must identify the borrower as responsible for paying for or otherwise completing the repairs or improvements. The amount that may be added to the sales price before calculating the maximum mortgage amount is the lower of:

a. The amount the value of the property exceeds the sales price
b. The Appraisers estimate of repairs and improvements
c. The amount of the contractors bid, if available.

Only improvements or repairs required by the appraiser may be included.

If repairs cannot be made prior to closing due to weather delays, the lender must establish an escrow account to insure eventual completion of all required repairs.

Typically 150% of the bid amount must be held in the escrow account.

Energy Related Items

If weatherization items are added and paid by borrower, they sometimes can be added to the appraised value.

These can include:

Weather stripping,
Thermostat
Insulation
Storm windows and doors
Caulking

The cost of Solar Energy systems maybe added to the mortgage loan amount before calculating the loan to value ratios. The maximum loan amount can be exceeded by up to 20% to accommodate the cost of the solar system. Both active and passive solar systems, as wells as wind systems are acceptable.

Mortgage Insurance

Upfront Mortgage Insurance Premium (UFMIP) is required on an FHA loan.
FHA is a self supporting government program where the insurance premiums are paid for by the borrower. Any upfront mortgage insurance premiums paid in cash are added to the total cost of settlement or they can be added to the maximum loan amount.

The the upfront mortgage insurance premium is risk based price depending on borrowers credit score.

FHA requires borrowers to pay monthly mortgage insurance for a minimum of 5 years from the inception of the loan. After 5 years, if the loan to value is 78% or less the borrower can apply to have mortgage insurance eliminated.

Premium pricing on FHA

Lenders may pay the borrowers allowable closing costs and or prepaid items with premium pricing. Premium pricing is where the interest rate is raised over a par amount with a rebate coming from the lender. The rebate is defined as yield spread premium or service release premium and is an amount based on loan pricing and yield. Closing costs paid in this manner are not be included as part of the 6% seller contribution limit. Premium pricing may never be used for any portion of the borrower's down payment.

Underwriting

The purpose of underwriting is to determine the borrower's ability and willingness to repay the mortgage debt thus limiting the probability of default and collection difficulties and to examine the property offered as security for the loan to determine if it is sufficient collateral.

The four C's of credit are evaluated during the underwriting process.

- Credit History
- Capacity to repay
- Cash to close
- Collateral

Borrowers, Co-borrowers, and Co-signers
A co-borrower is liable for the repayment of the debt and has interest in the property. Borrower and co-borrower's income, assets, liabilities and credit history are considered when determining credit worthiness. Borrowers and co-borrowers are obligated on the mortgage note and all must sign the security instrument.

Co-signers do not hold ownership interest in the property but are liable for repaying the obligation and must sign all documents with the exception of the deed of trust. Co-signers income, assets, liabilities and credit history are considered when determining credit worthiness for the loan.

A co-borrower or co-signer may not be a party that has a financial interest in the transaction such as the seller, builder, or real estate agent except if they are a blood relative, by marriage, or in law.

Unless otherwise exempted, non occupying co-borrowers or co-signers must have a principle residence in the US unless they are military or US citizens living abroad.

Citizenship
Citizenship in the US is not required for eligibility. The following immigration status is allowed.

- Lawful permanent resident alien
- Non permanent resident alien
- US citizens

If borrower does not have a social security card they must have appropriate documentation from the Bureau of Citizenship and Immigration Service formerly the Immigration and Naturalization Service within the Department of Homeland Security.

Borrowers Age
There is no maximum age limit for the borrower. The minimum age is the age at which the mortgage note can be enforced in the state in which the property is located. In Washington State the minimum age for capacity for contracts is 18 years old.

Living Trust
Property held in a living trust is eligible for an FHA mortgage for an owner occupied property as long as the individual borrower remains the beneficiary and occupies the property as a principle residence.

Borrowers Credit
Borrower must have 12 month verifiable previous rental or mortgage history. Recent or undisclosed debts that may have been incurred to obtain part of the required cash investment on the property being purchased must be explained by the borrower in writing including any credit report inquiries in the last 90 days.

Collections and judgments
Court ordered judgments must be paid off before the loan is eligible for FHA insurance endorsement. FHA does not require that collection accounts be paid off as a condition of mortgage approval.

Previous mortgage foreclosure

Borrower must be clear of past foreclosure for 3 years to be eligible for an FHA insured mortgage. In cases of extenuating circumstances such as serious illness or death of a wage earner, the underwriter may grant an exception to the rule.

Bankruptcy

Two years after Chapter 7 bankruptcy discharge borrower may be eligible for FHA insured mortgage with re-established good credit.

Borrower may qualify for an FHA loan under chapter 13 bankruptcy reorganization after one year, a 12 months of positive pay history and a letter of acceptance from the court.

Consumer credit counseling

Same rules as Chapter 13 bankruptcy apply to borrowers participating in consumer credit counseling payment programs. The borrower must obtain written permission from the consumer credit counseling agency to enter into a new mortgage debt.

Credit report requirements

A credit report required by FHA for each borrower has information pulled from three repositories merged together. An alternative to the tri-merge report for FHA loans is a residential mortgage credit report (RMCR) from an independent consumer reporting agency.

Non traditional credit

If borrower has no traditional established credit, non traditional credit sources may be used to establish a credit history.

Delinquent federal Debt

If a borrower is delinquent on any federal debt including student loans, borrower does not qualify for FHA.

Income

Borrowers need a two year work history in the same line of work or related work field unless they were in school for that line of work in which the two year history can be waived. The underwriter should expect that the borrower will continue in that line of work for the following three years.

Borrowers must explain any substantial gaps in employment history. If borrower expects to retire, qualification must be based on projected retirement income.

Typical documentation

A borrower must provide current W2's or 1099's for the last two years. In addition, two years tax returns and retirement account statements, a month's worth of pay stubs, two months bank statements, copy of drivers license or government issued ID (patriot act), copy of social security card, statements on any investment accounts or life insurance.

Borrower qualifying

Debt to income ratios

To determine maximum PITI and MI (principle, interest, taxes and insurance and mortgage insurance) the total housing expense cannot exceed 31% of the borrower's gross effective income. All inclusive debt including mortgage cannot exceed 43% of the borrowers effect gross income. If the home is a documented energy efficient home, the ratios increase to 33% and 45% respectively.

Compensating factors
A compensating factor can be used to justify exceeding the debt to income ratio guidelines

- Borrower has successfully demonstrated that they can pay more than the housing amount equal to or greater than the proposed housing expense over the past 12-24 months.
- Borrower makes a large down payment of 10% or more towards the purchase
- Borrower has demonstrated an ability to accumulate savings and a conservative attitude towards the use of credit.
- Previous credit history shows that the borrower has the ability to devote a greater portion of income to housing expenses.
- There is only a minimal increase to the borrowers housing expense Borrower
- has substantial cash reserves - at least 3 months after closing Borrower has
- the potential for increased earnings as indicated by job training or education
- The home is being purchased as a result of relocation and the secondary wage earner has an established work history and is expected to return to work.

Appraisal

The property must be appraised by an FHA approved appraiser at the sales price or higher. The appraisal is completed on a standard appraisal form with an FHA addendum.

If the appraisal comes in less than the sales price the borrower can pay the difference or the seller can lower the price. According to the Amendatory Clause Addendum, the buyer shall have the right to withdraw without penalty if an agreement cannot be reached.

Federal Requirements

Fair Housing Laws
The Federal Fair Housing Act prohibits discrimination based race, color, religion, sex, national origin, familial status and handicap in obtaining mortgage loans and residential real estate transactions.

Equal Credit Opportunity Act (ECOA)
The Equal Credit Opportunity Act prohibits discrimination in the extension of credit on the basis of race, color, religion, sex, national origin, familial status and handicap.

Federal Credit Reporting Act
The Federal Credit Reporting Act is intended to control collection and dissemination of information about granting credit to the borrower. It is designed primarily to insure the consumer reporting agencies exercise fairness, confidentiality, and accuracy in preparing and disclosing credit information.

Home Mortgage Disclosure Act (HMDA)
The Home Mortgage Disclosure Act and Regulation C of the Federal Reserve Board require lenders to collect and to report information pertaining to applications for mortgage loans in addition to data regarding originations and purchases of such loans.

Assumptions of FHA Mortgages
All FHA insured mortgages are assumable. FHA has placed restrictions on the assumability of FHA loans originated since 1986. They have a due on sale clause but the lender can approve the new qualified borrower assuming the loan.

FHASecure
More than 200,000 families have refinanced their mortgage through the FHASecure program, an innovative program that enables families with non-FHA insured loans to refinance from expensive, exotic mortgages into a safe and secure FHA loan.

FHASecure is a refinancing option that gives homeowners with non-FHA adjustable rate mortgages (ARMs), current or delinquent and regardless of reset status, the ability to refinance into a FHA-insured mortgage. With FHASecure, the lender will not automatically disqualify you because you are delinquent on your loan, and the lender may offer you a second mortgage to make up the difference between the value of your property and what you owe. So long as you are current on your mortgage and have sufficient income to make the mortgage payment, you are eligible for an FHASecure refinance. If you are delinquent, the default must have been due to the payment shock of an interest rate reset or, in the case of an Option ARM, the "recasting" of the mortgage to fully amortizing.

FHA Loan limits in Washington State

FHA lending limits in WA state vary based on a variety of housing types and the cost of local housing. FHA loans are designed for borrowers who are unable to make large down payments.

In King, Snohomish and Pierce County the loan limit for a single family house in 2023 is $977,500.
The lowest loan limit that includes most of the other counties in the state is $472,030.

The down payment required can be as low as 3.5%.

Discussion Questions

What would typically be considered inducements in your market?

What if the seller contributes 6% toward closing costs and the actual costs are only 5%?

Can the down payment come from a friend?

What if the borrower brings art as a down payment?

What is the maximum loan amount for our area?

What if the sellers want to sell the lawnmower to the buyer for $500? Do you include it in the transaction?

Can the borrower make appraiser required repairs themselves without a contractors license?

What happens to the money in escrow not used to make required repairs?

What is the difference between closing costs and prepaids?

Does the agent have the right to get a copy of the buyer's credit report?

What is the difference between FHA, VA, and other government programs?

VA Loan Guaranty Program

Background

The Veterans Administration guarantees repayment of certain residential loans made to eligible veterans. The program is a loan guaranty, not the actual funds, to institutional lenders who provide the loans according to the VA guidelines. Just as the FHA insurance program protects lenders against default, so the VA guaranty covers a lenders loss at the time of foreclosure. This is not an insurance program and so there is no mortgage insurance premium to be paid.

The VA loan program was created for eligible veterans.

Lenders who have been approved by the VA to make these loans take and process applications from borrowers and loan approval is handled:
1. By the local VA office, or,
2. By the lender if they have the authority to approve the loans in their underwriting department.

The prospective borrowers apply to lenders and not directly to the VA.

Requirements

The requirements to get a VA guaranteed loan include:

1. The veteran must have a Certificate of Eligibility. Veterans must meet the minimum requirements to be eligible for the program.

2. It is a guaranty program and the lender is only to be reimbursed for the amount of the guaranty. The size of the guaranty is known as the veteran's entitlement a standard amount which is established by the Department of Veterans Affairs. The entitlement is $36,000 for home valued at less than $144,000 and $50,750 for home appraised at values between $144,000 to $203,000. The maximum loan offered by most lenders currently is $417,000 with the ability to go upwards with a very small down payment.
3. The home must be appraised by a VA appraiser and is called a Certificate of Reasonable Value and it must meet minimum standards of construction and maintenance.

4. VA loans are available for financing a home, new construction, mobile homes or condominiums.

Characteristics of VA Guaranty Loans

These loan programs target only eligible veterans or surviving spouses. But they are an ideal program for a veteran.

- A veteran can purchase a home with no down payment. T*his is the only institutional loan program available to buyers with no down payment up to a maximum loan amount. Any home above this the veteran has the option to put more down to make up the purchase price.*

- VA loans are fixed rate mortgages most often 30 year terms. There are some 15 year loans available as well as a 3-2-1 Buydowns. Veterans are required to qualify at the fully indexed note rate.

- The VA Loan is an insured loan. Therefore, there is no Mortgage Insurance. It is a "Guaranteed Loan". The Veterans Administration does extract a loan guarantee fee, called a "VA Funding Fee". The Funding Fee is collected on all VA Guaranteed loans, <u>unless</u> the Veteran has a VA related disability. Veterans with disabilities are exempt from being charged the VA Funding Fee. For Veterans who have never obtained a VA loan before, the funding fee is 2% of the loan amount. If the Veteran is placing a down payment into the transaction, he/she may qualify for a less expensive funding fee, depending on the percentage amount of the down payment. Under certain circumstances, members/former members of the "Active Reserves" may qualify for a VA Guaranteed loan. The Funding Fee for Reservist is 2.75% of the loan amount. All of the funding fee may be financed, (that is, added into the loan) .

- The loan can be assumed by another veteran using their certificate or not. *It can be assumed by another party without VA eligibility that makes a full application to qualify for the loan amount.*

- There are no prepayment charges. *VA loans may be paid off at any time and the veteran gains back his/her eligibility to get another VA loan providing that the veteran has sold the subject property.*

- The property must be owner-occupied primary residence.

Qualifying for a VA Loan

Ratios and Cash Flow Method

Lenders use the guidelines established by the Veterans Administration when qualifying a veteran. The Veteran must qualify under the ratio and cash flow methods. The total debt to income ratio is 41% of the borrowers gross income. This figure includes the vet's monthly debts as well as the proposed housing expense.

Using the cash flow method, the lender takes the proposed housing expense, all recurring obligations, and certain taxes and subtracts them from the vet's gross monthly income to determine his or her residual income. This residual income must meet the VA's minimum requirements which vary per region. The VA guidelines are generally more flexible than FHA and Fannie Mae.

Discussion Questions

Do you have to be a veteran to get a VA loan?

Can a spouse of a veteran who has passed away get a VA loan?

If a veteran purchases a house with a VA loan, what happens to his family if he passes away?

How little can a veteran put down on a house with a VA loan?

What happens if the veteran sells the house? Can that veteran buy another house using a VA loan.

What if the veteran was dishonorably discharged from the military. Can they qualify?

So many agents discuss with their seller that a VA loan will cost them so much more and there will be delays in the closing if they consider a VA loan from a buyer. How can the agent dismiss this and help their buyer buy the house?

Conclusion

There are a variety of loan programs available to real estate borrowers. It is best to evaluate the different programs with a lender that is knowledgeable, The programs change over time.

