Chapter 12

Real Property Financing

Chapter 12 Goals:

- How loan policy initiated by the Federal Reserve affects the availability and qualification of mortgage programs
- How interest rates effect the real estate market
- Basic guidelines for loan approval
- The role of private and public financing
- Primary and secondary financing
- Loan Disclosures
- Various mortgage types and programs
- Various government institutions that effect mortgage policy such as the FHA and VA
- Mortgage regulations set by the state and federal government
- The loan process

Chapter 12: Real Property Financing

Key Terms

80-20 loan adjustable-rate mortgage (ARM) adjustment period amortization assumable ARM back-end qualification blanket trust deed buyer qualification CalVet loan cap rate collateral conventional loan convertible ARM cosigner direct endorsement due-on-sale clause Federal Housing Administration (FHA)	FICO score fixed-rate loan front-end qualification gap loan gross income hard money loan Housing Affordability Index hybrid loan index rate interest-only loan loan-to-value (LTV) ratio loan servicing margin mortgage loan costs mortgage qualification ratio negative amortization open-ended mortgage	option ARM partial release clause prepayment penalty private mortgage insurance (PMI) renegotiable-rate mortgage reverse mortgage seller carryback financing Servicemen's Readjustment Act of 1944 servicing a loan Uniform Residential Loan Application VA loan verification of employment form wraparound mortgage

Chapter Overview

In this chapter, readers will learn about:

- The criteria used to qualify a borrower for a loan
- The borrower qualification process
- How to choose the best loan
- The various mortgage types, including fixed-rate loans and ARMs

Qualifying a Buyer

Nearly nine out of ten home purchases require some form of a loan. A buyer's ability to get successfully approved for a loan will ultimately determine whether or not a transaction closes.

The worst thing that an agent can do is spend time finding a buyer's dream home, negotiating the terms of the sale, and being ready to close the deal… only to discover that the buyer's application for a home loan has been rejected.

An agent should ensure that a prospective buyer has the necessary capital and credit to purchase a home prior to beginning his or her representation efforts. An agent can do this by kindly requesting that a buyer get preapproved for a loan.

Not only will this allow a buyer to be more invested in the purchase process, it will also prevent an agent from wasting time on finding homes for which the buyer may not be qualified to purchase.

Furthermore, sellers take offers from prequalified buyers more seriously. If a seller has multiple offers, he or she will generally accept an offer from a pre-approved buyer as that transaction can close the fastest. An agent must make a buyer understand that the buyer must be preapproved in order to submit a competitive offer.

As soon as a buyer is ready to purchase a home, he or she should submit a loan application to a lender and get prequalified.

There is no set industry standard for determining a borrower's qualification for a loan; each lender uses its own guidelines for qualification and they can be altered on a case-by-case basis.

However, in order to minimize risk and maximize profit, most lenders utilize the three Cs of the qualification process:

- Credit
- Capacity
- Collateral

Credit

Lenders use a borrower's credit history as evidence of his or her financial stability. A prospective borrower's FICO score is often used as evidence of that credit history. A **FICO score** includes:

a. How long a borrower has had established credit
b. Percentage of credit used vs. available credit
c. Payment patterns
d. Total debt (i.e. school loans, car loans, credit cards, mortgages)
e. Late payments
f. Negative credit experiences

Credit scores generally range from 300 to 840. A 720 credit score is the minimum qualifying score for most traditional mortgage programs.

How to Build a Good Credit Score

- *Open a checking and savings account.* The minimum deposit for each account is at least $250. Having multiple accounts with money in them demonstrates to credit agencies that an account holder has financial history.

- *Apply for a major credit card.* Open lines of credit also allow a borrower to establish financial history. A borrower's credit score typically increases within six to twelve months after consistent credit card payments.

- *Make payments on time.* A borrower's ability to make payments prior to the conclusion of a billing cycle is proof to lenders that the borrower is responsible and has the capacity to meet debt obligations. Lenders and credit card companies increase a borrower's line of credit and borrowing ability after making consistent, timely payments.

In addition to a borrower's credit score, a lender takes into consideration the type of debts a borrower has previously taken on. If a borrower has borrowed and fully paid off large debts in the past, a lender can be more confident that its loan will be paid back on time.

Capacity

Before providing a loan, a lender must determine whether a borrower has the income and financial stability (or "capacity") to afford monthly mortgage payments throughout the duration of the loan. Put another way, a lender must assess its level of risk in providing a loan to a particular buyer.

A lender will evaluate a borrower's entire financial situation, including:

- Employment/Income
- Assets
- Debt-to-income ratio
- Down payment amount
- Loan-to-value (LTV) ratio

Employment/Income

A prospective borrower must state his or her employment and income on a **verification of employment form**. A lender will send this form directly to the borrower's employer for verification.

A borrower's form of employment impacts his or her ability to pay back a loan. If a borrower's job is reliable and consistent, he or she is more likely to make mortgage payments on time; if a borrower's job is seasonal or in a high-risk industry, he or she might be more susceptible to missing payments.

Loan qualification can be difficult for prospective borrowers who are self-employed, as it is difficult for them to demonstrate income. Certain lenders specialize in providing creative financing solutions for self-employed borrowers.

Lenders typically use gross income when evaluating a borrower's income. **Gross income** refers to total income prior to taxes and deductions. Most loan programs stipulate that a borrower's income cannot exceed 33% of the total household gross income. This means that in order to qualify for a mortgage the borrower/s mortgage payments cannot be higher than 33% of the household income. This is used as an approval guideline to ensure the lender that the borrower has the financial means to pay back the debt.

The **Housing Affordability Index** determines a borrower's level of affordability as it relates to purchasing property. The National Association of Realtors produces the Index on a monthly basis. It analyzes the most recent price and income data to determine whether a typical family earns enough income to qualify for a mortgage loan based on a typical home. A number above 100 means a borrower has the income required to afford mortgage payments for a subject property; a borrower below 100 does not.

In the case of married couples, most lenders accept both spouses' income in the qualification process. A lender may require both spouses to sign the loan application. A second signatory on a loan is known as a **cosigner**.

A cosigner with strong credit and income can strengthen a borrower's loan application as it increases the borrower's ability to pay back the loan and significantly reduces a lender's risk. Having a co-signer may encourage a lender to reduce the down payment requirement.

Loan-To-Value (LTV) Ratio

A **loan-to-value (LTV) ratio** is the value of a loan compared to the value of the asset purchased with the loan. The higher the LTV percentage, the greater the risk is for a lender. The LTV is also known as the **mortgage qualification ratio**.

The LTV determines a borrower's monthly costs using either front-end or back-end qualification.

Front-End Qualification

Front-end qualification determines a borrower's loan qualification by comparing a monthly mortgage payment (including principal, interest, taxes and insurance) to the borrower's income.

Lenders traditionally use a borrower's gross income to calculate the ratio (as opposed to their net income). Most banks have a maximum front-end lending ratio of 28%, which means that a borrower's housing costs cannot exceed 28% of their total income or up to 30% in some scenarios.

The following formula is used to calculate front-end qualification method:

Total Monthly Payment / Gross Monthly Income

= **Front-End Qualification**

For example, say a borrower has a monthly income of $5,500 and a monthly mortgage payment would be $1,520 a month. Using front-end qualification ($1,520/$5,500), the borrower's front-end percentage is 27.63%. This means that the borrower would likely qualify for a loan.

The following chart lists the maximum monthly mortgage payment a borrower can qualify for under front-end qualification based on their income level:

Gross Annual Income	**Monthly Mortgage Payment**
$30,000	$700
$40,000	$933
$50,000	$1,167
$60,000	$1,400
$70,000	$1,633
$80,000	$1,867
$90,000	$2,100
$100,000	$2,333
$130,000	$3,033
$150,000	$3,500
$175,000	$4,088

$200,000	$4,667
$250,000	$5,833

Back-End Qualification

Back-end qualification considers a borrower's total monthly debt obligations as compared to his or her income. Debt obligations include all mortgages, credit card debt, and student debt. Most lenders do not qualify borrowers that exceed a back-end percentage of 36% or sometimes up to 40%.

The following formula is used to calculate back-end qualification method:

Total Monthly Debt Obligations /

Gross Monthly Income

= Cannot Exceed 36%

For example, say a borrower makes $5,500 a month and has monthly debts that total $1,900. Using back-end qualification ($1,900/$5,500), the borrower's back-end percentage is 34.5%. This means that the borrower would likely qualify for a loan.

The following chart lists the maximum monthly mortgage payment a borrower can qualify for under back-end qualification based on their income level:

Gross Annual Income	Monthly Mortgage Payment
$30,000	$700
$40,000	$1,200
$50,000	$1,500
$60,000	$1,800
$70,000	$2,100
$80,000	$2,400
$90,000	$2,700
$100,000	$3,000
$130,000	$3,900
$150,000	$4,600

$175,000	$5,250
$200,000	$6,000
$250,000	$7,500

If a borrower is very close to the cut-off for qualification, a lender may require the borrower to increase his or her down payment amount.

Mortgage Qualification Ratios

There are two ratios used to qualify borrowers for mortgage programs. Lenders may use one or both ratios to determine eligibility.

1. Front-end ratio
2. Back-end ratio

Front-End Ratio (28% maximum)

$$\frac{\text{PITI (Principal, Interest, Taxes \& Insurance)}}{\text{Borrower's Monthly Gross Income}} = .28 \text{ or less}$$

Back-End Ratio (36% maximum)

$$\frac{\text{Total Loan Obligations}}{\text{Borrowers Monthly Gross Income}} = .36 \text{ or less}$$

A lender will request proof of a borrower's financials in the form of:

- Tax returns
- Bank statements
- Paystubs
- Investments
- Profit and loss
- Investment income
- Rental income
- Financial statement of assets and liabilities
- Letter of explanation of financials

- Other debt obligations

Collateral

Collateral involves a borrower pledging some form of security to a lender in exchange for securing a loan. If the borrower defaults on the loan, the lender is entitled to that collateral.

Lenders hire a professional property appraiser to determine the current and projected value of a subject property. The property's appraised value is equity that serves as collateral for a lender's loan.

That way, if a borrower defaults on a lender's loan, the lender is entitled to sell the borrower's property to recoup its losses.

A lender also requires a sizable down payment in order to minimize its risk. A large down payment ensures that a borrower has a vested interest in a property and provides a lender with cash collateral in the event that the borrower defaults.

Traditionally, minimum down payment requirements for home purchases were 3% of the purchase price. However, on January 1, 2009, the minimum down payment requirement increased to 3.5%.

If a property's appraised value is lower than a seller's listing price, a lender may require a borrower to make a higher down payment. This protects a lender's investment by adjusting for a property's true value.

Originating a Loan

Borrowers can initiate the loan process – or "originate a loan" – in person, over the phone, or online.

Applying in person may be the most effective option, particularly if a borrower has unique financial circumstances (i.e. self-employed).

To apply in person or on the phone, a borrower/buyer or the borrower/buyer's agent directly contacts a lender. If a borrower/buyer is established with a particular bank or credit union, he or she should contact that institution.

Online resources for originating loans include:

- MortgageLoanGo.com
- QuickenLoans.com
- Zillow.com

- WellsFargo.com
- ELoan.com

Originating a loan requires a borrower to submit his or her loan application and all documentation required by a lender. At this point, a borrower/buyer and the borrower/buyer's agent should compare various mortgage programs and select the one that best fits a borrower/buyer's needs.

Uniform Residential Loan Application

This application is designed to be completed by the applicant(s) with the Lender's assistance. Applicants should complete this form as "Borrower" or "Co-Borrower," as applicable. Co-Borrower information must also be provided (and the appropriate box checked) when ☐ the income or assets of a person other than the Borrower (including the Borrower's spouse) will be used as a basis for loan qualification or ☐ the income or assets of the Borrower's spouse or other person who has community property rights pursuant to state law will not be used as a basis for loan qualification, but his or her liabilities must be considered because the spouse or other person has community property rights pursuant to applicable law and Borrower resides in a community property state, the security property is located in a community property state, or the Borrower is relying on other property located in a community property state as a basis for repayment of the loan.

If this is an application for joint credit, Borrower and Co-Borrower each agree that we intend to apply for joint credit (sign below):

Borrower Co-Borrower

I. TYPE OF MORTGAGE AND TERMS OF LOAN

Mortgage Applied for:	☐ VA ☐ FHA	☐ Conventional ☐ USDA/Rural Housing Service	☐ Other (explain):	Agency Case Number	Lender Case Number
Amount $	Interest Rate %	No. of Months	**Amortization Type:**	☐ Fixed Rate ☐ GPM	☐ Other (explain): ☐ ARM (type):

II. PROPERTY INFORMATION AND PURPOSE OF LOAN

Subject Property Address (street, city, state & ZIP)	No. of Units
Legal Description of Subject Property (attach description if necessary)	Year Built

Purpose of Loan ☐ Purchase ☐ Refinance ☐ Construction ☐ Construction-Permanent ☐ Other (explain): | Property will be: ☐ Primary Residence ☐ Secondary Residence ☐ Investment

Complete this line if construction or construction-permanent loan.

Year Lot Acquired	Original Cost	Amount Existing Liens	(a) Present Value of Lot	(b) Cost of Improvements	Total (a + b)
	$	$	$	$	$

Complete this line if this is a refinance loan.

Year Acquired	Original Cost	Amount Existing Liens	Purpose of Refinance	Describe Improvements ☐ made ☐ to be made
	$	$		Cost: $

Title will be held in what Name(s)	Manner in which Title will be held	Estate will be held in: ☐ Fee Simple ☐ Leasehold (show expiration date)
Source of Down Payment, Settlement Charges, and/or Subordinate Financing (explain)		

Borrower III. BORROWER INFORMATION Co-Borrower

Borrower				Co-Borrower			
Borrower's Name (include Jr. or Sr. if applicable)				Co-Borrower's Name (include Jr. or Sr. if applicable)			
Social Security Number	Home Phone (incl. area code)	DOB (mm/dd/yyyy)	Yrs. School	Social Security Number	Home Phone (incl. area code)	DOB (mm/dd/yyyy)	Yrs. School
☐ Married ☐ Separated	☐ Unmarried (include single, divorced, widowed)	Dependents (not listed by Co-Borrower) no. ages		☐ Married ☐ Separated	☐ Unmarried (include single, divorced, widowed)	Dependents (not listed by Borrower) no. ages	
Present Address (street, city, state, ZIP)		☐ Own ☐ Rent ____No. Yrs.		Present Address (street, city, state, ZIP)		☐ Own ☐ Rent ____No. Yrs.	
Mailing Address, if different from Present Address				Mailing Address, if different from Present Address			

If residing at present address for less than two years, complete the following:

Former Address (street, city, state, ZIP)	☐ Own ☐ Rent ____No. Yrs.	Former Address (street, city, state, ZIP)	☐ Own ☐ Rent ____No. Yrs.

Borrower IV. EMPLOYMENT INFORMATION Co-Borrower

Borrower			Co-Borrower		
Name & Address of Employer	☐ Self Employed	Yrs. on this job	Name & Address of Employer	☐ Self Employed	Yrs. on this job
		Yrs. employed in this line of work/profession			Yrs. employed in this line of work/profession
Position/Title/Type of Business	Business Phone (incl. area code)		Position/Title/Type of Business	Business Phone (incl. area code)	

If employed in current position for less than two years or if currently employed in more than one position, complete the following:

IV. EMPLOYMENT INFORMATION (cont'd)

Borrower			Co-Borrower		
Name & Address of Employer	☐ Self Employed	Dates (from – to)	Name & Address of Employer	☐ Self Employed	Dates (from – to)
		Monthly Income $			Monthly Income $
Position/Title/Type of Business	Business Phone (incl. area code)		Position/Title/Type of Business	Business Phone (incl. area code)	
Name & Address of Employer	☐ Self Employed	Dates (from – to)	Name & Address of Employer	☐ Self Employed	Dates (from – to)
		Monthly Income $			Monthly Income $
Position/Title/Type of Business	Business Phone (incl. area code)		Position/Title/Type of Business	Business Phone (incl. area code)	

V. MONTHLY INCOME AND COMBINED HOUSING EXPENSE INFORMATION

Gross Monthly Income	Borrower	Co-Borrower	Total	Combined Monthly Housing Expense	Present	Proposed
Base Empl. Income*	$	$	$	Rent	$	
Overtime				First Mortgage (P&I)		$
Bonuses				Other Financing (P&I)		
Commissions				Hazard Insurance		
Dividends/Interest				Real Estate Taxes		
Net Rental Income				Mortgage Insurance		
Other (before completing, see the notice in "describe other income," below)				Homeowner Assn. Dues		
				Other:		
Total	$	$	$	**Total**	$	$

* **Self Employed Borrower(s) may be required to provide additional documentation such as tax returns and financial statements.**

Describe Other Income

Notice: **Alimony, child support, or separate maintenance income need not be revealed if the Borrower (B) or Co-Borrower (C) does not choose to have it considered for repaying this loan.**

B/C		Monthly Amount
		$

VI. ASSETS AND LIABILITIES

This Statement and any applicable supporting schedules may be completed jointly by both married and unmarried Co-Borrowers if their assets and liabilities are sufficiently joined so that the Statement can be meaningfully and fairly presented on a combined basis; otherwise, separate Statements and Schedules are required. If the Co-Borrower section was completed about a non-applicant spouse or other person, this Statement and supporting schedules must be completed about that spouse or other person also.

Completed ☐ Jointly ☐ Not Jointly

ASSETS Description	Cash or Market Value	Liabilities and Pledged Assets. List the creditor's name, address, and account number for all outstanding debts, including automobile loans, revolving charge accounts, real estate loans, alimony, child support, stock pledges, etc. Use continuation sheet, if necessary. Indicate by (*) those liabilities, which will be satisfied upon sale of real estate owned or upon refinancing of the subject property.		
Cash deposit toward purchase held by:	$			
List checking and savings accounts below		**LIABILITIES**	**Monthly Payment & Months Left to Pay**	**Unpaid Balance**
Name and address of Bank, S&L, or Credit Union		Name and address of Company	$ Payment/Months	$
Acct. no.	$	Acct. no.		
Name and address of Bank, S&L, or Credit Union		Name and address of Company	$ Payment/Months	$
Acct. no.	$	Acct. no.		
Name and address of Bank, S&L, or Credit Union		Name and address of Company	$ Payment/Months	$
Acct. no.	$	Acct. no.		

VI. ASSETS AND LIABILITIES (cont'd)

Name and address of Bank, S&L, or Credit Union		Name and address of Company	$ Payment/Months	$
Acct. no.	$	Acct. no.		
Stocks & Bonds (Company name/ number & description)	$	Name and address of Company	$ Payment/Months	$
		Acct. no.		
Life insurance net cash value Face amount: $	$	Name and address of Company	$ Payment/Months	$
Subtotal Liquid Assets	$			
Real estate owned (enter market value from schedule of real estate owned)	$			
Vested interest in retirement fund	$			
Net worth of business(es) owned (attach financial statement)	$	Acct. no.		
Automobiles owned (make and year)	$	Alimony/Child Support/Separate Maintenance Payments Owed to:	$	
Other Assets (itemize)	$	Job-Related Expense (child care, union dues, etc.)	$	
		Total Monthly Payments	$	
Total Assets a.	$	Net Worth (a minus b) ▸ $	**Total Liabilities b.**	$

Schedule of Real Estate Owned (If additional properties are owned, use continuation sheet.)

Property Address (enter S if sold, PS if pending sale or R if rental being held for income) ▼		Type of Property	Present Market Value	Amount of Mortgages & Liens	Gross Rental Income	Mortgage Payments	Insurance, Maintenance, Taxes & Misc.	Net Rental Income
			$	$	$	$	$	$
		Totals	$	$	$	$	$	$

List any additional names under which credit has previously been received and indicate appropriate creditor name(s) and account number(s):

Alternate Name	Creditor Name	Account Number

VII. DETAILS OF TRANSACTION		
a.	Purchase price	$
b.	Alterations, improvements, repairs	
c.	Land (if acquired separately)	
d.	Refinance (incl. debts to be paid off)	
e.	Estimated prepaid items	
f.	Estimated closing costs	
g.	PMI, MIP, Funding Fee	
h.	Discount (if Borrower will pay)	
i.	Total costs (add items a through h)	

VIII. DECLARATIONS	Borrower Yes	Borrower No	Co-Borrower Yes	Co-Borrower No
If you answer "Yes" to any questions a through i, please use continuation sheet for explanation.				
a. Are there any outstanding judgments against you?	☐	☐	☐	☐
b. Have you been declared bankrupt within the past 7 years?	☐	☐	☐	☐
c. Have you had property foreclosed upon or given title or deed in lieu thereof in the last 7 years?	☐	☐	☐	☐
d. Are you a party to a lawsuit?	☐	☐	☐	☐
e. Have you directly or indirectly been obligated on any loan which resulted in foreclosure, transfer of title in lieu of foreclosure, or judgment? (This would include such loans as home mortgage loans, SBA loans, home improvement loans, educational loans, manufactured (mobile) home loans, any mortgage, financial obligation, bond, or loan guarantee. If "Yes," provide details, including date, name, and address of Lender, FHA or VA case number, if any, and reasons for the action.)	☐	☐	☐	☐

VII. DETAILS OF TRANSACTION		
j.	Subordinate financing	
k.	Borrower's closing costs paid by Seller	
l.	Other Credits (explain)	
m.	Loan amount (exclude PMI, MIP, Funding Fee financed)	
n.	PMI, MIP, Funding Fee financed	
o.	Loan amount (add m & n)	
p.	Cash from/to Borrower (subtract j, k, l & o from i)	

VIII. DECLARATIONS		Borrower		Co-Borrower	
If you answer "Yes" to any question a through i, please use continuation sheet for explanation.		Yes	No	Yes	No
f.	Are you presently delinquent or in default on any Federal debt or any other loan, mortgage, financial obligation, bond, or loan guarantee?	☐	☐	☐	☐
g.	Are you obligated to pay alimony, child support, or separate maintenance?	☐	☐	☐	☐
h.	Is any part of the down payment borrowed?	☐	☐	☐	☐
i.	Are you a co-maker or endorser on a note?	☐	☐	☐	☐
j.	Are you a U.S. citizen?	☐	☐	☐	☐
k.	Are you a permanent resident alien?	☐	☐	☐	☐
l.	**Do you intend to occupy the property as your primary residence?** If "Yes," complete question m below.	☐	☐	☐	☐
m.	Have you had an ownership interest in a property in the last three years?	☐	☐	☐	☐
	(1) What type of property did you own—principal residence (PR), second home (SH), or investment property (IP)?	______		______	
	(2) How did you hold title to the home—by yourself (S), jointly with your spouse (SP), or jointly with another person (O)?	______		______	

IX. ACKNOWLEDGEMENT AND AGREEMENT

Each of the undersigned specifically represents to Lender and to Lender's actual or potential agents, brokers, processors, attorneys, insurers, servicers, successors and assigns and agrees and acknowledges that: (1) the information provided in this application is true and correct as of the date set forth opposite my signature and that any intentional or negligent misrepresentation of this information contained in this application may result in civil liability, including monetary damages, to any person who may suffer any loss due to reliance upon any misrepresentation that I have made on this application, and/or in criminal penalties including, but not limited to, fine or imprisonment or both under the provisions of Title 18, United States Code, Sec. 1001, et seq.; (2) the loan requested pursuant to this application (the "Loan") will be secured by a mortgage or deed of trust on the property described in this application; (3) the property will not be used for any illegal or prohibited purpose or use; (4) all statements made in this application are made for the purpose of obtaining a residential mortgage loan; (5) the property will be occupied as indicated in this application; (6) the Lender, its servicers, successors or assigns may retain the original and/or an electronic record of this application, whether or not the Loan is approved; (7) the Lender and its agents, brokers, insurers, servicers, successors, and assigns may continuously rely on the information contained in the application, and I am obligated to amend and/or supplement the information provided in this application if any of the material facts that I have represented herein should change prior to closing of the Loan; (8) in the event that my payments on the Loan become delinquent, the Lender, its servicers, successors or assigns may, in addition to any other rights and remedies that it may have relating to such delinquency, report my name and account information to one or more consumer reporting agencies; (9) ownership of the Loan and/or administration of the Loan account may be transferred with such notice as may be required by law; (10) neither Lender nor its agents, brokers, insurers, servicers, successors or assigns has made any representation or warranty, express or implied, to me regarding the property or the condition or value of the property; and (11) my transmission of this application as an "electronic record" containing my "electronic signature," as those terms are defined in applicable federal and/or state laws (excluding audio and video recordings), or my facsimile transmission of this application containing a facsimile of my signature, shall be as effective, enforceable and valid as if a paper version of this application were delivered containing my original written signature.

Acknowledgement. Each of the undersigned hereby acknowledges that any owner of the Loan, its servicers, successors and assigns, may verify or reverify any information contained in this application or obtain any information or data relating to the Loan, for any legitimate business purpose through any source, including a source named in this application or a consumer reporting agency.

Borrower's Signature	Date	Co-Borrower's Signature	Date
X		X	

X. INFORMATION FOR GOVERNMENT MONITORING PURPOSES

The following information is requested by the Federal Government for certain types of loans related to a dwelling in order to monitor the lender's compliance with equal credit opportunity, fair housing and home mortgage disclosure laws. You are not required to furnish this information, but are encouraged to do so. The law provides that a lender may not discriminate either on the basis of this information, or on whether you choose to furnish it. If you furnish the information, please provide both ethnicity and race. For race, you may check more than one designation. If you do not furnish ethnicity, race, or sex, under Federal regulations, this lender is required to note the information on the basis of visual observation and surname if you have made this application in person. If you do not wish to furnish the information, please check the box below. (Lender must review the above material to assure that the disclosures satisfy all requirements to which the lender is subject under applicable state law for the particular type of loan applied for.)

BORROWER ☐ I do not wish to furnish this information		**CO-BORROWER** ☐ I do not wish to furnish this information	
Ethnicity:	☐ Hispanic or Latino ☐ Not Hispanic or Latino	**Ethnicity:**	☐ Hispanic or Latino ☐ Not Hispanic or Latino
Race:	☐ American Indian or Alaska Native ☐ Asian ☐ Black or African American ☐ Native Hawaiian or Other Pacific Islander ☐ White	**Race:**	☐ American Indian or Alaska Native ☐ Asian ☐ Black or African American ☐ Native Hawaiian or Other Pacific Islander ☐ White
Sex:	☐ Female ☐ Male	**Sex:**	☐ Female ☐ Male

To be Completed by Loan Originator:
This information was provided:
- ☐ In a face-to-face interview
- ☐ In a telephone interview
- ☐ By the applicant and submitted by fax or mail
- ☐ By the applicant and submitted via e-mail or the Internet

Loan Originator's Signature		Date
X		
Loan Originator's Name (print or type)	Loan Originator Identifier	Loan Originator's Phone Number (including area code)
Loan Origination Company's Name	Loan Origination Company Identifier	Loan Origination Company's Address

CONTINUATION SHEET/RESIDENTIAL LOAN APPLICATION		
Use this continuation sheet if you need more space to complete the Residential Loan Application. Mark **B** for Borrower or **C** for Co-Borrower.	Borrower:	Agency Case Number:
	Co-Borrower:	Lender Case Number:

I/We fully understand that it is a Federal crime punishable by fine or imprisonment, or both, to knowingly make any false statements concerning any of the above facts as applicable under the provisions of Title 18, United States Code, Section 1001, et seq.

Borrower's Signature	Date	Co-Borrower's Signature	Date
X		**X**	

Choosing the Best Loan

Know the Borrower's Goals

Every borrower is in a different financial position. Therefore, a loan that works for one borrower will not work for another. In order to help a borrower select the best kind of loan for their financial circumstances, an agent must understand the borrower's goals.

There are three basic types of borrowers:

- Short-term borrowers
- Long-term borrowers
- Investors

Each of these borrower types has distinctly different mortgage needs.

For example, if a borrower/buyer intends to live in a home for a shorter period of time (i.e. less than five years), he or she should secure a loan without a prepayment penalty or he or she may have to pay a fee in order to refinance the loan before the end of the penalty period.

Conversely, if the borrower/buyer intends on living in the home for a longer period of time (i.e. more than five years), he or she may be well suited for a fixed rate mortgage with a prepayment penalty. This would provide the borrower/buyer with long-term stability and allow them to calculate consistent monthly expenditures.

Mortgage Loan Costs

Before recommending any loans to a borrower/buyer, an agent should provide an estimated breakdown of the costs associated with those loans. A borrower/buyer can use these breakdowns to compare which programs best fit his or her needs.

Mortgage loan costs may include:

- Application fee
- Document fee
- Loan Points
- Flat fee
- Private mortgage insurance (PMI)
- Loan escrow costs
- Title insurance
- Service or processing fees

Some lenders charge points (percentage), others charge a flat fee, and others charge a combination of various fees. Most lenders charge between one to three points (or 1-3%) of the total loan amount at closing.

For example, say a borrower is preapproved for a $340,000 loan and the lender charges two points upfront for the loan. In order for a borrower to obtain that loan, he or she must pay $6,800 (or 2%) in total costs to the lender.

If a lender's loan offer appears drastically better than other loan offers, the lender is likely adding costs somewhere else. For example, a lender who is offering an extremely low interest rate may charge higher loan costs to offset the reduced interest rate.

There may also be additional loan costs if a borrower has limited equity. **Private mortgage insurance (PMI)** refers to an insurance coverage that a borrower must purchase if his or her mortgage has below 20% equity. Its purpose is to protect the interests of a lender in the event a borrower defaults.

Loan Comparison

A borrower should consider all of the following major points before committing to a mortgage loan:

- Down payment requirements
- Interest rate
- Loan terms (i.e. prepayment penalties, closing costs, fees)
- Length of loan (the longer the loan period, the lower the payment)
- Loan type (i.e. fixed, adjustable, hybrid)
- Future refinance requirements

Common Loan Terms

- *Principal.* The underlying debt on which a borrower pays interest.
- *Interest Rate.* The cost of borrowing, expressed as a percentage.
- *Principal and Interest.* Payment structure that pays off the principal with interest via monthly mortgage payments over a specific period of time.
- *Loan Period.* The length of time on which a borrower's mortgage payments are based. The most common loan term is a 30-year fixed program. Other common programs include 10-year, 15-year, and 20-year terms.

- *Amortization*. Repayment schedule based on consistent monthly installments over a period of time. Interest is divided among each installment.
- *Interest-Only Payment*. Payment that only covers the interest on the principal without paying down the principal.
- *Impound Account*. Trust account used to divert mortgage payments and property taxes through one payment, instead of through multiple payments.
- *Points*. Also known as origination fees. These are lender loan fees expressed through percentages. Each point is represented by one percent. Points can be charged directly by a lender or by a broker who is assisting a borrower.

Types of Mortgages

Mortgage programs are constantly changing: one program that is available today may not be around tomorrow. An agent does not need to be a loan professional. However, having knowledge of loan qualifications, available mortgage programs, and current interest rates can dramatically affect an agent's ability to confidently sell clients.

Fixed-Rate Loans

A **fixed-rate loan** is a loan in which the interest rate remains "fixed" for the entire life of the loan.

Fixed-rate loans are the most popular in the United States. They offer borrowers the ability to make consistent monthly payments on a predetermined payment schedule. This is particularly beneficial to families.

Fixed interest rates provide an attractive alternative to the fluctuations of adjustable-rate mortgages and produce security in an otherwise unpredictable mortgage market. Even if the Federal Reserve raises interest rates, fixed-rate loans maintain their agreed-upon interest rates.

Borrower qualification for a fixed-rate loan is generally easier and requires less documentation than other loans.

The primary parameters of a fixed-rate loan are:

- Maximum loan amount of $417,000 for a single-family home (can be adjusted to a jumbo loan in more expensive regions)
- Down payment of at least 5% of the total property value

Fixed-rate loans are similar, except for the amount of time it takes to pay them off and the amount of interest paid throughout the loan period. The longer the loan period, the smaller the monthly mortgage payments are.

The three most common fixed-rate programs are:

- 15-year fixed
- 20-year fixed
- 30-year fixed

A borrower's most ideal loan period depends on the borrower's financial situations and goals.

For example, borrowers who have a substantial income and wish to pay off their home in the shortest amount of time possible may select a 15-year fixed loan. Conversely, borrowers who plan to stay in a home for the foreseeable future and wish to make lower monthly payments may select the 30-year fixed loan.

A 40-year fixed loan is the least common fixed-rate loan. Such loans provide borrowers with the lowest monthly mortgage payment, but also require borrowers to pay the highest amount of interest to a lender over the life of the loan.

Fixed-Rate Loan Comparison

Say a borrower wishes to take out a fixed-rate loan for $200,000. Her bank offers her an interest rate of 4.5%* for either a 15-year, 20-year, 30-year, and 40-year fixed loan with various monthly mortgage payments. Below is a breakdown of the monthly mortgage payments and total cost of each fixed-rate loan.

**Note: Interest rates typically differ based on the length of the loan period. The same interest rate is being used here for simplicity in understanding.*

15-Year Loan

Monthly Mortgage Payment = $1,530
Annual Cost = $18,360
Total Loan Cost = $275,400

20-Year Loan

Monthly Mortgage Payment = $1,265
Annual Cost = $15,180

Total Loan Cost = $303,672

30-Year Loan

Monthly Mortgage Payment = $1,013
Annual Cost = $12,156
Total Loan Cost = $364,813

40-Year Loan

Monthly Mortgage Payment = $899
Annual Cost = $10,788
Total Loan Cost = $432,520

Adjustable-Rate Mortgages (ARM)

Unlike a fixed-rate mortgage, an **adjustable-rate mortgage (ARM)**'s interest rates fluctuate at predetermined adjustment periods during the life of the loan.

If interest rates drop during an adjustment period, a borrower can refinance his or her loan at a lower interest rate and pay less on his or her monthly mortgage payment. If interest rates rise, a borrower may have to refinance at higher interest rates and pay more.

Nearly one out of every five borrowers has an adjustable-rate mortgage on their primary residence.

Borrowers should be aware of all the provisions and potential drawbacks to ARMs, including:

- Initial interest rate
- Adjustment period
- Index rate
- Cap rate
- Negative amortization
- Due-on-sale clause
- Prepayment penalty

Initial Interest Rate

The initial interest rate of an ARM is lower than most fixed-rate loans. It remains fixed for a short period of time (typically one to three years), and then it adjusts.

Interest rate adjustments occur on a predetermined adjustment period schedule. The specific rate of change is not defined until the date of the adjustment period, although it typically results in an increase to a borrower's monthly mortgage payment.

If a borrower/buyer is planning to sell his or her property before the adjustment period ends and is allowed to refinance without penalty, this low, initial interest rate offer may be worthwhile.

However, if a borrower/buyer plans does not realize the substantial rate increase that comes after the adjustment period, the borrower may not find him- or herself unable to afford the higher mortgage payments.

Many borrowers got caught in such situations prior to the 2008 real estate collapse. They took out loans without realizing that their monthly mortgage payments would eventually increase.

A borrower should understand the specifics of an initial interest rate offer, including:

- When does the adjustment period end?
- How will the increased interest rate affect my monthly mortgage payments?
- Is there a prepayment penalty that prevents me from refinancing and getting a lower rate in the future?

Adjustment Period

The **adjustment period** is the amount of time in between interest rate adjustments on an ARM loan. These periods are scheduled in the original terms of the loan.

Some loans have adjustment periods of every few months, others have one every year. The standard adjustment period for most loans is one to three years.

A 1/1 ARM denotes an adjustment period of one year, 3/1 ARM denotes a period of three years, and 5/1 ARM denotes a period of five years.

Index Rate

The **index rate** is a rate derived from market forces, including interest rates, inflation, and the cost of treasuries. It is commonly based on the 3-year and 5-year Treasury cost of securities (known as T-Bills). The Treasury or a private lender puts forth the index rate.

The index rate influences the interest rates a lender charges. An increase in the index rate usually means an increase in the interest rate on a borrower's ARM; a decrease in the index rate typically means a reduction.

A loan's interest rate is also determined by the margin. The **margin** refers to the points (percentage) that banks charge to profit off of a loan. Each lender uses different margins for their loans, but most charge two to three points (or 2-3%).

Generally, the lower the initial loan origination costs, the higher the margin will be (so as to offset the initial low costs).

A borrower should ask a lender which index rate would be used to calculate the borrower's mortgage payment. This allows a borrower to do research on the index rate and track its recent trends in order to anticipate changes in the future.

Cap Rate

The **cap rate** is the maximum interest rate a borrower will pay when an ARM adjusts, even if the index rate rises significantly. Most ARMs have a cap rate to protect borrowers from unlimited increases by lenders.

There are three different mortgage caps:

- *Cap Rate.*
- *Periodic Cap.* This limits how frequently a loan can be adjusted.
- *Lifetime Interest.* This limits the total amount of interest a borrower is responsible for paying over the life of a loan.

Every lender has different ARM cap rates. A lender's approach varies based on the individual client, economic conditions in the market, and what other lenders are offering. Some lenders may use a combination of one or all of the above caps. Most lenders use a combination of the periodic cap and cap rate.

Negative Amortization

When a borrower is unprepared for a sudden increase in interest rates, the borrower may be unable to make full payments.

Negative amortization, also known as deferred interest, refers to when a borrower fails to pay interest due on the loan and the interest is added to the principal loan amount.

Although a borrower may make lower monthly payments in the short-term, negative amortization increases the overall loan amount and makes future mortgage payments more costly. This challenging financial position could eventually result in foreclosure.

Due-On-Sale Clause

A **due-on-sale clause** is a mortgage provision that requires a borrower to repay the full principal loan amount plus interest upon the sale or conveyance of the property.

Prepayment Penalty

A **prepayment penalty** is a mortgage provision that triggers a lump sum charge in the event that a borrower chooses to refinance a loan or sell a property within the penalty period.

Lenders provide loans to borrowers with the expectation that they will make a minimum amount of money by charging interest. Conversely, borrowers want the lowest interest rates possible. No lender wants to spend three months putting resources into approving a borrower, only to have that borrower refinance with another lender with cheaper financing shortly after.

A prepayment penalty ensures that a lender makes money, either through a borrower keeping a loan active for a minimum period of time or the borrower disrupting the loan terms and paying a penalty.

There are two types of prepayment penalties:

- *Soft.* A penalty is only applied if a borrower wants to refinance before the expiration date.
- *Hard.* A penalty is applied when a borrower wants to sell or refinance before a specified time period.

Borrowers should understand the ramifications of choosing a loan with a prepayment penalty.

For example, say a borrower takes out a loan with a prepayment penalty of $10,000 for a period of two years. If a borrower wants to refinance the loan at a more favorable rate six months later, he or she would have to pay $10,000 to do so. The borrower would also be subject to a $10,000 fine if he or she wants to sell his or her home before the end of the two years.

Types of ARM

There are hundreds of types of ARM loans. The following are a few basic examples that guide the basis of all ARM loans.

Option ARMs

An **option ARM** gives borrowers the flexibility to select different mortgage payment options, including:

- Principal and interest
- Interest-only
- Minimum

Interest-only loans provide borrowers with the option to reduce their monthly mortgage payments by only paying the interest that is owed on the loan. The remaining loan amount stays the same during an interest-only period, as the borrower is not paying down the principal.

Interest-only programs are attractive to borrowers who have a limited cash flow or who wish to save money for other expenses, such as starting a business, repairing a home, or paying off a debt.

With the minimum payment option, the difference between the minimum payment and the full principal and interest payment gets added to the principal loan balance. When interest rates rise and the loan balance grows, many borrowers are sent into "payment shock". At this point, they must either pay the loan, refinance, or go into foreclosure.

Option ARMs were never intended for homeowners. Instead, they were created for real estate investors who bought properties for "flipping". An option ARM allowed an investor to minimize his or her monthly mortgage payments during construction, and then sell a property before rates increased.

Convertible ARMs

A **convertible ARM** provides borrowers with the option to alter an ARM into a fixed-rate mortgage. Most lenders charge a fee or points for doing so.

Lenders market convertible ARMs as a way for borrowers to avoid paying higher interest rates when a loan is set to adjust or when interest rates are supposed to increase. This is attractive to borrowers who believe their financial circumstances may change in the future.

Borrowers must qualify for a convertible loan within a specified period of their loan period.

Assumable ARMs

An **assumable ARM** refers to when a borrower/buyer assumes responsibility for a seller's loan.

Oftentimes, sellers use assumable ARMs to entice buyers to purchase their properties at a lower interest rate. A seller can use this increased savings on the loan as leverage for increasing the listing price. As a seller already has a loan, it also decreases the time it takes a buyer to get approved for a loan and reduces the fees and points charged by the lender.

This type of loan is particularly attractive when interest rates are high, as it can reduce the cost of homeownership.

There are a few drawbacks to an assumable ARM. A borrower may be required to produce a significant down payment to prove his or her financial status. If a borrower cannot afford a large down payment, he or she may have to apply for a second loan, which eliminates the advantages of wanting an assumable ARM in the first place.

Considering an ARM

Questions for a Borrower to Ask a Lender:

- What is the initial interest rate on the ARM?
- How soon does the interest rate adjust?
- How often does the loan adjust after that?
- What is the current index rate?
- What index rate is the ARM tied to? (i.e. predetermined, federal)
- What is the maximum cap rate?
- Is the borrower allowed to refinance the loan? If so, is there a prepayment penalty?
- Is private mortgage insurance (PMI) required?
- Is the ARM assumable?
- Are there payment options? For example, does the ARM cover interest-only payments?
- With the monthly payment pay down the principal balance?

Questions for a Borrower to Ask Him- or Herself:

- If the interest rate adjusts and current interest rates are very high, can I afford the increased payment?
- Is the lower initial payment worth the risk of potentially having a higher payment in the future?
- Am I going to have future debts – such as car loans, school loans, kids tuition and other significant expenses – that will affect my ability to afford my mortgage if interest rates rise?

Between the initial interest rate, adjustment period, index rate, and cap rate, an ARM has many components that can be overwhelming or confusing for a borrower to understand. Borrowers should ask lenders extensive questions to ensure that they understand what selecting an ARM entails. Borrowers are also advised to consider how future interest rate increases will affect their monthly mortgage payments and financial situation as a whole.

Hybrid Loans

A **hybrid loan** is a loan that features fixed interest rates for the initial loan period and adjustable interest rates for the remaining period.

Most hybrid loans are based on a 30-year loan period. They provide fixed interest rates for the first five years and adjustable rates for the remaining 25 years.

Initial interest rates for hybrid loans are typically 1% lower than interest rates for fixed loans. This is an attractive option for borrowers who wish to sell a home or refinance in the near future and can take advantage of the initial low interest rate.

Before accepting the terms of a hybrid loan, borrowers should be aware of the cap rate.

Government Loans

Federal Housing Administration (FHA)

The **Federal Housing Administration (FHA)** is a government entity under the Housing of Urban Development.

Its purpose is to extend and promote financing to qualified borrowers by providing loans at a lower cost than conventional loans. Unlike **conventional loans**, in which all risk and profits are taken on directly by the loan's originator, the government guarantees the principal and interest payments on FHA and VA loans. This incentivizes lenders to provide more loans.

An FHA loan is the most common, federally backed type of mortgage loan. Such loans are beneficial to lower income borrowers and/or those who can only put a minimal amount of money towards a down payment.

There are FHA programs that assist with:

- First-time homeowners
- FHA streamline

- FHA reverse mortgage.

The FHA does not make loans directly to borrowers. Rather, borrowers must go to an institutional lender and qualify for an FHA loan. If a borrower's relative risk portfolio (i.e. income, tax returns, credit, debt) qualifies for the basic FHA loan application, the bank will send the documentation directly to the Federal Housing Administration. The FHA will then review the application and make a decision on whether to award a loan.

Not all lenders service FHA loans.

The Federal Housing Administration may authorize a lender to collect documentation and underwrite a loan on its behalf. This is known as a **direct endorsement**. The time to get approved for a loan is dramatically reduced when a lender has been directly endorsed.

The government requires borrowers to buy mortgage insurance to insure the risk of funding an FHA loan. The usual cost of mortgage insurance is 1.75% and is due at the close of the loan.

VA Loan

The **Servicemen's Readjustment Act of 1944** – more commonly known as the GI Bill – was a federal law enacted to provide affordable financing for returning WWII soldiers. These loans, which are still in use today, are known as **VA loans**.

The basic requirement for a VA loan is that a borrower has served a minimum of 181 days in the service.

A VA loan does not require a borrower to put down a down payment. If qualified, soldiers can buy homes with 100% financing. The maximum loan amount for 100% financing is $417,000 and is adjusted to a higher rate in more expensive counties.

The VA loan program's funding fee is between 0-3.3%. All fees can be added to a loan if the applicant qualifies.

VA loans are not serviced directly by the government. Similar to FHA loans, they are provided through lenders who assist with VA loans. The government guarantees a portion of VHA loans in order to help reduce the risk for lenders and incentivize them to provide loans for former soldiers.

CalVet Loans

A **CalVet loan** is a California state loan program that offers affordable financing to soldiers to purchase a single-family residence or farm. These loans are aimed at helping California veterans achieve homeownership.

CalVet loans offer a variety of benefits, including:

- Below market interest rates
- Current rate of 3.5% for 20-year fixed mortgage and 5.50% for 30-year fixed mortgage
- Low or no down payment
- Flexible mortgage programs
- Easy loan qualification compared to conventional loans

Hard Money Loans

Hard money loans are private loans made by an individual or a group of investors that have higher interest rates and faster approval processes than conventional loans.

Consumers utilize hard money loans when they cannot qualify for standard mortgages or need immediate access to financing.

Open-End Mortgage

An **open-end mortgage** – also known as an open-end trust deed – provides borrowers with the option to increase their loan amount at a future time (if loan qualifications are met).

Much like a credit card, this allows borrowers to borrow more money. The increased loan amount uses the same trust deed and equity as the initial loan.

Blanket Trust Deed

A **blanket trust deed** allows a borrower to use two or more parcels of land to secure a loan.

Developers commonly use blanket trust deeds in order to secure funds for construction projects. In this case, developers will likely request a **partial release clause** in the agreement. This ensures that a partial reconveyance will be obtained as the developer completes a lot or parcel.

Seller Carryback Financing

There are some situations in which a buyer wishes to purchase a particular property, but he or she is not qualified for a loan amount large enough to cover the entire cost. **Seller carryback financing** offers a solution: a lender provides a mortgage loan amount befitting the borrower's qualifications and the seller lends the buyer the remaining funds.

This gives buyers access to the capital required to buy a home and helps a seller incentivize buyers to purchase the property. Sellers who provide carryback financing have the option of charging above or below market interest rates. The terms of the loan are usually fixed for 3-5 years.

Each loan is customized to the specifics of a particular transaction and is dependent on negotiations between the buyer and seller. Both parties should have a real estate lawyer or a mortgage broker review the terms of an agreement before engaging in seller carryback financing.

Wraparound Mortgage

A **wraparound mortgage** – or a "wrap" – is a type of creative seller financing whereby the seller grants the buyer the right to purchase a property while maintaining the existing loan on the property. In this scenario, the buyer pays the seller mortgage payments directly, which the seller subsequently pays the lender.

A wraparound mortgage essentially transfers loan liability for the seller's first mortgage to the buyer. In the event the buyer does not make the agreed-upon payments, the seller has the right to foreclose on the property.

If the current owner of the property has a low interest rate on the property and rates have increased, a wraparound mortgage can be an enticing offer for buyers as it allows them to purchase real estate with a lower payment and allows them to buy the property without qualifying for a loan. This proves significant for both the buyer and seller, particularly in a slow real estate market.

In a wraparound mortgage, the seller acts as the bank by providing the loan to the buyer. In exchange for the loan and possession of the property, the seller holds a promissory note for the balance of the purchase price, minus down payments. The term "wraparound" stems from the fact that the buyer's new debt is "wrapped around" the seller's debt.

Gap Loan

A **gap loan** – also known as a bridge loan – provides funds to a borrower for the purchase of one property while he or she is waiting to sell another property.

Typically, a gap loan applies to two types of people:

- Sellers who need financing for a new home purchase, but have yet to sell their old home
- Real estate investors who don't have access to capital until one of their investment properties sells

Interest rates for bridge loans are substantially higher than conventional loans. However, with the necessary equity, it may be easier and quicker for a borrower to qualify for a bridge loan over a conventional loan.

80-20 Loans

Many lenders will only finance up to 80% of a home purchase price, which means that borrowers must provide 20% upfront as a down payment. If a borrower does not have the 20% required to qualify for a loan, an 80-20 loan is ideal.

An **80-20 loan** provides a borrower with a second loan equivalent to 20% to be used as a down payment. The loan can be taken out as a home equity deed of trust.

As the 20% is a second loan, it is a riskier investment for a lender. Therefore, interest rates – as well as any additional fees, points, and origination costs – are generally higher.

Qualifying for 80-20 loans is difficult as very few lenders offer them. Since the 2008 real estate market collapse, many lenders have been reluctant to offer such risky programs.

Only the most credit-worthy and risk adverse borrowers will qualify for an 80-20 loan when lenders do offer them. Borrowers must display a sound credit history that shows they have low debt, low debt obligations, money in their savings account, and consistent, documented income.

Renegotiable-Rate Mortgages

A **renegotiable-rate mortgage** – also known as a rollover loan – offers fixed interest rates for a set period of time. Upon the expiration of the fixed term, borrowers have the ability to refinance the loan directly with the lender or apply for a loan with another lender.

The fixed term is typically 3-10 years.

Renegotiable-rate mortgages begin with low interest rates. After the initial fixed term, rates may rise substantially.

These loans are attractive to investors who buy properties with the intention of "flipping" them. The investor is able to pay low interest rates and hopefully sell the property for a profit before the end of the fixed term.

An **open-ended mortgage** permits borrowers to increase the loan amount on their mortgage if certain conditions are met. It is a change in the borrower's existing mortgage program.

Reverse Mortgage

A **reverse mortgage** allows seniors to use their home's equity to pay the home's monthly mortgage payments. In this case, the lender is responsible for paying the mortgage. Borrowers are still responsible for paying property taxes and HOA fees, however.

A reverse mortgage requires a borrower to have substantial equity or projected equity in his or her home. The interest that accrues over the life of a loan is added to the principal balance, thereby adding more to the loan every month. The principal balance will continue increasing, possibly above the value of the home.

The major benefit of a reverse mortgage is that it allows seniors to tap into the equity of their home to keep up mortgage payments, pay off bills, or make repairs.

The major disadvantage is that a lender takes legal possession of a property once a borrower dies. This means that the borrower's heirs have no claim to the property.

Loan Approval

Once a prospective borrower meets all of a lender's qualifications and has selected the best mortgage for his or her financial situation, the lender will approve the borrower for a loan.

A lender processes a loan by preparing and forwarding all required loan documents, disclosures, and forms and fees. A borrower must sign and date all loan documents in order to close a loan. If a borrower is unable to go to a lender's physical location, a lender may send a licensed notary.

Servicing a loan refers to a lender creating a payment schedule, collecting a borrower's monthly mortgage payments, and managing the borrower's loan account throughout the duration of the loan period. A lender can either service a loan directly or have a third party service the loan on the lender's behalf.