

Rediscovering FHA

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Our industry has undergone quite a transition over the last couple of years. There are few "uncomplicated" sales, as foreclosures and short sales dominate the marketplace. Isn't it nice to reminisce about the time when you just sold a house, gave knowledgeable advice, followed up on the transaction, kept people informed and your clients thanked you for doing a great job.

The lending industry has also experienced monumental change. "Easy" loans are a distant memory. "Declining markets" has become a part of our industry vocabulary. 80/20's, well, they just aren't available anymore.

All are indications that conventional guidelines have been growing more cautious with each passing month, with higher downpayment requirements and more conservative guidelines, fewer and fewer home purchasers (and properties) can pass through the filters established for these conventional programs.

On top of all of this, the rules and guidelines of the mortgage insurance companies have been changing so fast, it no longer makes sense for them to print their rates. Even if a borrower (and property) might meet the standards for conventional financing, they must also be acceptable to the MI companies, and find their way through a different set of rules. In summary, much of what was acceptable as recently as last spring is no longer available.

That is the bad news - but there is also **good news** for those REALTORS® who are flexible enough to adapt to the industry changes. During the past decade, due to the ease with which borrowers could obtain home financing, there was no need to become involved with anything that seemed like it might be complicated. So the industry gravitated away from FHA financing. Well, it's now time to revisit this mode of financing.

So what are the reasons that many have rediscovered FHA financing to enable them to successfully complete more transactions? Simply, FHA guidelines permit greater flexibility in most areas of loan underwriting. The following is a brief discussion of some of those areas:

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Property Appraisal and Property Issues

If you are familiar with the term "declining markets", you will be pleased to know that FHA doesn't have a declining markets policy, even where the appraiser identifies the property as being in a declining market. Also, there is widespread anxiety among REALTORS® that FHA will mandate many repairs, disrupting the transaction. People need to be aware that in 2005 FHA issued a reform to its appraisal requirements, permitting "as is" appraisals. Many of the old requirements no longer exist. Simply, FHA wants the property appraisal to only deal with property conditions that may represent a risk to the health and safety of the occupants or the soundness of the property, and no longer cares about cosmetic or lesser property issues.

Downpayment

While it's true that conventional loans permit LTV's of 97% under the FannieMae and FreddieMac guidelines, all lenders price these loans at higher risk, which equates to higher rates. In addition, these conventional loans require mortgage insurance, and obtaining insurance will be challenging as the MI companies require high credit scores. While some MI companies still price coverage for 97% LTV's (commonly a 680 credit score is required), the ability to secure approval comes with many caveats. One MI company would caution as follows:
** Note LTVs greater than 95% are limited to certain characteristics and markets. LTVs greater than 90% may not be eligible in all markets.* In short, you will be "walking through a mine field" to get this loan completed. FHA, on the other hand, has a simple 3.5% downpayment requirement. Moreover, while conventional borrowers must have 5% of their own funds to invest, FHA would permit downpayment gifts as well as "family loans" for the needed monies – a very important distinction.

Credit Scoring

Although the FHA guidelines still do

not express a "minimum credit score" most of the lenders making these loans have self-imposed their own minimum acceptable score. Despite this, however, the defined acceptable score is far more tolerant than the scores required on insured conventional loans.

Competitive MI Costs

There was a time when the cost for FHA's mortgage insurance was higher than what was available on conventional loans, this is no longer the case for many borrowers. In general, borrowers putting less than 10% down will find a much lower total payment if utilizing FHA financing.

Greater Seller Concessions Permitted

When the borrower needs a downpayment, and funds are limited, it may become important to be able to negotiate a purchase where the seller is paying the buyer's closing costs. For conventional financing, the seller is limited to paying 3% toward the buyer's costs.

More Forgiving Underwriting Rules

This generally is apparent within some of the categories previously discussed. In just about every area of underwriting, whether it is credit, money needed to close, employment and job stability, FHA guidelines will be more favorable. This is especially true for borrowers who have experienced past credit issues.

This contrast can be seen by discussing some specific credit related examples. First, it should be noted that FHA is generally looking for borrowers who have shown during the past year that they have their finances under control. Past collections may often be overlooked, especially collections for medical reasons. If the borrower has had a bankruptcy or property foreclosure in their past, the FHA guideline for the required amount of time that must pass from the time of the credit transgression is one to two years less than would be required by FannieMae or FreddieMac. Following are several examples: where FannieMae would require four years from a Chapter 7 bankruptcy, FHA would require two; where FannieMae would

require five years from a foreclosure, FHA would require three; and finally, where FannieMae would require two years from the discharge of a Chapter 13 bankruptcy, FHA would actually permit the borrower to purchase while still in the Chapter 13 plan, as long as the bankruptcy trustee approves the purchase (which they commonly do).

The market share for FHA financing was approximately 25% in 1996. Over the next decade, it gradually fell to a low of about 5% in 2005. With the elimination of conventional options, the FHA market share has grown substantially over the past year to, once again, over 20%. If you are not considering FHA, you are shortchanging yourself and your clients.

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