

MORTGAGE LENDING UPDATE

By David Griffin

Past President of Mortgage Bankers Association of Middle Georgia

FHA Home Loans

With the collapse of the sub-prime mortgage market and many other similar mortgage programs blamed for the housing crisis, Federal Housing Administration (FHA) mortgage loans have been called upon to fill the gap. FHA mortgage loan programs are administered by the Department of Housing and Urban Development (HUD). FHA was originally created in the 1930's to help pull the country out of the Great Depression and to provide an avenue for average folks to become homeowners.

The number of home loans insured by FHA recently fell to its lowest point in the summer of 2005 when only 5% of the nation's mortgages originated were FHA loans. FHA now insures nearly a third of all the nation's home loans. FHA loans haven't had that kind of market share since about 1990. This is a sign of just how dramatically the mortgage market has changed.

You will recall that a few short years ago just about anybody could get a home loan. There were a lot of different mortgage options such as subprime loans for people with low credit scores or stated-income loans for those who didn't tell Uncle Sam everything and 100% conventional loans or piggyback mortgages that essentially meant buyers didn't have to make a down payment. Those programs are now history and you've seen the results.

FHA loans are back in fashion and how. There are a number of reasons. Principally, FHA loans are popular because of the low down payment allowed. Purchasers of homes under the FHA home loan program are only asked to have a minimum of 3.5% cash investment for down payment. The full amount of that down payment or any other required closing costs can also be a gift from a relative or family member. A gift letter is required and full documentation of the gift itself and the borrower's receipt of the gift must be furnished. The seller may pay closing costs and the buyer's prepaid expenses (escrows) up to a maximum of 6% of the sales price.

The maximum FHA loan amount for single family homes is \$271,050, which should be enough for most folks. Compare that with conventional guidelines which do allow mortgage amounts up to \$417,000, but are increasingly requiring a minimum down payment of 10%.

FHA Mortgage Insurance Premium (MIP) is required on all FHA loans. The "up-front" MIP is 1.75% of the "base" (sales price less down payment) loan amount and is most often added to that base loan amount to arrive at the "total" loan amount. The annual renewals of MIP are .55% of the loan amount and are paid into escrow monthly until the loan to value (LTV) falls to 78% or for 5 years, whichever happens last.

There are two payment ratios applicable to FHA loans. The "housing" ratio is determined by taking the total new monthly house payment including escrows and dividing the total by the gross (before taxes) monthly income of the applicants. This ratio should not exceed 29%. The second ratio is the "total debt" ratio. This ratio is determined by taking the total monthly new house payment and adding all other required monthly repayments for installment loans, credit cards and child support or other obligations, then dividing that grand total by the same gross monthly income of the applicants. This ratio should not exceed 41%. With compensating factors such as excellent credit and/or large cash reserves, these ratios can even be exceeded.

Employment and residency will be verified for the previous 2 years. Stable employment with the same employer for the previous 12 months should exist, unless a job change was within the same field and for career advancement. Recent employment after completion of education or military service in the same field is acceptable.

A minimum middle credit score of 620 is usually required. However, if an applicant does not have a history of credit use, perhaps because they pay by cash and do not borrow, it is possible that a "substitute" credit profile could be developed to prove the applicant is an acceptable credit risk for FHA purposes. This could be accomplished by verifying the manner in which the applicant paid their rent to a former landlord, and by verifying the timely payment of gas, water, electricity or phone bills. Loans of this type would naturally have to be manually underwritten and not run through the normal automated underwriting systems (AUS). A straight (Chapter 7) bankruptcy will normally have to be discharged for two years and any prior foreclosure aged for 3 years.

Now, how 'bout those WRALL WORLD CHAMPION softball players?

David Griffin has been financing homes in Macon, Warner Robins and all of Middle Georgia since 1983 and is a member of the Mortgage Bankers Association of Georgia, mbag.org. For an archive of past articles visit mbag.org/ML_Update.htm.(8/20/09)