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Chapter 7

Introduction to Government Agency Loan Programs

In This Chapter

The federal government plays a key role in the national real estate market, and its influence seems to grow every year. In addition to passing legislation that affects mortgage lending in general, one of the most direct ways in which the government can impact a specific borrower is through government agency loan programs that help borrowers purchase or refinance residential real estate. (Don't confuse these programs with government-sponsored entities and their involvement in the secondary mortgage markets.) The two most common programs are **FHA-insured loans**, under the authority of the Department of Housing and Urban Development (HUD), and **VA-guaranteed loans**, under the authority of the Department of Veterans Affairs (VA). Other specialized loan programs exist as well, which will also be briefly discussed in this chapter. This chapter provides an ***introduction*** to these programs; it is not intended to be a comprehensive lesson on underwriting FHA and VA loans.

At the end of this chapter, you will be able to:

- Identify basic qualifying standards for FHA-insured loans.
- Define the use of upfront mortgage insurance premiums.
- Recognize different loan programs available through the FHA.
- Identify basic qualifying standards for VA-guaranteed loans.
- Define eligibility and entitlement for veterans.
- Describe other government agency loan options.

Key Terms

Area Median Income (AMI)
Automatic Endorsers
CAIVRS
Department of Veterans Affairs (VA)
Direct Endorsers
Federal Housing Administration (FHA)
Funding Fee
Mortgage Insurance Premium (MIP)
Rural Development
TOTAL Scorecard

Federal Housing Administration (FHA) Insured Loans

To begin, let's clear up some possible misconceptions: The Federal Housing Administration (FHA) rarely provides mortgage funds directly to borrowers; the FHA does *not* build houses, nor does the FHA set interest rates. Instead, the Federal Housing Administration **insures** loans for single family and multifamily homes made by approved lenders. Mortgage insurance, you'll recall, provides lenders with protection against losses when borrowers default.

Another common misconception about FHA loans is that they are targeted to lower-income borrowers or first-time homebuyers only, but this is not the case. The Federal Housing Administration does *not* have income limits to determine who is eligible for FHA loans. Anyone who is a U.S. citizen, permanent resident, or non-permanent resident with a qualifying work visa, and who meets the lending guidelines may qualify for a FHA-insured loan. The FHA does, however, set a *maximum mortgage amount* that it will insure, as you'll see.

The FHA is part of the Department of Housing and Urban Development (HUD). Oversight of FHA loan programs is through HUD's Office of Housing, which has three business areas related to real estate transactions:

- Single Family Housing
- Multifamily Housing
- Regulatory Programs, which includes the Real Estate Settlement Procedures Act (RESPA) and the Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act)

HUD issues regulations and establishes guidelines for approving lenders authorized to make FHA loans. Its regulations have the force and effect of law. FHA defines the loan programs and sets guidelines for the programs in accordance with HUD's regulations.

Approved Lenders

Lending institutions that make FHA-insured loans must first be **approved**. If approved as an unconditional **Direct Endorser** (DE), the lender may then underwrite and close mortgage loans without prior FHA review or approval. This includes all aspects of the mortgage loan application, the property analysis, and borrower underwriting. The purpose of the Direct Endorsement program, as authorized under § 203(b) of the National Housing Act (12 U.S.C. 1709 (b), (I)), is to simplify and expedite the process by which mortgagees can obtain mortgage insurance endorsements from HUD.

HUD Homeownership Centers

Four regional Homeownership Centers process FHA loans and oversee the selling of HUD-owned homes acquired through foreclosure or through deed in lieu of foreclosure. Homeownership Centers are organized to serve specific states:

Philadelphia, PA	Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia
Atlanta, GA	Alabama, Florida, Georgia, Kentucky, Illinois, Indiana, Mississippi, North Carolina, South Carolina, Tennessee
Denver, CO	Arkansas, Colorado, Iowa, Kansas, Louisiana, Missouri, Minnesota, Montana, Nebraska, New Mexico, North Dakota, Oklahoma, South Dakota, Texas, Wisconsin, Utah
Santa Ana, CA	Alaska, Arizona, California, Hawaii, Idaho, Nevada, Oregon, Washington

HUD is further organized in 10 regions, each of which is managed by a regional administrator who also oversees the regional office. Within each region are a number of local field offices that offer various support services.

Limited Denial of Participation (LPD)

A **Limited Denial of Participation** (LDP) is an action taken by a HUD Field Office or the Deputy Assistant Secretary for Single Family or Multifamily Housing that excludes a person or company who fails to comply with HUD program standards from further participation in a HUD program area. LDPs are effective nationwide unless otherwise noted and generally expire in one year. Parties who have been issued an LDP should be prevented from new participation in the HUD program; therefore, mortgage loan originators need to check the LPD list before attempting to process an FHA loan application.

In addition to the LDP list, the General Services Administration's (GSA) **Lists of Parties Excluded from Federal Procurement or Nonprocurement Programs** must be checked to determine if individuals or companies are suspended or debarred from further participation in HUD programs.

Underwriting Standards for FHA Loans

When evaluating an application for an FHA loan, underwriters or lenders consider FHA's "4 Cs of Underwriting":

- **C**redit history of the borrower, which indicates the borrower's willingness to repay debt
- **C**apacity to repay the loan, which includes income and employment history
- **C**ash assets available to close the mortgage
- **C**ollateral, which evaluates the value of the home

Although an underwriter likes to see a stellar **credit history**, some prior credit issues might not be a problem. As with other mortgages, however, court-ordered judgments must be paid off first. In addition, a borrower who has defaulted on a student loan or is delinquent or in default on any federal debt would *not* qualify for an FHA loan. This is confirmed through the **Credit Alert Verification Reporting System**—CAIVRS—a federal database of delinquent federal debtors that allows federal agencies to reduce the risk to federal loan and loan guarantee programs. CAIVRS alerts participating federal lending agencies when an applicant for credit benefits, or for a position of trust in support of the administration of a federal credit program, has a federal lien, judgment, or a federal loan that is currently in default or foreclosure, or has had a claim paid by a reporting agency.

FHA is less stringent when it comes to a borrower's level of **income**. While no minimum or maximum income is required for an FHA loan, the borrower must have sufficient income to service the debt on the home mortgage and all other credit obligations. This is determined by housing expense and total debt-to-income ratios, which are slightly more liberal than those allowed for conventional loans.

FHA Underwriting Guidance

HUD Housing Handbooks provide detailed underwriting guidance on FHA loan programs. In particular, MLOs making single family FHA loans will likely become very familiar with these handbooks:

- Mortgage Credit Analysis (4155.1)
- Lender's Guide to the Single Family Mortgage Insurance Process (4155.2)

These are available online from the FHA Handbook page on this website:

www.fhaoutreach.gov/FHAHandbook/prod/index.asp

FHA Underwriting Guidance (continued)

In addition, HUD regularly publishes **Mortgagee Letters** as a way to communicate program changes, commentary on regulations, and other critical information to lenders and mortgage loan originators. Current and past Letters, numbered sequentially by year, can be found on this HUD website:

www.hud.gov/offices/adm/hudclips/letters/mortgagee

Note that the following guidelines discussed in this chapter generally apply to standard **FHA 203(b)** loans on **single family homes**. Other FHA loan types may have different guidelines or additional criteria.

FHA TOTAL Scorecard

The **Technology Open to Approved Lenders** (TOTAL) Mortgage Scorecard was developed by HUD to evaluate the credit risk of FHA loans that are submitted to an automated underwriting system (e.g., Desktop Underwriter® or Loan Prospector®). TOTAL evaluates the overall creditworthiness of the applicants based on a number of variables:

- Credit score
- Monthly housing expense
- Number of monthly payments in reserve
- Loan-to-value ratio
- Loan term

When combined with the functionalities of the AUS, TOTAL indicates a recommended level of underwriting and documentation to determine a loan's eligibility for insurance by FHA:

- **Accept/Approve**, which means that the loan is eligible for FHA endorsement
- **Refer**, which will require the lender to manually underwrite the loan

It is FHA's policy that no borrower will be denied an FHA insured mortgage loan solely on the basis of a risk assessment generated by the TOTAL Scorecard.

Mortgage Payment Expense to Effective Income Ratio

A borrower's mortgage payment expense to effective income ratio, more commonly referred to as the **housing expense ratio**, is *the relationship of the borrower's total monthly housing expense to income, expressed as a percentage*. FHA considers a borrower's income adequate for a loan if the proposed total mortgage payment does not exceed **31%** of gross stable monthly income. As with conventional loans, FHA's maximum mortgage payment includes **principal, interest, taxes, and insurance (PITI)**, as well as any required monthly homeowners association dues.

When you know a borrower's stable monthly income, you can multiply that by the housing expense ratio to determine the maximum monthly housing expense the borrower can afford. For example, if a borrower has a stable monthly income of $3,200, the maximum housing expense on an FHA loan would be $992 ($3,200 x .31).

Here's another way to use this ratio. When you know the total housing expense, you can determine whether the borrower's income is sufficient to qualify under the loan guidelines.

Class Activity: FHA Loan Qualifying (Part 1)

Mary wants an FHA loan to buy a house. She would have these monthly expenses:

	$536.82	Principal and Interest ($100,000 at 5% for 360 months)
	$ 53.00	Property Taxes
	$ 25.00	Homeowners Insurance
	$ 95.83	MIP (FHA Mortgage Insurance Premium based on 96% LTV)
+	$ 90.00	Homeowners Association Dues
	$800.65	Total Housing Expense (PITI)

What would be Mary's required stable monthly gross income in order to qualify for this loan?

Total Debt-to-Income Ratio

A borrower's **total debt-to-income ratio** is *the relationship of the borrower's total monthly debt obligations (including housing and other long-term debts that will not be cancelled) to income, expressed as a percentage*. This back end ratio is given primary consideration by TOTAL Scorecard, looking to ensure the borrower's total expenses do not exceed **43%** of monthly income.

Class Activity: FHA Loan Qualifying (Part 2)

	$800.65	Housing Expense (from previous example)
	$192.65	Auto Payment
+	$ 40.00	Revolving Credit Account
	$1,033.30	Total Debt

Based on her debt, what would be Mary's required stable monthly gross income in order to qualify for this loan using the total debt-to-income ratio?

Compensating Factors

If a loan applicant exceeds either or both of the permissible ratios of 31/43, the lender must document compensating factors that mitigate the risk:

Compensating Factor	Comments
Housing expense ratio	The borrower has successfully demonstrated the ability to pay housing expenses greater than or equal to the proposed monthly housing expenses for the new mortgage over the past 12-24 months.
Down payment	The borrower makes a large down payment of 10 percent or higher toward the purchase of the property.
Accumulated savings	The borrower has demonstrated an ability to accumulate savings and a conservative attitude toward using credit.
Previous credit history	A borrower's previous credit history shows that he/she has the ability to devote a greater portion of income to housing expenses.
Compensation or income not reflected in effective income	The borrower receives documented compensation or income that is not reflected on the 1003, but may affect his/her ability to pay the mortgage.
Minimal housing expense increase	There is only a minimal increase in the borrower's housing expense.
Substantial cash reserves	The borrower has substantial documented cash reserves (at least three months worth) after closing.
Substantial non-taxable income	The borrower has non-taxable income that is not included in on the 1003.
Potential for increased earnings	The borrower has a potential for increased earnings, as indicated by job training or education in his/her profession.
Primary wage-earner relocation	The home is being purchased because the primary wage-earner is relocating, and the secondary wage-earner has an established employment history, is expected to return to work, and has reasonable prospects for securing employment in a similar occupation in the new area.

Property Guidelines for FHA Loans

Among the important property guidelines for FHA loan approval are the **eligibility** of the property, the **condition** of the property, **maximum mortgage amount** permitted where the property is located, and **occupancy**.

Property Eligibility

Eligible one- to four-family dwellings include:

- Detached or semi-detached dwellings (with additional requirements for dwellings that are not detached)
- Row houses
- Multiplex dwellings
- Individual condominium units (approved)
- Some manufactured housing

Additionally, HUD guidelines indicate that utilities and other facilities should be independent for each unit and must include:

- A continuing supply of safe, potable water
- Sanitary facilities and a safe method of sewage disposal
- Heating adequate for health and comfort
- Domestic hot water
- Electricity for lighting and equipment

Property Conditions

At a minimum, the site conditions of a property must be free of health and safety hazards. FHA Handbooks provide **minimum property standards** (MPS) for new construction and **minimum property requirements** (MPR) for existing properties. An appraiser will note any issues and make recommendations about the need to engage qualified property inspectors as necessary to ensure that the property complies with FHA's MPR, or MPS, together with the estimated cost to cure. Typical conditions that would require further inspection or testing by qualified individuals or entities include:

- Infestation/evidence of termites
- Inoperative or inadequate plumbing, heating, or electrical systems
- Structural failure in framing members
- Leaking or worn-out roofs
- Cracked masonry or foundation damage
- Drainage problems

The lender determines which repairs for existing properties must be made for the property to be eligible for FHA-insured financing. Required repairs include those that are necessary to:

- Protect the health and safety of the occupants.
- Protect the security of the property.
- Correct physical deficiencies or conditions affecting structural integrity.

Occupancy

Borrowers with FHA loans are required to establish bona fide occupancy of the property as their principal residence **within 60 days** of signing a security instrument (e.g., mortgage, trust deed). Furthermore, they are required to live in the house for **at least one year**. Generally, a borrower may have only one FHA loan at a time, although some exceptions may be made.

√ **Note:** When there is a co-borrower who will ***not*** occupy the property as a principal residence, the maximum mortgage is limited to 75% LTV. However, if the non-occupying co-borrower is a family member or someone with documented evidence of a long-standing and substantial relationship separate from the loan transaction, maximum financing is available.

Maximum Mortgage Amount

Although there are no income limits with FHA loans, HUD limits the maximum loan amount—sometimes called a **loan ceiling** or **base**—that may be insured in a given community. When determining limits, boundaries may be based on county, zip code, or metropolitan statistical areas (MSAs). The loan amounts are reviewed every three years. For example, the 2011 limits for most single family homes is $271,050 (there are different loan ceilings for one-, two-, three-, and four-family dwellings). High cost area limits are subject to a ceiling based on a percent of the Freddie Mac loan limits. Section 214 of the National Housing Act provides that mortgage limits for Alaska, Guam, Hawaii, and the Virgin Islands may be adjusted up to 150 percent of the ceilings.

A current schedule of maximum FHA loan limits may be accessed from this website:

https://entp.hud.gov/idapp/html/hicostlook.cfm

Loan Regulations

Other important regulations for FHA loans are summarized here.

Required Minimum Investment

A borrower seeking an FHA loan must make a minimum required investment of at least **3.5%** of the home's purchase price or appraised value, *whichever is less* (i.e., maximum LTV of 96.5%) from an acceptable source. This assumes that the borrower has a credit score of **at least 580**. HUD indicates that borrowers applying for an FHA mortgage loan who have a credit score between 500 and 579 require a **10%** down payment, while those whose credit scores fall below 500 are *not* eligible for FHA-insured financing regardless of the down payment. Note that lenders may choose to impose higher standards than HUD in order to protect themselves from losses and have the ability to sell the mortgages on the secondary markets.

Closing costs (closing costs, pre-paid expenses, and discount points) may *not* be used to help meet the required minimum investment. A borrower may qualify for a **down payment assistance** grant from a state or municipal agency, non-profit organization, etc., however.

Gifts

The entire required minimum investment can be a non-repayable **gift** from a relative, an employer or labor union, a charitable organization, or a close friend with a clearly defined and documented interest in the borrower.

The gift donor may *not* be a person or entity with an interest in the sale of the property, such as the seller, a real estate agent or broker, or a builder/associated entity. Gifts from these sources are considered inducements to purchase, and *must* be subtracted from the sales price.

A lender must document any borrower gift funds through a **gift letter**, signed by the donor and borrower, that shows the donor's name and contact information; specifies the dollar amount of the gift; and states the nature of the relationship to the borrower and that no repayment is required.

Secondary Financing

FHA will insure first mortgage transactions that also include secondary financing if:

- The second mortgage or lien is by a federal, state, or local government agency or an approved nonprofit agency, and
- The monthly payment under the insured mortgage and second lien, plus housing expense and other recurring charges, does not exceed the borrowers' ability to pay.

With advance approval, FHA will insure a first mortgage loan on a property that has a second mortgage or lien held by an individual or company, provided that:

- The secondary financing is disclosed at the time of application,
- The required minimum cash investment is *not* financed,
- The first and second mortgage together do *not* exceed FHA mortgage limits,
- The borrower can afford the total amount of the payments,
- Any periodic payments are level and monthly,
- There is no balloon payment during the first ten years, and
- There is no prepayment penalty.

FHA reserves the right to refuse to insure the first mortgage if there is any secondary financing that does not serve the needs of the intended borrower or where the costs to participants outweighs the benefits derived by the borrower.

Seller/Third Party Contribution Limits

The seller and/or third party may contribute up to **6%** of the *lesser of* the property's sales price or the appraised value toward the buyer's closing costs, prepaid expenses, discount points, and other financing concessions. This limit also includes:

- Third party payment for permanent and temporary interest rate buydowns, and other payment supplements (note that borrowers must qualify at the note rate on temporary buydowns)
- Payments of mortgage interest for fixed rate mortgages
- Mortgage payment protection insurance
- Payment of the upfront mortgage insurance premium (UFMIP)

Such contributions *cannot* be used to reduce the borrower's required minimum investment, however.

Payment of real estate commissions or fees, typically paid by the seller under local or state law or local custom, is not considered an interested third party contribution. Contributions exceeding 6% are considered **inducements to purchase**, which requires that each dollar over the 6% limit must be subtracted from the property's sales price before applying the appropriate LTV factor.

√ **Note:** HUD has indicated its intention to reduce allowable seller contributions on FHA loans from 6% to only **3%**. This change is intended to reduce the risk of creating incentives to inflate appraised value. Final approval of this change is pending.

Loan Assumption

Most FHA loans made prior to December 15, 1989, are fully assumable—for a nominal handling fee—since they do not have alienation (due on sale) clauses. Recall that an **alienation clause** would *allow the lender to exercise certain rights upon the sale or transfer of an interest in the property*, for example, to call the note due, change the interest rate, or charge an assumption fee. However, it's important to note that the original borrower is NOT released from liability unless FHA agrees to the assumption.

FHA loans endorsed on or after December 15, 1989, may include an alienation clause. Such loans may be assumable, however, the lender will require a creditworthiness review of the new borrower as well as a fee. With these loans, assumptions without credit approval may be grounds for acceleration of the mortgage. Therefore, any offers involving mortgage assumptions must be investigated thoroughly with the lender, who must supply a specific release of liability, and perhaps even with legal counsel.

Prepayment Penalties

HUD regulations prohibit prepayment penalties in FHA loans. A borrower may prepay a mortgage, in whole or in part, on the first of any month. If the payment is received *after* the first of the month, however, the lender may, at its discretion, collect the remainder of the month's interest.

Mortgage Insurance Premium

A **mortgage insurance premium** (MIP)—not to be confused with PMI for conventional loans—is required for all FHA loans, regardless of the down payment. There is an initial premium—called the **upfront mortgage insurance premium** (UFMIP)—and an **annual premium**, which is based on the annual average outstanding loan balance divided into 12 monthly payments.

The UFMIP on 15- and 30-year purchase and refinance transactions for case numbers assigned on or after April 9, 2012, is **1.75%** of the loan amount. UFMIP for Hope for Homeowners and Home Equity Conversion Loans is 2.00%.

The monthly premium reflects the type of loan and loan-to-value. For example, the annual MIP on a 30-year loan is 1.20% if the LTV is 95% or less and 1.25% if the LTV is greater than 95% for case numbers assigned on or after 4/9/12. On a 15-year loan, it is 0.35% for loans with a 90% LTV or less, and .60% for loans with LTV over 90%. FHA will add an additional 25 bps to mortgages with base loan amounts exceeding $625,500 (effective 6/11/12).

Financing MIP

If the UFMIP for 15-year or 30-year loans is paid in cash at closing, it may be paid by the borrower or by the seller or other third party (within limits). It is most commonly financed into the loan itself, however. The Housing and Economic Recovery Act of 2008 limits the total FHA-insured first mortgage to 100% of the lesser of the sales price or appraised value, which would include the financing of the upfront mortgage insurance premium (UFMIP) within that limit.

Cancellation

For loans made after January 1, 2001, the MIP is automatically cancelled when the LTV reaches **78%** of the original value (for 30-year mortgages, the annual MIP must have also been paid for at least five years). Borrowers may be able to make additional or early payments of principal to reduce the LTV to that 78% threshold where MIP is automatically cancelled. Financed MIP cannot be cancelled.

Real Success

As you review the regulations discussed here or as you encounter others, be aware that laws regulating FHA loans continually evolve. Any changes to program details—for example, product availability, mortgage insurance premiums, seller contribution limits, credit score requirements, down payments, etc.—are communicated through **Mortgagee Letters**.

See: http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/

FHA Loan Programs

There are many FHA loan programs authorized under the federal statute that created the Federal Housing Administration. Most of these loan programs are referred to by the section number that describes them in the federal statute. For example, the most common type of loan is called a Section 203(b) loan after the statute section and paragraph that explains the requirements. Several programs are summarized here. More details on each of the specific FHA loan programs can be found in the HUD Handbooks.

FHA Loan Program	Description	Conditions
Section 203(b) Home Mortgage Insurance	• Basic owner-occupied loan for one- to four-family dwelling • Any term up to 30 years, fixed	• Required minimum investment of 3.5% with credit score of at least 580; 10% with credit score of 500-579 • Maximum loan origination fee of 1% • Requires UFMIP (1.75%) and monthly MIP up to 1.25% of loan balance (as of 4/9/12) • Maximum loan amounts range from $271,050 to $729,750 depending on geographic location
Section 203(k) Rehabilitation Home Mortgage Insurance and Streamlined Limited Repair Program	• Purchase and rehabilitate an existing one- to four-family dwelling • Loan for existing debt + repaid costs • Allows 110% LTV • Must bring the property into compliance with FHA standards • Repairs may include such items as: • Structural/additions (not on Streamline) • Siding/roofing • Plumbing/electrical • Heating/AC • Flooring/carpet	Section 203(k) • Must be able to occupy within six months • Minimum repair=$5,000 / Maximum repair=None Section 203(k) Streamline • Must be able to occupy within 30 days • Minimum repair=None / Maximum repair=$35,000
Section 234(c) Condominiums	Available for condo projects approved by FHA based on owner-occupancy and other criteria	Same eligibility as 203(b)
Section 251 Adjustable Rate Mortgages	• Available for 1- to 4-family dwelling or condominium • Allows for variable interest rate to reflect weekly average yield on U.S. Treasury Securities + margin • 1-, 3-, and 5-year ARMs allow: • 1% annual interest rate adjustment after the initial fixed interest rate period • 5% lifetime interest rate cap • 7- and 10-year ARMs allow: • 2% annual interest rate adjustment after the initial fixed interest rate period • 6% lifetime interest rate cap	• Only 30-year terms are allowed • Requires additional disclosures • Borrower must qualify at second year interest rate
Section 255 Home Equity Conversion Mortgage (HECM)	• Allows homeowners age 62 or older to convert equity in home to a monthly stream of income or line of credit	• Requires UFMIP (2.00%) and monthly premium (.5%) • Loan must be repaid when borrower sells, dies, or does not live in house for 12 consecutive months
Section 184 Indian Home Loan Guarantee Program	• Specifically for American Indian and Alaska Native families, tribes, Alaska Villages, or tribally designated housing entities	• 2.25% down payment requirement for loans over $50,000 • 1.25% down payment requirement for loans under $50,000 • No monthly mortgage insurance • A one-time, 1% loan guarantee fee
Energy Efficient Mortgage Program	• Allows borrowers to finance the cost of adding energy efficient improvements into a new home purchase or the refinancing of existing housing • May be used with the 203(k) Rehabilitation program	Same eligibility as 203(b)
Good Neighbors Next Door Program (GNND)	• Qualified civil servants, including firefighters, police officers, and teachers	• Assists public servants to purchase FHA foreclosures • Purchase price as low as 50% of the loan balance • Down payments as low as $100 • Requires occupancy as sole residence; borrower cannot own any other residential real property

Required Documentation

When making an FHA loan, the following documentation and disclosures are required to be given to applicants (in addition to the standard disclosures required in the loan origination process):

Disclosure	Purchase	Refinance
Amendatory Clause (to be included in the sales contract when the borrower has not been informed of the appraised value; provides the borrower with an "escape" clause if the property does not appraise for at least the sales price)	X	
Real Estate Certification (borrower, seller, and selling real estate licensee must certify that the terms and conditions of the sales contract are true to the best of their knowledge)	X	
Important Notice to Homebuyers (HUD 92900-B)	X	X
For Your Protection, Get a Home Inspection (HUD-92564-CN)	X	
Informed Consumer Choice Disclosure (compares terms of FHA loan with conventional financing or other available loan; must be made no later than 3 business days after receipt of the initial mortgage loan application)	X	X
FHA ARM Disclosure (for adjustable rate mortgages as applicable)	X	X
Release of Liability (for loan assumptions)	X	X
FHA Borrower Authorization (allows lender to verify borrower financial and employment information)	X	X
Identity of Interest Certification (identifies any relationship to the seller)	X	
92900 A FHA/VA Addendum (application for mortgage insurance)	X	X
HUD 92561 Hotel/Transient Usage (borrower certification that property will not be used for rentals of less than 30 days or if occupants receive customary hotel services)	X	X
FHA Social Security Number Verification Form	X	X

Important Notice to Homebuyers

U.S. Department of Housing and Urban Development
Office of Housing - Federal Housing Commissioner

OMB Approval No. 2502-0059
(Expires 11/30/2010)

You must read this entire document at the time you apply for the loan.
Return one copy to lender as proof of notification and keep one copy for your records.

Condition of Property

The property you are buying is not HUD/FHA approved and HUD/FHA does not warrant the condition or the value of the property. An appraisal will be performed to estimate the value of the property, but this appraisal does not guarantee that the house is free of defects. You should inspect the property yourself very carefully or hire a professional inspection service to inspect the property for you.

Interest Rate and Discount Points

HUD does not regulate the interest rate or the discount points that may be paid by you or the seller or other third party. You should shop around to be sure you are satisfied with the loan terms offered and with the service reputation of the lender you have chosen.

The interest rate, any discount points and the length of time the lender will honor the loan terms are all negotiated between you and the lender.

The seller can pay the discount points, or a portion thereof, if you and the seller agree to such an arrangement.

Lenders may agree to guarantee or "lock-in" the loan terms for a definite period of time (i.e., 15, 30, 60 days, etc.) or may permit your loan to be determined by future market conditions, also known as "floating". Lenders may require a fee to lock in the interest rate or the terms of the loan, but must provide a written agreement covering a minimum of 15 days before the anticipated closing. Your agreement with the lender will determine the degree, if any, that the interest rate and discount points may rise before closing.

If the lender determines you are eligible for the mortgage, your agreement with the seller may require you to complete the transaction or lose your deposit on the property.

Don't Commit Loan Fraud

It is important for you to understand that you are required to provide complete and accurate information when applying for a mortgage loan.

Do not falsify information about your income or assets.

Disclose all loans and debts (including money that may have been borrowed to make the downpayment).

Do not provide false letters-of-credit, cash-on-hand statements, gift letters or sweat equity letters.

Do not accept funds to be used for your downpayment from any other party (seller, real estate salesperson, builder, etc.).

Do not falsely certify that a property will be used for your primary residence when you are actually going to use it as a rental property.

Do not act as a "strawbuyer" (somebody who purchases a property for another person and then transfers title of the property to that person), nor should you give that person personal or credit information for them to use in any such scheme.

Do not apply for a loan by assuming the identity of another person.

Do not sign an incomplete or blank document; that is, one missing the name and address of the recipient and/or other important identifying information.

Penalties for Loan Fraud: Federal laws provide severe penalties for fraud, misrepresentation, or conspiracy to influence wrongly the issuance of mortgage insurance by HUD. You can be subject to a possible prison term and fine of up to $10,000 for providing false information. Additionally, you could be prohibited from obtaining a HUD-insured loan for an indefinite period.

Report Loan Fraud: If you are aware of any fraud in HUD programs or if an individual tries to persuade you to make false statements on a loan application, you should report the matter by calling your nearest HUD office or the HUD Regional Inspector General, or call the HUD Hotline on 1 (800) 347-3735.

Warning: It is a crime to knowingly make false statements to the United States Government on this or any similar form. Penalties upon conviction can include a fine and imprisonment. For details see: Title 18 U.S. Code Section 1001 and Section 1010.

Discrimination

If you believe you have been subject to discrimination because of race, color, religion, sex, handicap, familial status, or national origin, you should call HUD's Fair Housing & Equal Opportunity Complaint Hotline: 1 (800) 669-9777.

Previous editions are obsolete | Page 1 of 2 | form **HUD-92900-B** (12/2004) ref. Handbooks 4150.1 & 4155.1

Sample HUD Notice for Homebuyers

About Prepayment

This notice is to advise you of the requirements that must be followed to accomplish a prepayment of your mortgage, and to prevent accrual of any interest after the date of prepayment.

You may prepay any or all of the outstanding indebtedness due under your mortgage at any time, without penalty. However, to avoid the accrual of interest on any prepayment, the prepayment must be received on the installment due date (the first day of the month) if the lender stated this policy in its response to a request for a payoff figure.

Otherwise, you may be required to pay interest on the amount prepaid through the end of the month. The lender can refuse to accept prepayment on any date other than the installment due date.

FHA Mortgage Insurance Information

Who may be eligible for a refund?

Premium Refund: You may be eligible for a refund of a portion of the insurance premium if you paid an upfront mortgage insurance premium at settlement and are refinancing with another FHA mortgage.

Review your settlement papers or check with your mortgage company to determine if you paid an upfront premium.

Exceptions:

Assumptions: When a FHA insured loan is assumed the insurance remains in force (the seller receives no refund). The owner(s) of the property at the time the insurance is terminated is entitled to any refund.

FHA-to-FHA Refinance: When a FHA insured loan is refinanced, the refund from the old premium may be applied toward the upfront premium required for the new loan.

How are Refunds Determined?

The FHA Commissioner determines how much of the upfront premium is refunded when loans are terminated. Refunds are based on the number of months the loan is insured.

Monthly Insurance Premiums

If you paid an upfront mortgage insurance premium, you will also be charged a monthly mortgage insurance premium until the loan-to-value of your mortgage reaches 78 percent of the initial sales price or appraised value of your home, whichever was lower (provided that premiums are paid for at least five years). You will reach the 78 percent loan-to-value threshold in one of two ways: Through normal amortization as you make your monthly payments, or by paying additional principal on the mortgage. Your lender can advise you on when the mortgage will reach the 78 percent loan-to-value threshold. If you were not charged an upfront premium, you will pay the monthly premium for the life of the mortgage.

Important: The rules governing the eligibility for premium refunds are based on the financial status of the FHA insurance fund and are subject to change.

SI USTED HABLA ESPANOL Y TIENE DIFICULTAD LEYENDO O HABLANDO INGLES, POR FAVOR LLAME A ESTE NUMERO TELEFONICO 800.697.6967.

You, the borrower(s), must be certain that you understand the transaction. Seek professional advice if you are uncertain.

Acknowledgment: I acknowledge that I have read and received a copy of this notice at the time of loan application. This notice does not constitute a contract or binding agreement. It is designed to provide current HUD/FHA policy regarding refunds.

Signature & Date:

X______________________

Signature & Date:

X______________________

Signature & Date:

x______________________

Signature & Date:

x______________________

Previous editions are obsolete

Page 2 of 2

form **HUD-92900-B** (12/2004)
ref. Handbooks 4150.1 & 4155.1

Sample HUD Notice for Homebuyers

Mortgage Exercise 7-1

Borrower Stu wants to get an FHA loan for a home priced at $253,500 and appraised for $257,000. The monthly PITI payment on this house would be $1,780. He has a 680 credit score, gross monthly income of $6,850, other monthly recurring debts of $850, and $75 monthly electric bill. Stu will finance the 1.75% UFMIP into the loan. Assume that the FHA maximum loan amount for the county is $271,050. *See the Appendix for answers to check your work.*

1. What is borrower Stu's debt-to-income ratio? Based on the information provided, do you think this loan can be made? Why or why not?

2. What is the required minimum investment Stu must make to buy this home? What is the total loan amount? (Round to the nearest dollar.)

3. Would Stu be allowed to obtain secondary financing on this home to make the down payment?

4. What would be the prepayment penalty if Stu pays off the loan early?

VA-Guaranteed Loans

VA-guaranteed loans are *guaranteed by the federal government through the Veterans Benefits Administration*, which is part of the **Department of Veterans Affairs**. The VA's main purpose in guaranteeing loans is to help meet the housing needs of eligible veterans who have served or are currently serving on active duty in the U.S. Armed Forces, which includes: Army, Navy, Air Force, Marine Corps, Coast Guard, Reserves, or National Guard. VA loans are available to eligible veterans for the purchase of owner-occupied single family homes and for multifamily dwellings up to four units if the veteran intends to occupy one of the units as the primary residence.

The VA rarely loans money directly to borrowers. It may do so in isolated rural areas where financing isn't readily available, but usually a veteran must borrow money from a VA-approved lender. Lenders may also apply to become **Automatic Endorsers**, which gives them the authority to close VA-guaranteed loans without the prior approval of VA (except for certain types of loans—such as loans secured by a junior lien—

that must be submitted to VA for prior approval by all lenders). VA Automatic Endorsers are responsible for supervising the entire mortgage process through closing, performing underwriting functions (credit examination, appraisal review, etc.) then submitting the loan to the VA after closing for guaranty.

The VA provides access to an online **Lender's Handbook**—as well as other valuable resources—from their website:

www.homeloans.va.gov

Eligibility

Although the lender will examine the borrower's credit history, amount of income, and other factors before approving the loan, the primary requirement to be approved for a VA loan is the borrower's military **eligibility**, which is based on a person's length of continuous active service and other factors, such as when they enlisted and whether they served during war time. Spouses of veterans who died on active duty from service-related causes or who were MIA or a POW may also be eligible for a VA loan.

A current list of eligibility requirements is available from this VA website:

www.homeloans.va.gov/elig2.htm

Documentation

Lenders may not process or close a VA loan without verifying the eligibility of the borrower with a **Certificate of Eligibility** (COE) issued by the VA. Either the lender or the borrower may apply for a COE online (www.homeloans.va.gov/eligibility.htm). They may also apply for a COE through the mail using VA Form 26-1880, Request for a Certificate of Eligibility.

In order to receive a COE, the veteran must first be able to document his or her service:

- **Discharged veterans who served in a regular component of the Armed Forces.** Certificate of Release or Discharge from Active Duty, or **DD-214**, issued by the Department of Defense to identify the character of service and reason for discharge (honorable, dishonorable, etc,)
- **Discharged members of the Army or Air National Guard never activated.** NGB Form 22 (Report of Separation and Record of Service) or NGB Form 23 (Retirement Points Accounting) and proof of character of service
- **Veterans on active duty or individuals who are still members of the Reserve/Guard.** A statement of service signed by, or by the direction of, the adjutant, personnel office, or commander of the unit or higher headquarters to which they are attached

Maximum Loan Limit

The VA doesn't limit the price a veteran can pay for a house (as long as the house will appraise for the loan amount), but the VA does limit the amount it will guarantee in case of default to **25%** of the purchase price or the established reasonable value, whichever is less. A veteran's maximum guaranty amount, known as **entitlement**, represents the portion of the loan that the VA guarantees in the event of default by the borrowing veteran. Therefore, veterans can generally purchase a home priced up to **four times** the amount of their entitlement with no down payment.

All eligible veterans receive **$36,000 of basic entitlement**. Since the VA requires a minimum 25% of guaranty to meet secondary market requirements, the maximum loan amount a veteran would be eligible for using just basic entitlement would be $144,000 ($36,000 x 4 = $144,000). To account for the rise in the cost of homes, however, the Veteran's Benefits Improvement Act of 2008 provided that every eligible veteran receive a **bonus entitlement** that equals **25%** of the annual loan limit for single family homes in the **county where the property is located**.

In 2010, the single family home loan maximum for most counties is $417,000. This limit is significantly higher in some counties; for example, the 2010 loan limit in Marin County, CA, which is just north of San Francisco, is $962,500. A list of VA annual loan limits by county may be accessed from this website:

www.homeloans.va.gov/loan_limits.htm

The veteran's current eligible entitlement will be documented in the **Certificate of Eligibility** (COE). If the veteran's entitlement is insufficient—or if the purchase price/appraised value of the home exceeds the current VA loan limit for that county—the veteran can make a cash down payment so that the combination of entitlement and down payment equals the required guaranty of 25%. (Equity can also contribute to the 25% guaranty requirement for refinance loans.)

Restoring Entitlement

It is possible for a veteran to use some of his or her entitlement on a previous purchase, and have partial entitlement available for another purchase. Some or all of a veteran's entitlement previously used in connection with a VA home loan may be restored and used again for another VA loan under either of these circumstances:

- The property which secured the VA-guaranteed loan has been sold *and* that loan has been paid in full.
- An eligible veteran has agreed to assume the outstanding balance on a VA loan and substitute his or her entitlement for the same amount originally used on the loan. The assuming veteran must also meet occupancy, income, and credit requirements.

Case in Point

Let's look at some examples to illustrate. Assume each veteran is buying a home in a county where the current conforming loan limit for a single family home is **$417,000**, making the maximum guaranty **$104,250** ($417,000 x .25).

Example 1: Veteran Bob has full entitlement available and is purchasing a home for $350,000.

$350,000	Purchase Price
x .25	
$87,500	Guaranty Required

Since Bob has his entire entitlement of $104,250 available, he can purchase this house without a down payment. Even though he still has $16,750 in available entitlement, however, the loan-to-value on this purchase cannot exceed 100%.

Example 2: Veteran Ann wants to buy a house for $320,000. She has already used $27,500 of her entitlement on a prior loan, which has not been restored.

$ 104,250	Maximum Entitlement
- 27,500	Used Entitlement
76,750	Available Entitlement
$ 320,000	Purchase Price
x .25	
80,000	Guaranty Required
- 76,750	Available Entitlement
$ 3,250	Down Payment

If Ann wants to buy this house, she must convince the seller to lower the price, restore some of her entitlement, or make a down payment of $3,250.

Class Activity: Entitlement

Veteran Dave wants to buy a house for $480,000. He has his full entitlement of $104,250 available.

To buy this house, how much of a cash down payment must Dave make?

Borrower Qualifying Standards

Once a veteran's eligibility is confirmed, underwriters making VA loans must qualify the borrower to ensure that he or she is a satisfactory credit risk and has the means to repay loan. This is accomplished by looking at both the borrower's debt-to-income ratio and the residual income. If legally married, a spouse's income may also be considered for qualification purposes. A non-married co-borrower, however, is *not* allowed on a VA-guaranteed loan unless he or she is also an eligible veteran who will occupy the home as a primary residence.

Total Debt-to-Income Ratio

One difference from conventional underwriting is that underwriters on VA loans do not generally consider the housing expense ratio, also called the front end ratio. Instead, underwriters start with the total debt-to-income ratio, or back end ratio, when evaluating a potential borrower. In general, they also have more latitude than with conventional loans, generally looking for a total DTI that does not exceed **41%.**

√ **Note:** Tax-free income may be "grossed up" for purposes of calculating the debt-to-income ratio only, using current income tax withholding tables to determine an appropriate adjustment. Tax-free income generally includes certain military allowances, child support payments, workers' compensation benefits, disability retirement payments, and certain types of public assistance payments.

Class Activity: VA Loan Qualifying

A veteran with a family of three who lives in the Midwest is applying for $114,000 loan and has the following income and debts:

Gross Monthly Income:

	$1,950	Primary Employment
+	640	Part-time Employment
	$2,590	Total Income

Expenses:

	$ 706.42	Expected Housing Expense (PITI)
	209.00	Car Payment
	122.65	Student Loan
+	52.09	Revolving Credit Account
	$1,090.16	Total Expenses

What is the total debt-to-income ratio?

Residual Income

In addition to the debt-to-income ratio, an underwriter must ensure that an eligible borrower has the appropriate balance of cash flow remaining for family support. This is determined by looking at **residual income**, which is *the amount of income remaining after subtracting taxes, housing expenses, and all recurring debts and obligations.* Residual income uses **net effective income** in its calculation, not gross income. This analysis also takes the **size of the veteran's family** into consideration when determining whether the residual income meets the VA's minimum requirements. These figures are determined **regionally**, based on loan amount. The values shown in Figure 7.1 are simply for illustration purposes. VA alerts mortgage loan originators when income values are adjusted.

	Loan amounts $79,999 and below			
Family Size *	Northeast	Midwest	South	West
1	$390	$382	$382	$425
2	654	641	641	713
3	788	772	772	859
4	888	868	868	967
5	921	902	902	1,004

* Add $75 for each additional member up to a family of seven.

	Loan amounts $80,000 and above			
Family Size *	Northeast	Midwest	South	West
1	$450	$441	$441	$491
2	755	738	738	823
3	909	889	889	990
4	1,025	1,003	1,003	1,117
5	1,062	1,039	1,039	1,158

* Add $80 for each additional member up to a family of seven.

Figure 7.1: Residual Incomes by Region.

Class Activity: Residual Income

Let's say, that based on VA guidelines, a veteran with a family of three who lives in the Midwest applying for a $114,000 loan should have residual income of at least $889 in order to qualify:

$2,590.00	Gross Monthly Income
- $ 432.70	Income Tax Withheld
$2,157.30	Effective Net Income
- $1,090.16	Total Expenses
$1,067.14	Balance for Family Support (Residual Income)

While this borrower meets the residual income standard, recall that his total DTI was 42%. One way for a VA loan underwriter to justify approving a loan when the total DTI ratio exceeds 41% is if a borrower's residual income is at least 20% above the minimum standard established by the VA.

Does this family meet the income qualifications required for approval?

Other Factors to Consider

In addition to residual income and total debt-to-income, other factors an underwriter considers when evaluating a VA loan application include:

- Borrower's demonstrated ability to accumulate cash or other liquid assets, such as stocks or bonds
- Borrower's demonstrated ability to use credit wisely and to avoid incurring an excessive amount of debt
- Relationship between the housing expense for the property being acquired and what the borrower is accustomed to paying
- Number and ages of the borrower's dependents

- Location and general economic level of the subject property's neighborhood
- Likelihood that the borrower's income will increase or decrease
- Borrower's employment history and work experience
- Borrower's demonstrated ability and willingness to make payments on time
- Amount of any down payment made
- Borrower's available cash after paying all closing costs and any other prepaid items related to the purchase of the property

Property Guidelines for VA Loans

An existing home which has either been previously owner-occupied or had all onsite and offsite improvements fully completed for one year or more is eligible for a VA loan. Newly completed properties (completed less than one year and never owner-occupied) are eligible if covered by a one-year VA builder's warranty, enrolled in a HUD-accepted ten-year insured protection plan, or have been built by a veteran, as the general contractor, for his/her own occupancy. Some manufactured homes may also be eligible.

VA's minimum property requirements (MPRs) provide general acceptability criteria for properties that will become the security for VA-guaranteed loans.

Establishing the Reasonable Value

As with any mortgage loan, the value of the collateral being used to secure the note is critical. An appraisal is required to help ensure that any property that will become the security for a VA-guaranteed loan has a value of at least as much as the loan amount and that it is in a condition acceptable to the VA.

Every appraisal made for VA purposes must be reviewed either by the lender's VA-authorized staff appraisal reviewer or a VA staff appraiser, who then issues a **Notice of Value** (NOV) or a **Certificate of Reasonable Value** (CRV). Every NOV or CRV issued in conjunction with an appraisal review must include a list of any conditions and requirements that must be satisfied for the property to be eligible for VA loan guaranty.

The **established reasonable value** (or the sales price, whichever is less) defines the maximum mortgage amount a veteran may have on a VA-guaranteed loan for that property. If the price of the property exceeds the established reasonable value, the veteran must contribute the difference in cash to buy that property. The loan amount cannot exceed the established reasonable value, except to finance the required funding fee.

Occupancy

The law requires a veteran obtaining a VA-guaranteed loan to certify that he or she intends to personally occupy the property as his or her home. As of the date of certification, the veteran must either:

- Personally live in the property as his or her home, or
- Intend, upon completion of the loan and acquisition of the dwelling, to personally move into the property and use it as his or her home within a reasonable time, which generally means **within 60 days** after the loan closing.

Single or married service members, while deployed from their permanent duty station, are considered to be in a temporary duty status and able to meet the occupancy requirement.

VA Loan Regulations

Many terms of a VA loan, such as the interest rate, may be negotiated between the veteran borrower and the lender. However, VA does impose certain requirements and restrictions on loans that it guarantees, some of which are covered here.

Variable Funding Fee

While there is no upfront or monthly mortgage insurance premiums required for VA loans, borrowers must pay a non-refundable one-time **variable funding fee** at closing for guaranteeing the loan. The variable funding fee is waived for disabled veterans and surviving spouses of veterans who died in service or from service-connected disabilities.

The funding fee may be financed or paid in cash. If financed, the funding fee percentage must be applied to the loan amount. The fee is based on the veteran's status, the number of times the veteran has used the program, and the amount of any down payment:

VA Variable Funding Fees (% of loan amount on purchase, new construction)			
	Down Payment	**1st Use**	**Subsequent Use**
Regular Military	No down payment * Up to 9.9% down More than 10% down	2.15 % 1.50 % 1.25 %	3.30 % 1.75 % 1.50 %
National Guard and Reservists	No down payment * Up to 9.9% down More than 10% down	2.40 % 1.75 % 1.50 %	3.30 % 1.75 % 1.50 %
Interest Rate Reduction Refinancing Loans		.50 %	

* Also apply to cash-out refinancing loans

Figure 7.2: VA Variable Funding Fees.

Closing Costs

The veteran can pay a maximum of reasonable and customary amounts for any or all of the itemized fees and charges designated by VA, for example:

- Initial appraisals (VA certificate of reasonable value)
- Inspections
- Credit report
- Recording fees
- Insurance
- Title examination

Whenever the charge relates to services performed by a third party, the amount paid by the borrower must be limited to the actual charge of that third party.

In addition to the itemized charges, the lender may charge a **flat fee not to exceed 1% of the loan amount** to cover the lender's costs and services for originating the loan. If the loan does not close for any reason, the lender must refund this 1% flat fee.

Veteran borrowers cannot be charged commissions, brokerage fees, or buyer broker fees. In addition, VA will not allow the veteran to pay certain other "closing" fees, for example:

- Interest rate lock-in fees
- Tax service fee
- Notary fee
- Escrow fee

The seller, lender, or any other party may pay these fees and charges, including discount points, on behalf of the borrower. VA regulations do not limit the payment of such fees and charges by other parties.

Seller Concessions

A **seller concession** is *anything of value added to the transaction* by the builder or seller for which the buyer pays nothing additional and which the seller is *not* customarily expected or required to pay or provide, for example:

- Payment of the VA funding fee

- Prepayment of property taxes and/or insurance
- Gifts of personal property
- Payment of extra points to provide permanent interest rate buydowns
- Provision of escrowed funds to provide temporary interest rate buydowns
- Payoff of credit balances or judgments on behalf of the buyer

Payment of the buyer's closing costs or points that are appropriate to the market are *not* considered seller concessions.

Any seller concession or combination of concessions which **exceeds 4% of the established reasonable value** of the property is considered excessive, and unacceptable for VA-guaranteed loans. The reason for this restriction is to prevent concessions from enticing unwary and unqualified veterans into home mortgages they cannot afford.

Secondary Financing

The VA permits secondary financing simultaneous with a VA-guaranteed first loan for a variety of purposes, for example, closing costs or a down payment (unless the down payment is required to cover an excess purchase price beyond the VA's established reasonable value). The following conditions must be met:

- The veteran cannot be placed in a substantially worse position than if the entire amount borrowed had been guaranteed by VA.
- The second loan must be subordinated to the VA-guaranteed loan.
- There can be no cash-back to the veteran.
- The veteran must qualify for the second mortgage, which is underwritten as an additional recurring monthly obligation.
- The interest rate on the second mortgage may not exceed the rate on industry standards for second mortgage.
- The second mortgage should not restrict the veteran's ability to sell the property any more than the VA first mortgage (assumable).

Loan Assumption

All VA loans committed or closed prior to March 1, 1988, are freely assumable, meaning that the veteran may sell the property and allow the loan to be assumed without the approval of VA or the loan holder. The veteran still remains liable for any loss associated with the VA loan should the borrower assuming the loan fail to meet the mortgage obligations, however.

For VA loans committed and closed on or after March 1, 1988, VA loan assumptions are *not* allowed unless the veteran first has the assumption **approved** by the Department of Veterans Affairs or its authorized agent (i.e., the loan holder). If an assumption is approved by VA or the loan holder, the veteran is released of liability in the event the assumer defaults on the loan resulting in a loss to VA.

Entitlement associated with an assumption may only be restored to the veteran if these conditions are met:

- The assumer is an eligible veteran.
- The assumption has been approved by the loan holder or VA.
- The assumer-veteran agrees to substitute his or her VA home loan entitlement for the original veteran and occupies the property as his or her principal residence.

Prepayment Penalties

The VA does not allow clauses for prepayment penalties to be included in VA loans. VA loans may be paid off early without additional charges or penalties of any kind. (But the VA may allow these clauses for secondary financing.)

VA Loan Programs

VA Loan Program	Description	Conditions
Purchase Loans	• 100% financing for one- to four-family dwellings • Loan terms negotiated with lender • Repayment plans generally include: • Fixed • Traditional ARM • Hybrid ARM • Graduated payment • Growing equity	• Requires certification that veteran intends to occupy as primary residence • Veteran must have sufficient available entitlement, down payment, and/or equity for 25% guaranty • Requires non-refundable funding fee • Limits lender fee to flat 1% of loan amount
Interest Rate Reduction Refinance Loan (IRRRL or VA Streamline)	• VA-to-VA loan (vet re-uses entitlement) • Available to an original veteran who still owns the home, a surviving spouse of a deceased veteran, an original veteran with a new spouse, or a new veteran who has substituted entitlement • Must be used to lower interest rate, shorten the term of loan, or to change an ARM loan to a fixed rate of an existing VA-guaranty loan	• Requires only certification of prior residency • May add up to $6,000 of energy efficiency improvements to loan • Loan may not exceed sum of outstanding balance of existing loan (no cash-out) except for allowable closing costs, fees, and up to 2 discount points
Cash-Out Refinancing	• A refinance loan where proceeds may be used to pay off other liens or taken as cash for any purpose acceptable to the lender • Can be used to convert a non-VA loan to a VA loan • Veteran must have sufficient available entitlement	• Requires certification that veteran intends to occupy as primary residence • Must be secured by a first lien on the property • Maximum loan amount is 100% of appraised value + any energy efficiency improvements + VA funding fee

OMB Control No. 2900-0523
Respondent Burden: 30 minutes

Department of Veterans Affairs

LOAN ANALYSIS

LOAN NUMBER

PRIVACY ACT INFORMATION: The VA will not disclose information collected on this form to any source other than what has been authorized under the Privacy Act of 1974 or Title 5, Code of Federal Regulations 1.526 for routine uses as (i.e., the record of an individual who is covered by this system may be disclosed to a member of Congress or staff person acting for the member when the request is made on behalf of the individual) identified in the VA system of records, 55VA26, Loan Guaranty Home, Condominium and Manufactured Home Loan Applicant Records, Specially Adapted Housing Applicant Records, and Vendee Loan Applicant Records - VA, published in the Federal Register. Your obligation to respond is required in order to determine the veteran's qualifications for the loan.

RESPONDENT BURDEN: This information is needed to help determine a veteran's qualifications for a VA guaranteed loan. Title 38, USC, section 3710 authorizes collection of this information. We estimate that you will need an average of 30 minutes to review the instructions, find the information, and complete this form. VA cannot conduct or sponsor a collection of information unless a valid OMB control number is displayed. You are not required to respond to a collection of information if this number is not displayed. Valid OMB control numbers can be located on the OMB Internet Page at: **www.whitehouse.gov/omb/library/OMBINV.VA.EPA.html#VA.** If desired, you can call 1-800-827-1000 to get information on where to send comments or suggestions about this form.

SECTION A - LOAN DATA

1. NAME OF BORROWER	2. AMOUNT OF LOAN	3. CASH DOWN PAYMENT ON PURCHASE PRICE
	$	$

SECTION B - BORROWER'S PERSONAL AND FINANCIAL STATUS

4. APPLICANT'S AGE	5. OCCUPATION OF APPLICANT	6. NUMBER OF YEARS AT PRESENT EMPLOYMENT	7. LIQUID ASSETS *(Cash, savings, bonds, etc.)*	8. CURRENT MONTHLY HOUSING EXPENSE
			$	$
9. UTILITIES INCLUDED ☐ YES ☐ NO	10. SPOUSE'S AGE	11. OCCUPATION OF SPOUSE	12. NUMBER OF YEARS AT PRESENT EMPLOYMENT	13. AGE OF DEPENDENTS

NOTE: ROUND ALL DOLLAR AMOUNTS BELOW TO NEAREST WHOLE DOLLAR

SECTION C- ESTIMATED MONTHLY SHELTER EXPENSES *(This Property)*

SECTION D - DEBTS AND OBLIGATIONS ***(Itemize and indicate by (✓) which debts considered in Section E, Line 40)*** *(If additional space is needed please use reverse or attach a separate sheet)*

	ITEMS	AMOUNT		ITEMS	(✓)	MO. PAYMENT	UNPAID BAL.
14.	TERM OF LOAN: YRS.		22.			$	$
15.	MORTGAGE PAYMENT (Principal and Interest) @ ____________ %	$	23.				
			24.				
16.	REALTY TAXES		25.				
17.	HAZARD INSURANCE		26.				
18.	SPECIAL ASSESSMENTS		27.				
19.	MAINTENANCE & UTILITIES		28.				
20.	OTHER *(HOA, Condo fees, etc.)*		29.	JOB RELATED EXPENSE *(e.g., child care)*			
21.	TOTAL	$	30.	TOTAL		$	$

SECTION E - MONTHLY INCOME AND DEDUCTIONS

	ITEMS		SPOUSE	BORROWER	TOTAL
31.	GROSS SALARY OR EARNINGS FROM EMPLOYMENT				$
32.	DEDUCTIONS	FEDERAL INCOME TAX	$	$	
33.		STATE INCOME TAX			
34.		RETIREMENT OR SOCIAL SECURITY			
35.		OTHER *(Specify)*			
36.		TOTAL DEDUCTIONS	$	$	$
37.	NET TAKE-HOME PAY				
38.	PENSION, COMPENSATION OR OTHER NET INCOME *(Specify)*				
39.	TOTAL *(Sum of lines 37 and 38)*		$	$	$
40.	LESS THOSE OBLIGATIONS LISTED IN SECTION D WHICH SHOULD BE DEDUCTED FROM INCOME				
41.	TOTAL NET EFFECTIVE INCOME				$
42.	LESS ESTIMATED MONTHLY SHELTER EXPENSE *(Line 21)*				
43.	BALANCE AVAILABLE FOR FAMILY SUPPORT			GUIDELINE $	$
44.	RATIO *(Sum of Items 15, 16, 17, 18, 20 and 40 ÷ sum of Items 31 and 38)*				%

45. PAST CREDIT RECORD ☐ SATISFACTORY ☐ UNSATISFACTORY

46. DOES LOAN MEET VA CREDIT STANDARDS? *(Give reasons for decision under "Remarks," if necessary, e.g., borderline case)* ☐ YES ☐ NO

47. REMARKS *(Use reverse or attach a separate sheet, if necessary)*

CRV DATA (VA USE)

48A. VALUE	48B. EXPIRATION DATE	48C. ECONOMIC LIFE
		YRS.

SECTION F - DISPOSITION OF APPLICATION AND UNDERWRITER CERTIFICATION

☐ Recommend that the application be approved since it meets all requirements of Chapter 37, Title 38, U.S. Code and applicable VA Regulations and directives.

☐ Recommend that the application be disapproved for the reasons stated under "Remarks" above.

The undersigned underwriter certifies that he/she personally reviewed and approved this loan. *(Loan was closed on the automatic basis.)*

49. DATE	50. SIGNATURE OF EXAMINER/UNDERWRITER	
51. FINAL ACTION ☐ APPROVE APPLICATION ☐ REJECT APPLICATION	52. DATE	53. SIGNATURE AND TITLE OF APPROVING OFFICIAL

VA FORM SEP 2006 **26-6393**

EXISTING STOCKS OF VA FORM 26-6393, OCT 2005, WILL BE USED.

Sample VA 26-6393 Summary

Mortgage Exercise 7-2

Borrower Nan wants a VA loan to buy her first home. The home is priced at $114,900, and the estimate of reasonable value is $115,000. Nan has stable income, few debts, excellent credit history, but little cash on hand for a down payment. Nan has her COE and her DD-214 showing that she was honorably discharged from regular service in the U.S. Navy. *See the Appendix for answers to check your work.*

1. Do you think this loan can be made? Why or why not? If so, how much would the borrower have to pay at closing as a down payment?

2. What's the maximum flat fee the lender can charge on this loan? How much is the variable funding fee? Can either of these be financed into the loan? If so, what is the total loan amount? (Round to the nearest dollar.)

3. How much of her entitlement did Nan use on this loan?

4. Three years later, Nan wants to move to a bigger home. Can someone assume her mortgage? If so, under what circumstances will Nan be able to restore her entitlement?

Comparison of FHA and VA Qualifying Standards

FHA and VA qualifying standards tend to be more liberal than those for conventional loans. A borrower considered marginal by Fannie Mae and Freddie Mac may qualify more easily for an FHA or VA loan.

	FHA	VA
Borrower: Eligibility	Any qualified borrower	Eligible veteran only (COE and DD-214 or equivalent)
Property: Units Owner-Occupant Only	1-4 Yes (move in within 60 days)	1-4 Yes (move in within 60 days)
Maximum Loan (Neither can exceed appraisal)	Can't exceed maximum for geographic location	No limits
Borrower Qualifying Standards	Housing Expense Ratio: 31% Total Debt-to-Income: 43%	Residual income guidelines Total Debt-to-Income: 41%
Lender Protection	Insured to full extent of losses from default	Maximum guaranty amount = 25% loan limit/county
Maximum Interest Rate	Negotiated between borrower and lender	Negotiated between borrower and lender
Minimum Required Investment/Down Payment?	3.5% if credit score 580 or above 10% if between 500-579	None unless loan amount is greater than 4 times entitlement on COE
Fee/Insurance Premium Required	UFMIP 1.75%; monthly MIP up to 1.25% of annual average loan balance (as of 4/9/12)	Variable funding fee 1.25% to 3.30% (unless disabled); no insurance premium required
Fee Financed?	Yes (UFMIP only, not monthly)	Yes
Closing Costs Financed?	No	No
Seller Contribution Limit?	Yes, 6 points (proposed reduction to 3 points)	Discount points: No limit (if reasonable) Seller concessions: 4 points
Secondary Financing?	Yes, except minimum down payment	Yes
Assumable Loan?	Not without FHA creditworthiness check	Not without VA/lender approval
Prepayment Penalty?	No	No

Figure 7.3: Comparison of FHA and VA Loans.

USDA Rural Development Programs

In 1994, the U.S. Department of Agriculture (USDA) was reorganized under the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act. Under that Act, **USDA Rural Development** was created to administer the former Farmers Home Administration's (FmHA) non-farm financial programs for rural housing, community facilities, water and waste disposal, and rural businesses.

The opportunities available through the Rural Development **Housing and Community Facilities Programs** (HCFP) are extensive. For example, the USDA makes grants and loans to rural communities for essential facilities and services such as health clinics, schools, and fire and rescue stations. On the housing front, Rural Development has programs to assist with single family and multifamily housing, site preparation, rental assistance, water and waste, and repair and rehabilitation.

Although one mission of Rural Development is to provide financial support to low-income homebuyers in rural communities, the definition of "rural" may be broader than one might think. It can include small towns up to 20,000 people, even those in areas that may be in close proximity to larger metropolitan areas. In addition, the USDA could determine that particular areas are temporarily eligible for their programs in response to certain conditions or natural disasters such as a flood or hurricane. For this reason, a loan officer needs to verify whether the property is located in designated areas for specific programs.

Section 502 Loans

In the remainder of this chapter, we'll look at **Section 502 loans** for single family homes. The Section 502 loan program either **guarantees loans** made by approved private lenders or **makes direct loans** if no local lender is available. Section 502 loans can be used to:

- Purchase an existing home.
- Construct a new home.
- Renovate or repair an existing home.
- Relocate an existing home.
- Purchase and prepare a site for a home, including sewage and water facilities.

Under the Section 502 programs, eligible houses must be modest in size, design, and cost—defined as having a market value that does not exceed the applicable area loan limit and does not contain certain prohibited features.

Applicants for Section 502 loans—guaranteed and direct—must meet certain income requirements based on the **area median income** (AMI). Assuming that the applicant meets the income eligibility and the house is in an approved area, the borrower may receive **100% financing**, based on the appraised value or acquisition cost, whichever is less. The terms of the loan will be different depending on whether it is a guaranteed loan or a direct loan.

Effective October 1, 2011, USDA mortgage insurance rates are:

- For purchases, 2.00% upfront fee paid at closing, based on the loan size.
- For refinances, 1.00% upfront fee paid at closing, based on the loan size.
- For all loans, 0.30% annual fee, based on the remaining principal balance.

Note that the annual fee is for the life of the loan. It does not end with the loan-to-value reaches a certain point as with an FHA loan.

To check property eligibility and income limits for Section 502 Direct and Guaranteed loans, visit the USDA website:

http://eligibility.sc.egov.usda.gov/eligibility/

Guaranteed Rural Housing (GRH) Loans

The USDA guarantees loans made by approved lenders through the Section 502 Guaranteed Rural Housing Loan program. Approved lenders may be state housing agencies, any Farm Credit System institution with direct lending authority, or lenders approved by the VA, FHA, Fannie Mae, Freddie Mac, or Ginnie Mae. With these loans, the promissory note rate is set *by the lender.*

Lenders may require borrowers to pay an upfront guarantee fee of 2% when they take out the loan, but borrowers may be able to finance that fee under certain circumstances, allowing them up to **102% LTV**. Loan terms are fixed rate up to **30 years**.

Applicants for Section 502 guaranteed loans may have an income of up to **115%** of the area median income (AMI).

Homeownership Direct Loans

Mortgages obtained through the Direct Loan program are funded by the USDA. Promissory note rates for these direct loans are set by the Housing and Community Facilities Program based on the government's cost of money. The interest rate that the borrower actually pays may be modified by a payment assistance subsidy that could reduce the interest paid on the mortgage to as little as 1%.

Loan terms are up to **33 years** or up to **38 years** for those with incomes below 60% of AMI who cannot afford 33-year terms (limited to 30 years for manufactured housing).

Applicants for Section 502 direct loans must have **very low** or **low** incomes. Very low income is defined as **below 50%** of the area median income (AMI); low income is **between 50% and 80%** of AMI. With direct loans, payment subsidy is available to applicants to enhance repayment ability.

Chapter 7 Summary

1. For the purposes of this chapter, government agency financing refers to real estate loans that have been traditionally insured or guaranteed by government programs. This occurs at the federal level and should not be confused with government sponsored enterprises active in secondary markets. Government agency programs include FHA-insured, VA-guaranteed, and USDA Rural Development guaranteed and direct loans.
2. **FHA-insured** loans are for owner-occupied single family and multifamily dwellings of 4 or fewer units, made by approved lenders. FHA loans require lower down payments and less stringent qualifying standards than conventional loans. Direct Endorsers can underwrite FHA loans. The FHA sets a maximum mortgage amount, depending on the geographic area. HUD issues regulations for FHA loans, including: 1. Required minimum investment of **3.5%** of lesser of purchase price or appraised value with 580 credit score; 10% with 500-579 credit score; 2. UFMIP required (**1.75%** for most purchase and refinance; monthly MIP on annual average loan balance up to 1.25%; may be cancelled when original value reaches 78% LTV; 3. Assumable only with lender approval for loans on or after December 15, 1989; 4. Prepayment penalty not allowed, but lender can require pay off be made on due date or collect an extra month's interest; 5. Items paid by seller are negotiable, but seller contribution limited to 6 points (proposed reduction to 3 points). MLOs can stay current on FHA loan programs via Mortgagee Letters.
3. **VA-guaranteed** loans help eligible veterans buy homes often with no down payment. Veteran must occupy the home. VA doesn't limit home price, but limits guaranty amount that the lender can recover for default to 25% of maximum loan limit in county where property is located. VA loan rules include: 1. Borrower needs **DD-214** (discharge papers) and **COE** (Certificate of Eligibility); 2. VA issues **Notice of Value** (NOV) or **Certificate of Reasonable Value** (CRV) based on appraisal; if price exceeds estimate of reasonable value, veteran must make up difference with down payment/equity; 3. Secondary financing may be permitted; 4. Required variable **funding fee**—paid in cash or financed (waived for disabled veterans); Lender flat fee limited to 1% of loan amount. 5. No limit on seller contribution to closing costs; 4% limit on seller concessions; 6. Assumable by eligible veterans only with VA approval (for loans after March, 1, 1988); 7. Prepayment penalty not allowed; 8. Veteran may restore entitlement if loan is paid off, home is sold and mortgage assumed by eligible veteran.
4. **Rural Development** is an agency under the U.S. Department of Agriculture (USDA) that offers various assistance programs for both businesses and homebuyers in rural communities, which can include small towns and areas hit by natural disasters. The Rural Development's Housing and Community Facilities Programs **Section 502** loans for single family homes either **guarantees** loans made by private lenders or makes **direct loans** if no local lender is available. Eligible borrowers can get **102% financing**. There is an upfront guaranty fee and an annual fee. Applicants for Section 502 Guaranteed Loans may have an income of up to **115%** of the area median income (AMI). Applicants for Section 502 Direct Loans must have **very low** (below 50% AMI) or **low** (between 50% and 80% of AMI) incomes.

Chapter 7 Quiz

1. ***A borrower with a FICO score of 700 applies for an FHA loan on a house with an appraised value of $100,000 and a purchase price of $96,000. What is the required minimum investment?***
   A. $3,000
   B. $3,360
   C. $3,500
   D. $4,800

2. ***An upfront mortgage insurance premium is required***
   A. on all FHA loans.
   B. only when the buyer cannot pay the required down payment in cash.
   C. only when the LTV exceeds 80%.
   D. only when the LTV exceeds 90%.

3. ***Which statement about FHA-insured loans is FALSE?***
   A. FHA loans are intended for low-income first-time homebuyers.
   B. FHA loans have less stringent qualifying standards.
   C. FHA loans require low down payments.
   D. FHA offers an adjustable rate mortgage.

4. ***To qualify for an FHA loan, a borrower should have a maximum housing expense ratio of _____and a total debt-to-income ratio of _____***
   A. 28%; 36%.
   B. 29%; 36%.
   C. 29%; 41%.
   D. 31%; 43%.

5. ***FHA-insured loans are funded by***
   A. approved lenders.
   B. the Department of Housing and Urban Development.
   C. the Federal Deposit Insurance Corporation.
   D. the Federal Housing Administration.

6. ***The VA provides guaranty on eligible home loans for up to ______ of the loan amount.***
   A. 10%
   B. 25%
   C. 50%
   D. 100%

7. ***A veteran's entitlement for a VA loans is specified in what document?***
   A. COE
   B. CRV
   C. DD-214
   D. NOV

8. ***What is the maximum flat fee that a lender may charge on a VA loan?***
   A. 3.5%
   B. 2%
   C. 1%
   D. There is no limit; the fee is negotiable.

9. ***Full VA entitlement can generally be restored to a veteran***
   A. if any disabled veteran assumes the loan.
   B. if an eligible veteran substitutes his entitlement for the seller's.
   C. when the loan is paid down to below 50% LTV.
   D. under no circumstances.

10. ***The VA may use what document to determine the maximum loan amount on the property being used as collateral?***
   A. county tax assessment roll
   B. DD-214
   C. notice of value
   D. sales contract

11. ***Section 502 home loans are administered by which federal agency?***
   A. Department of Housing and Urban Development
   B. Federal Housing Administration
   C. Federal Housing Finance Agency
   D. U.S. Department of Agriculture

12. ***A buyer wishes to purchase a home in a designated rural community where the area median income is $50,000. What is the maximum LTV allowed for a Rural Development Section 502 guaranteed loan?***
   A. 80%
   B. 90%
   C. 100%
   D. 102%