

Five New Rules for Getting the Right Mortgage

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(March, 2009)

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1. The Better Your Credit Score, the Lower Your Interest Rate

There was never a tiered pricing range with mortgages before the big bang in the mortgage industry. If your mortgage was approved, you got the same rate as everybody else. Under the new rules for mortgages, the better your credit the lower your interest rate. Your interest rate is calculated based on your FICO score and your loan to value of the mortgage. It is subjected to price tiering, which should be the same with most lenders, but ask to be safe. No matter how much equity you have in your home, a low credit score will affect your interest rate!

2. Cash Reserves Are Just as Important as FICO Scores!

The rules have changed as far as money and how much you have—or don't have. Borrowers used to need only to show just enough money to close; now they need to show more than enough.

Old mortgage guidelines required only your down payment, closing costs and two months housing payments in reserve after you closed. The new rules require a larger down payment, closing costs and six to twelve months payments in post-closing reserves.

The more reserves you have left over after the closing, the better able you are to continue making payments if you lose your job or run into financial trouble. The lenders now also look at total debt vs. liquidity. Thus, if you owe \$25,000 on credit cards and have \$40,000 in the bank, you could pay them all off if you had to. I used to ask borrowers to verify only enough money to make the deal work. Now I say show me the money and ask them for every account they have.

3. Fraudulent Appraisals and the lending process

The problem is that an appraisal is an opinion based on subjective research done by one person. The value can vary from person to person and therefore is somewhat arbitrary. The quandary has been compounded by the fact that the appraisal industry had been booming, and many people started new careers thinking they could earn big bucks on sheer volume alone. Appraisers were hiring inexperienced people to do the actual inspections and never visited the homes themselves. Then they hired other inexperienced people to do the research and would not always review it as carefully as they should have done. Business was booming and they had to keep up with the volume and turn-around time. Mortgage companies and realtors would drop them in a minute if

they couldn't turn the work around in a matter of days. A rush was considered same day turnaround. It was a crazy time, and everybody wanted a piece of the action. Lenders, also hiring green people off the street, could not properly train the staff to read and review the appraisals. Therefore, the underwriters were just rubberstamping them to get through all the files.

This whole situation led to manipulation. This process spiraled into an exacerbation of false inflation of values. You cannot tell me that something that was worth \$250,000 in 2004 was worth \$400,000 in 2006. It is impossible and unreasonable. Then the market began to lose steam, and inventory began to build. As more homes stayed on the market, buyers had more to choose from and could question prices.

Values were easily inflated during the real estate boom, which in turn enlarged loan amounts much higher than they should have been. As values decrease, appraisals are coming in lower, and loans are going upside down. When a loan is upside down, the borrower owes more than the home is worth. These situations will impede refinancing as well as selling. Unless the buyer must sell and can make up the difference out of pocket, they stay put.

As part of the appraisal, the last five years sales history is listed. It will show how many times the property sold and for how much. I suggest you ask the realtor for this info before you proceed. You will see if it transferred several times or if the seller is trying to make big buck on a flip deal.

4. Declining Market Values

If the home values in a certain area have declined between 10-15% year over year, then that area is considered a declining market. The geographic area can be a state, county or town. The year over year is measured is comparing current prices to the same time last year. This information is obtained from the Board of Realtors data on sales and listing.

The appraiser will include this information in the appraisal and the lender will reference the data they have on site. If the house is in a declining market value area, the lender has the right to take 5% off the top of the value and base the loan to value on that, which means the mortgage will be less than you think.

Richard is buying a house in Bronx, New York, for \$300,000 and applying for a \$270,000 mortgage, which is 90% loan to value. This county is listed as a declining market, and the lender is choosing to reduce the appraisal by 5%, making the value \$285,000. This will reduce Richards's loan amount to \$256,500, so he will have to come up with the difference. If he cannot, the deal will die.

To avoid falling into this situation, ask your realtor:

- The last two sales of the house, date and price
- A list of recent sales in the area, similar to your house, also known as "comps"
- If this home is in a "declining market value area"

Getting information like this helps in negotiating a price and will give you a comfort level with values.

5. For Sale: No refi allowed

Most banks will not allow a refi or cash out refi on any home that has been listed for sale within the last 12 months. The premise is that the house could not sell and are now pulling the equity out of the home, and if a buyer came along, they would sell it. Originating mortgages is expensive and the banks are not looking for short-term investments.

The time starts from the date of the listing or the date the listing was removed depending on the bank. They will want proof that the listing is distinguished and an explanation as to why the borrowers changed their mind and intension of staying.

Remember, if the listing was removed, it will remain in the listings that banks and appraisers use to research home values. The appraiser is obligated to state that the house was listed for sale in the last five years, so there is no way of hiding it. They think of everything that you can do!

Please contact Dale Robyn Siegel directly for additional information or to interview regarding the subject matter.

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