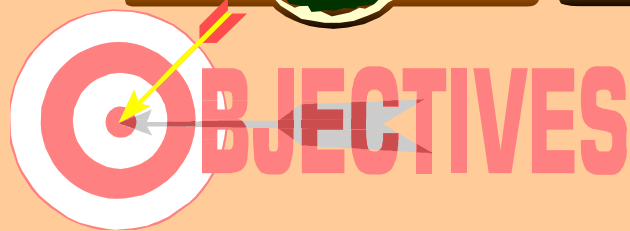


# **CHAPTER 11**

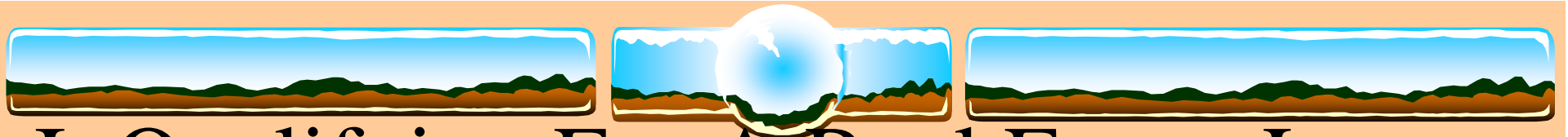
## **REAL ESTATE LOAN AND SECONDARY MONEY MARKET**





## STUDENT LEARNING OUTCOMES (SLOs):

1. Explain methods to qualify a buyer.
2. List and describe the difference between institutional and non-institutional real estate lenders.
3. Identify the key characteristics of the California lending market.
4. Explain the purpose of the secondary mortgage market.
5. Explain various government programs available in California.
6. Explain FNMA, GNMA & FHLMC benefits.



# I. Qualifying For A Real Estate Loan

A. 3 “C” of credit are:

1. Character (desire)

Credit history

Credit Report

2. Capacity (ability)

Income to make the payments

VOE/2yr tax returns/last pay stub/Income statement

3. Capital (assets)

Reserves to convert to cash

VOD/(Asset-Liabilities=Net worth)/Balance Sheet



# Monthly Payment

It's "A PITI" to have to make the payment!

A

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P

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T

axes on the property

I

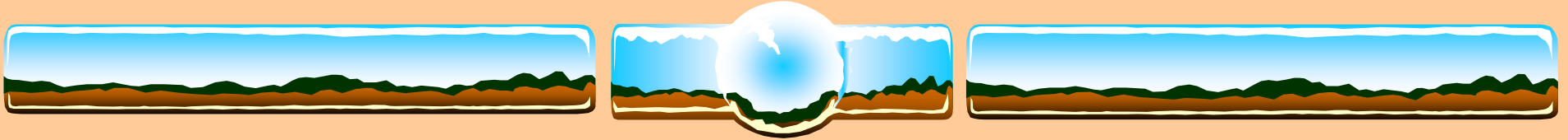
nsurance





## B. Multiplier or Ratios to Qualify Borrowers

	Ratios (%)		
	Conventional	FHA	DVA
1. <b><u>Front End Ratio</u></b>	28%	29%	
2. <b><u>Back End Ratio</u></b>	36%	41%	41%



## Sample Conventional Qualifying Ratios:

- ❖ Gross monthly income \$6,000
- ❖ Long term debts \$500
- ❖ \$6,000 [x] 28% [=] \$1,680 for APITI

❖ \$6,000 [x] 36% [=] \$2,160 for APITI and debts

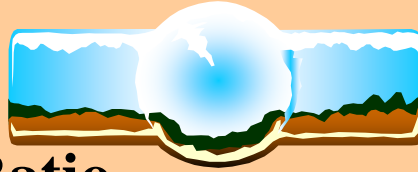
- 500 debts

= \$1,660 for APITI

The *lower* of the two.

For the above: \$1,680 vs. \$1,660 =

Maximum payment of \$1,660 per month for PITI



### 3. LTV = Loan-to-value Ratio

Appraised Price (NOT sales price) x 80% = Conservative Maximum loan

Pg 11-1

## II. Fees Incurred When Obtaining A Loan

A. Loan Origination fee - 1 point = 1% of the loan amount

B. Impound Account – Collection for future taxes and insurance  
(collects 1/12<sup>th</sup> of annual taxes & insurance)

C. Appraisal fees

D. Credit Report fee with extensive information

E. Escrow and Title fees are negotiable

F. Fees: tax service, document fees, recording fees.

G. Beneficiary Demand Statement showing existing loan balance

Pg 11-2



### III. Loans Are Either Conventional Or Government Backed

#### A. Conventional loans

- ❖ Private mortgage insurance

#### B. Government-backed loans:

##### 1. FHA

- ❖ Government **insures** loan

##### 2. DVA

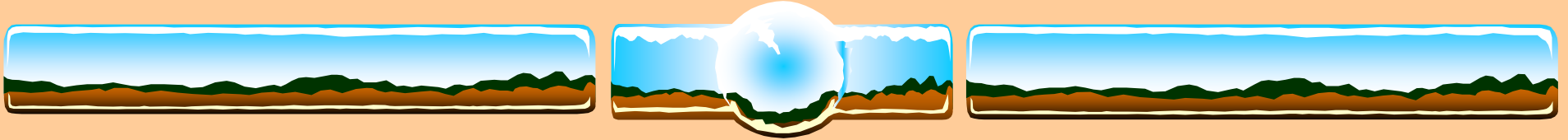
- ❖ Government **guarantees** loan

##### 3. Cal-Vet

- ❖ California state buys the property and

sells it to the vet on a **land** contract and long term lease

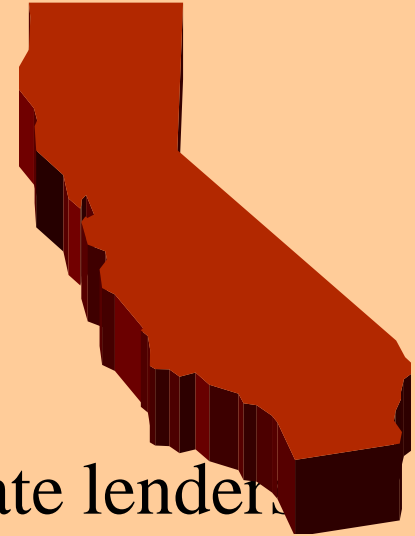


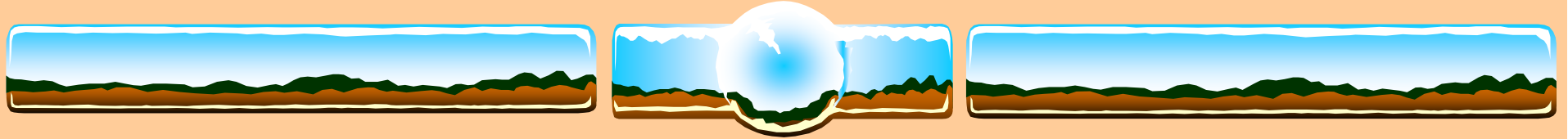


## IV. The California Mortgage Market

Identifiable characteristics:

1. High demand
2. Increasing population
3. Numerous large financial institutions
4. Use of mortgage companies for out-of-state lenders
5. Escrow and title companies provide fast service
6. Loan security is Trust Deed not a mortgage contract
7. Active secondary market to trade loans for cash  
to generate more loans



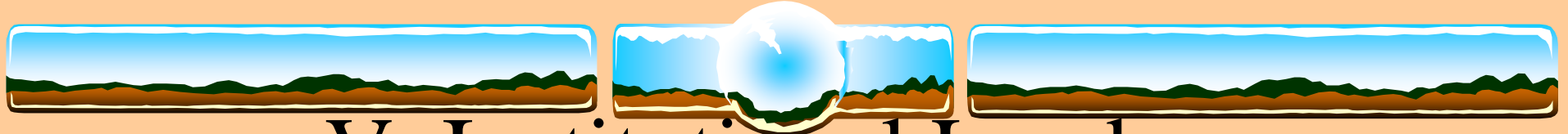


## Federal Reserve System

- ❖ Regulates Commercial Banks (FDIC)
- ❖ Sets Reserve Requirements
- ❖ Sets Discount Rate
- ❖ Buys and Sells Securities
- ❖ Increases/Decreases Money Supply

Federal Home Loan Bank System  
Regulates Savings and Loans (FSLIC)





## V. Institutional Lenders

### A. Commercial Banks

1. Federal or state chartered
2. Loans up to 95% of appraised value for 30 year term
3. Short term and construction loans

### B. Thrift Institutions (Savings & Loan)

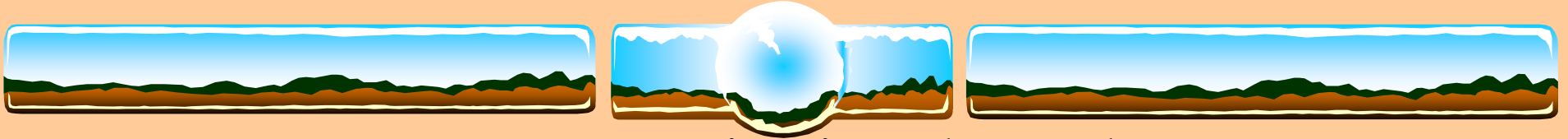
1. Federal or state chartered
2. 30 year term
3. up to 95% of appraised value for 30 year term

### C. Life Insurance Companies

1. Prefer large commercial or industrial loans
2. 75% to 80% L-T-V with 30 year or longer term

# Institutional Lenders

Savings & Loan	Commercial Banks	Insurance Companies
Federal & State	Federal & State	State
Usual maximum 90% (Can go to 95%)	Usually 80% (Can go to 95%)	75%
30 years	25 years (short-term) (Can go to 30 years)	25 to 30 years
Usually at the higher end of the market	Usually middle of the market	Usually at the lower end of the market
Prefer conventional made on single family dwellings, apartments buildings, mobile homes, condominiums	Prefer construction loans with backup takeout loan assured from another lender; Equity home loans Business loans FHA/VA backed	Prefer high quality loans Larger commercial and industrial properties with AAA tenants Hotels and office buildings -FHA/VA
Greatest share of market	Present or former	4. Lend through <b><u>loan correspondents</u></b> mortgage companies 5. <b><u>Participation loan</u></b> where lender gets a percentage of ownership in the project



## VI. Non-Institutional Lenders

### Second Deed of Trust Junior Lien

#### Purpose

Close the gap between the sales price and the first loan plus down payment

#### A. Private lenders

Short term loan on single family dwellings

#### B. Mortgage brokers: agents for private loans

#### C. Mortgage bankers: lend their own or other's funds

#### D. Real Estate Investment Trust (REIT)

Must distribute 95% or more of income

Created by Federal law; involves at least 100 investors

Must get at least 75% of income from real estate activities

Credit Unions are a group of voluntary savers Pg 11-3

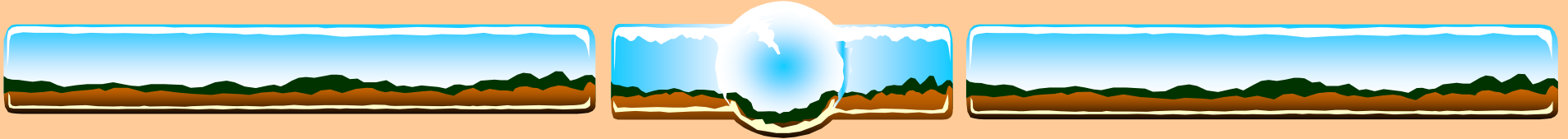
## VII. Private Mortgage Insurance (PMI)

- A. PMI sold by private insurance companies.

Premiums paid by borrower

- A. Strict credit requirements due to higher risk.  
Lender reimbursed if borrower defaults
- B. Required **80%** LTV, less than 20% down





## VII. Federal Housing Administration (FHA)

### A. Government insures NOT makes loan

1. Loan made from lender
2. Requires up-front mortgage insurance premium UFMIP
3. Requires annual premium fee paid monthly of  $\frac{1}{2}$  of 1% of unpaid balance

### B. Program

1. Payments = PITI (insurance)
2. Requires pest control certification
3. No secondary financing with NEW loan
4. Requires down payment
5. No maximum price. IS a maximum loan amount
6. 1-4 unit residential dwellings
7. Discount points are negotiable & paid by either party



# (FHA)

## C. Advantages of FHA

Lower down payment

Fixed or adjustable rate loans

Assumable with no prepayment penalty

Minimum property standards



## D. Disadvantages of FHA

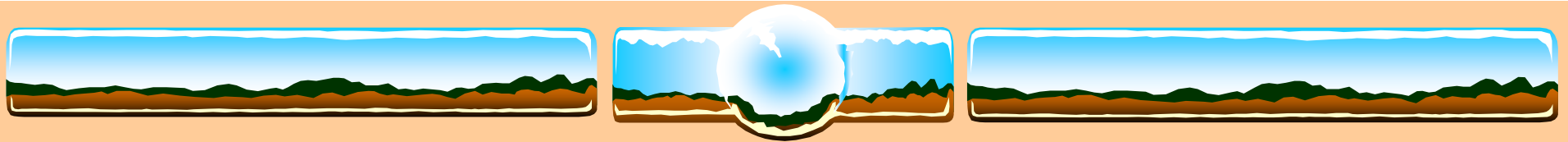
Buyer must pay their own impounds

Increased time

Property requirements may discourage sellers

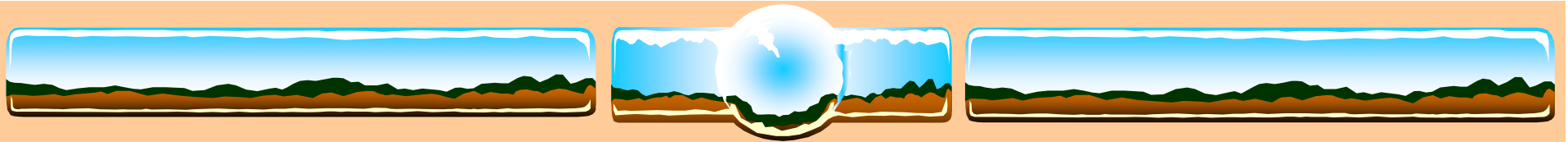
Relatively low loan limit

Cost of mortgage insurance decreases amount of home loan



## IX. Veteran's Administration (VA) LOANS

- A. DVA **guarantees** the loan to protect lender
- B. Loan information
  1. Interest rate negotiable between borrower & lender
  2. Value determined by **Certificate of Reasonable Value** (CRV)
  3. Zero down payment required
  4. Vet must have **Certificate of Eligibility** (DD214)
  5. Vet must occupy the property

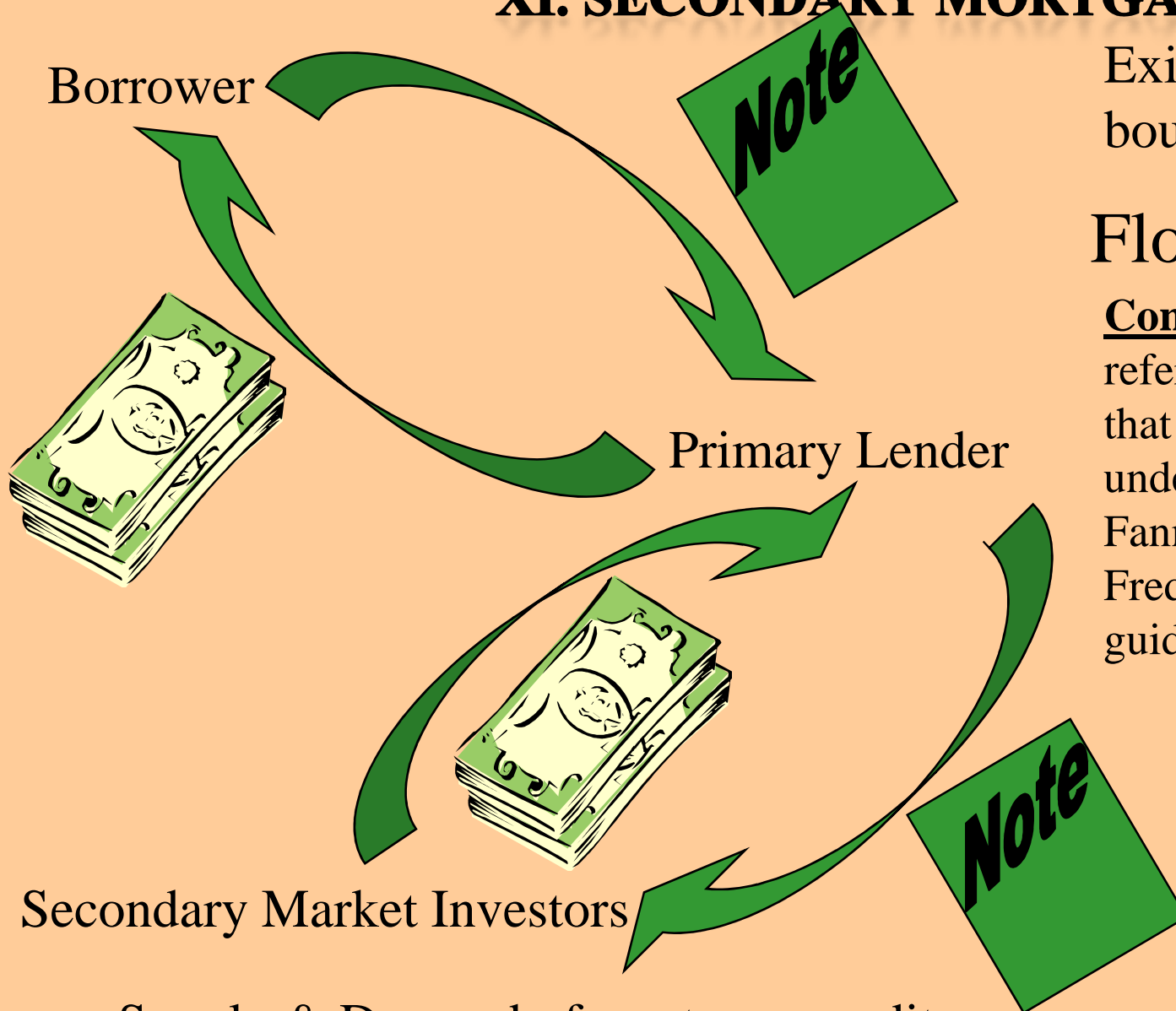


## X. California Farm & Home Purchase Program for Veterans (CAL-VET)

- ❖ All vets residing in California
- ❖ Title is in the name of the State\_of California
- ❖ Title passes to vet when state paid off
- ❖ Vet gets a long-term lease and land contract
- ❖ Veteran required to purchase life insurance policy
- ❖ Variable rate loan
- ❖ Funds received from sale of bonds
- ❖ Prepayment penalty of 2% during 1st 2 yrs of loan



## XI. SECONDARY MORTGAGE MARKET



Existing loans are bought and sold

### Flow of funds

Conforming loan refers to any loan that was underwritten using Fannie Mae and Freddie Mac guidelines.



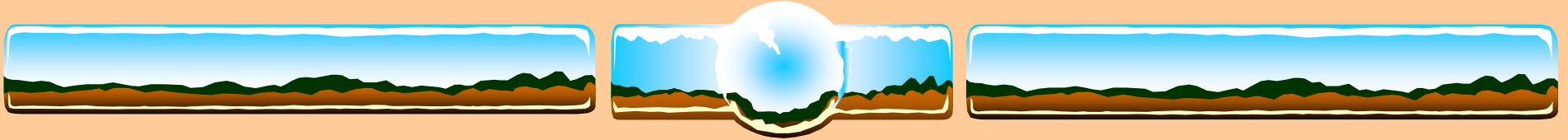
# XI. Secondary Mortgage Market

## Federal National Mortgage Association

### 1. Fannie Mae (FNMA)

- ❖ Issues stock to general public
- ❖ Provides blended rate mortgages
- ❖ Issues mortgage-backed securities
- ❖ FHA/VA/Conventional 1-4 units





# XI. Secondary Mortgage Market (cont.)

Government National Mortgage Association

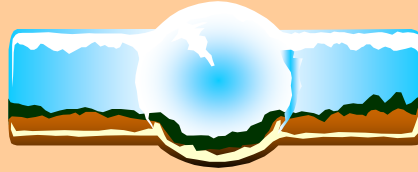
## 2. Ginnie Mae (GNMA)

- ❖ Guarantees securities issued by FHA-approved home mortgage lenders

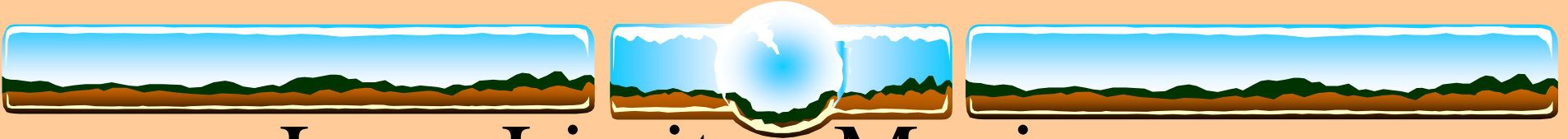
Federal Home Loan Mortgage Corporation

## 3. Freddie Mac (FHLMC)

- ❖ Issues stock to general public
- ❖ Buys and resells residential conventional mortgage loans
- ❖ Requires loan insurance if loan over 80% of appraisal

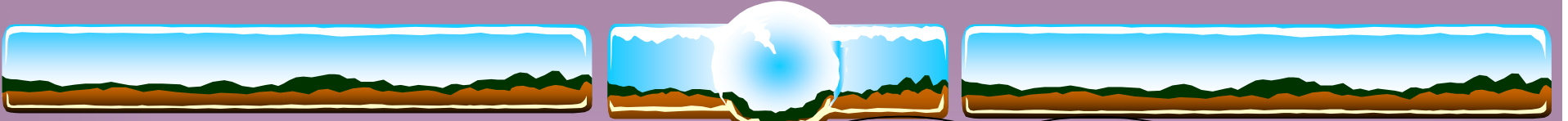


❖ PROGRAM	FHA	DVA	Cal-Vet	FNMA/FNLMC
What	1-4 units	1-4 units	1-4 units	1-4 units
Who	Anyone	Any veteran	Any veteran	Anyone
Maximum price	NONE	NONE	NONE	NONE
Interest Rate	Set by lender/market	Set by lender/market	Set by State of Calif.	Set by lender/market
Type of Interest	Fixed or variable	Fixed or GPM	Variable interest rate	Fixed or variable
Prepayment Penalty	None	None	2% of loan for 1st 5 years	Negotiable
Title Held By	Borrower	Borrower	State of California	Borrower
Program Name	Federal Housing Administration	Department of Veterans Affairs	California Department of Veterans Affairs	Conforming Conventional
Max Loan	as of 10-1-02	as of 9-25-02	as of 8-1-02	as of 1-1-03
Units: 1	\$253,650.00	\$322,700.00	Cal-Vet/VA	\$322,700.00
2	\$285,650.00		\$240,000.00	\$413,100.00
3	\$347,100.00		Cal-Vet 2000/97	\$499,300.00
4	\$400,500.00		\$250,000.00	\$620,500.00
			Cal-Vet 80/20	
			\$250,000.00	
Down	3%	0%	VA/2%	Negotiable
Payment			97/3%	
			20%	
Costs	1% Loan Origination Fee	1% Loan Origination Fee	1% Loan Origination Fee	Negotiable



# Loan Limits - Maximum

- ❖ VA – <http://www.benefits.va.gov> \$ \_\_\_\_\_
- ❖ FHA – [www.HUD.gov](http://www.HUD.gov)
  - ❖ 1 Unit \$ \_\_\_\_\_
  - ❖ 2 Units \$ \_\_\_\_\_
  - ❖ 3 Units \$ \_\_\_\_\_
  - ❖ 4 Units \$ \_\_\_\_\_
- ❖ Cal-Vet(1-800-952-LOAN) \$ \_\_\_\_\_
- ❖ FNMA/FHLMC ([www.fanniemae.com](http://www.fanniemae.com) )
  - ❖ Single Family \$ \_\_\_\_\_
  - ❖ Two Units \$ \_\_\_\_\_
  - ❖ Three Units \$ \_\_\_\_\_
  - ❖ Four Units \$ \_\_\_\_\_



**Finance is Magic**

**Let's go home**

