

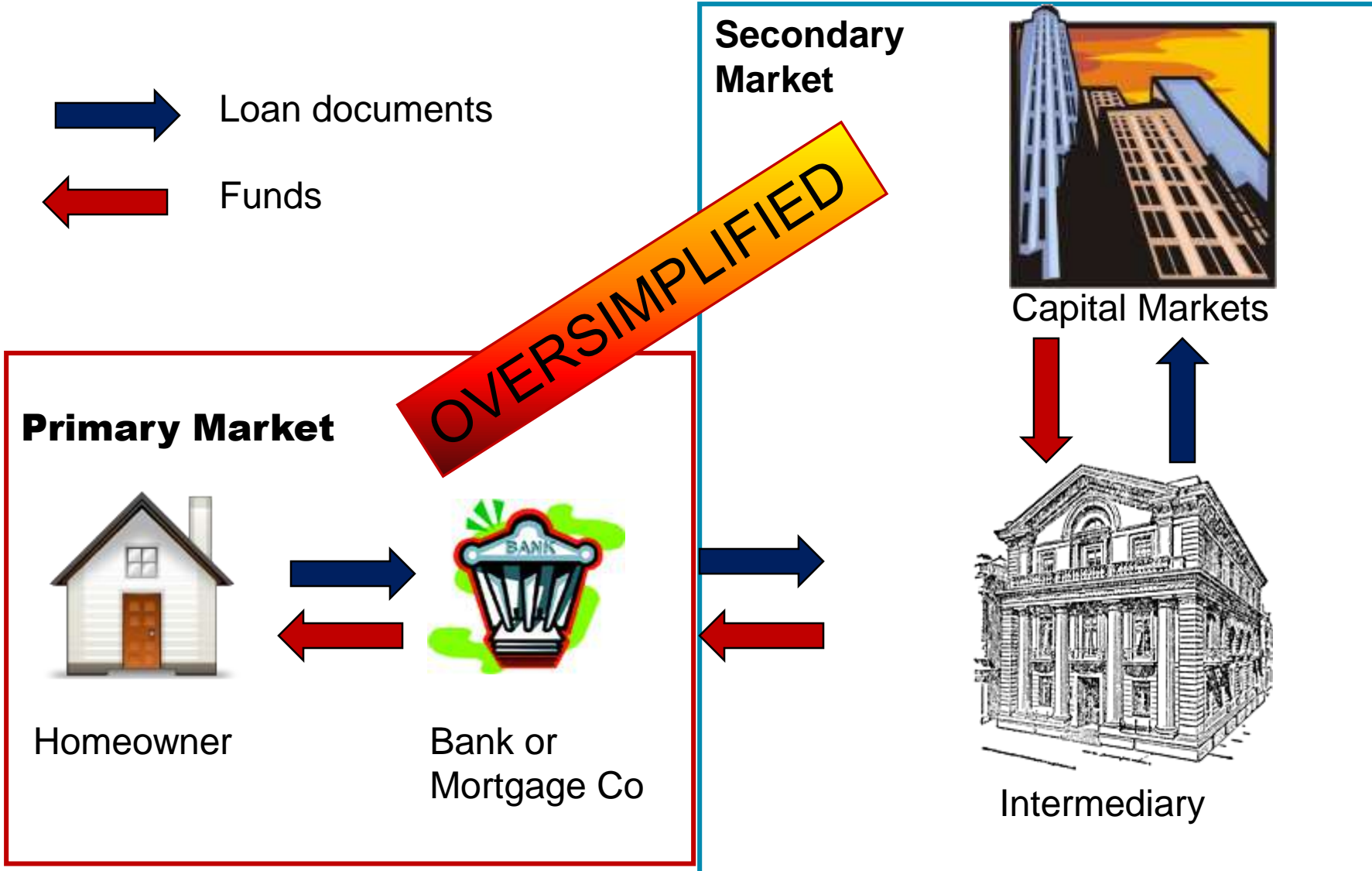
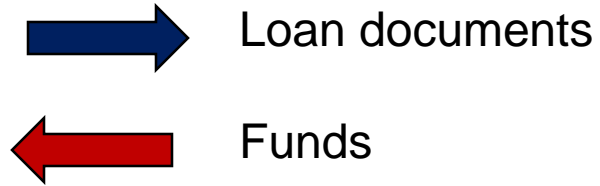
Chapter 8

Underwriting and Financing Residential Properties

Before covering this chapter, we'll cover a special topic (more later in course)

Introduction to Secondary Mortgage Market

Secondary Mortgage Market



The Players (the intermediaries)



Fannie Mae



Freddie Mac



Others

GSE's
(Government Sponsored
Enterprises)

Historically referred to as
"Agencies"

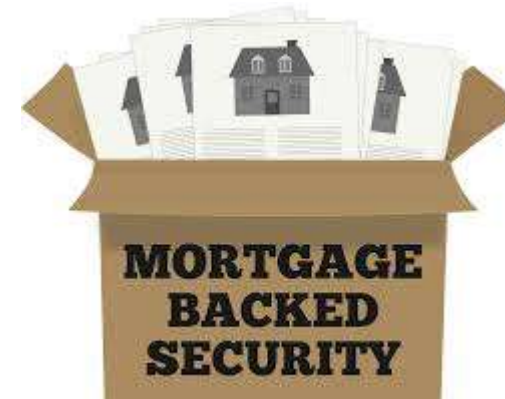
The term "Agency Loans"
sometimes used to refer
to those qualified to be
purchased by one of
these.

Securitization - Concept

“Pool” of mortgages



“Bonds” or Securities
Backed by (secured by) the pool



Now, back to our chapter

Classification of Mortgage Loans

- **FHA Insured** Mortgages (Federal Housing Administration)
 - Part of insurance is “one-time” paid at closing
 - Ongoing mortgage insurance premium (MIP)*
 - See: <http://www.zillow.com/mortgage-learning/fha-loan>
- **VA Guaranteed** Mortgages (Veteran’s Administration)
- **Conventional** Mortgages (may require “private” insurance)
 - Conforming
 - Non-conforming

Classification of Mortgage Loans

Mortgage Classifications in Marketplace		
FHA (&VA) - Gov't sponsored	Conventional	
	Conforming	Non-conforming
High LTV	Underwriting Rules	
Loan Limits	Loan Limits	No limits
Insurance: fees to government	Possible private insurance	
Low interest rates	Reasonable rates	Higher rates
<u>Important Names</u>		
FHA	Fannie	Jumbo Loans
VA	Freddie	Alt-A loans
		Subprime loans

Classification of Mortgage Loans

- Conventional Mortgages
 - No government guarantee or insurance
 - May require private mortgage insurance
- Conforming loans
 - Meet government sponsored enterprises (“GSE”) loan limit requirements
- Nonconforming
 - “Jumbo” loans
 - Large dollar amount loans
 - Higher interest rate
 - Subprime
 - ALT A (or “low-doc”) (alternative to “A” paper)

Classification of Mortgage Loans

- Privately Insured Conventional Mortgages
 - LTV usually > 80% (Less than 20% down)
 - Private Mortgage Insurance
 - Insurer assumes default risk of the larger loan
 - Covers loan amount > 80% LTV
 - Can be eliminated if LTV falls
 - Homeowners Protection Act helps borrowers

Classification of Mortgage Loans - Details

- FHA Insured Mortgages
 - Lender completely insured against default loss
 - Strict qualification procedures for borrower and property
 - Lower borrower down payments
 - Loan maximums
 - Most are fixed term (15 to 30 yrs)

Classification of Mortgage Loans - Details

- VA Guaranteed Mortgages
 - Qualified veterans
 - Very structured program
 - Guarantee may not exceed 25% of loan
 - Certificate of reasonable value (“CRV”)
 - Loan entitlement caps and restoration unique to veteran.
 - Unlike FHA program, the VA is providing a loan guarantee, not default insurance

Underwriting Default Risk

- Loan Types
- Qualifying the borrower and property
 - Borrower loan application
 - Property appraisal
- Default insurance
- Payment-to-income ratio
- Loan-to-value ratio

Underwriting Process

- Borrower Income
 - Verify employer, wages, expected continuity
 - Verify other income
 - Will it continue?
 - Is it verifiable on prior tax returns?
 - Dual income
 - Stability of joint income

Underwriting Process

- Borrower Assets
 - Verify closing cost and down payment funds
 - Additional savings and investments
- Credit History
 - Credit reports
 - Credit scoring models
 - FICO score

Underwriting Process

- Ratios of Monthly Expense to Income
 - Housing expense to Income
 - Total Obligations to Income
- Housing Expenses
 - Principal & Interest
 - Mortgage insurance
 - Property taxes
 - Hazard insurance
 - Homeowners association dues (if applicable)
- Other Obligations
 - Auto loans, credit cards, child support etc.

Automated Underwriting

- Use of technology to assist
- Fannie: Desktop Underwriter (DU)
- Freddie: Loan Prospector (LP)

The “Closing” Process

- Loan and title transfer happen at the same time.
- Title company usually acts as Settlement Agent.
Closing will show all funds.
 - Financing costs (borrower)
 - Property tax proration
 - Escrow accounts
 - Property taxes
 - Hazard insurance (or Homeowner’s Insurance)
 - Mortgage insurance

The Closing Process

- Title insurance, lawyer's title opinion
- Release fees
- Attorney's fees
- Pest inspection
- Real estate commission
- Statutory Costs
 - Recording fees
 - Transfer taxes
- Mortgage cancellation insurance (optional life)

Problem 8-4 Residential Closing

Real Estate Settlements and Procedures Act ("RESPA")

- Consumer Information
- Advance disclosure of settlement costs
- Title Insurance Placement
- Prohibition on Kickbacks & Referral Fees
- Uniform Settlement Statement (Closing Disclosure)
- Advanced Inspection of Uniform Settlement Statement
- Escrow Deposits

Truth-In-Lending Law

- Disclosure requirements
 - Annual Percentage Rate (APR)
 - This law does not apply to commercial transactions.
-
- In general, there are more consumer protections in place for residential real estate ownership, lending, and tenancy than there are for the commercial side of the industry.

Insurance Recap

- Hazard Insurance
 - Fire, flood etc. Continuing cost of property owner. Likely to be escrowed. (**Homeowners insurance** includes this and some additional).
- Title Insurance
 - One time closing cost. Usually a policy for the owner and a separate policy for lender. No escrow requirement as settled at closing
- Mortgage Insurance
 - To insure lender against default. Likely to be escrowed