

**California Mortgage Loan Brokerage:  
A Practical Guide to Residential Loan Brokering and Lending**

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**Course Outline**

**Chapter 1 What Is a Mortgage Broker?**

Introduction

- Mortgage brokers assist consumers with home purchase financing
- Mortgage brokers in California must be licensed

The Role of the Mortgage Broker

- Mortgage broker brings together or provides services to the borrower and lender in a real estate transaction in exchange for compensation
- Loan agent works for the mortgage broker to perform brokerage activities

Licensing Requirements—Same as those for a real estate broker or a real estate salesperson employed by a real estate broker, good for four-year term

California Department of Real Estate—Offices in Sacramento, Fresno, Los Angeles, Oakland, and San Diego

Mortgage broker

- must be at least 18,
- legal resident of U.S.,
- pass qualifying examination,
- have been active as real estate salesperson for at least two of the five years preceding the application or have other relevant experience, or one year of experience if applicant has a two-year AA degree, or no experience if applicant has a four-year degree from an accredited college
- eight three-semester-unit college level courses
- three additional courses
- renewal requires 45 course hours of continuing education

Loan agent

- must be at least 18,
- legal resident of U.S.,
- pass qualifying examination,
- three college-level courses
- first renewal requires 15 course hours of continuing education, with 45 hours for subsequent renewals

## **Exercise 1.1**

Education recommended includes Mortgage Brokering and Lending course and continuing education in mortgage brokering and lending

### **Employment**

Employment agreement between mortgage broker and loan agent must be in writing

Policy manual details office hours, office procedures, and staff duties and stresses compliance with fair housing laws

Supervision of loan agent's work by mortgage broker required by Regulation 2725 of Real Estate Commissioner

Unlicensed employees can perform any act that does not require a real estate license, which typically includes office administration, accounting, and secretarial services, under broker's supervision; unlicensed employee can never participate in negotiations between borrower and lender

Licensed Mortgage Brokerage Activities—specified by California Real Estate Law, found in Business and Professions Code, which permits real estate broker to

- solicit borrowers or lenders
- engage as a principal with the public in buying, selling, or exchanging real property sales contracts or real property-secured promissory notes
- perform services for the public in connection with real property sales contracts or real property-secured promissory notes

Lender notification—if acting as a lender of his or her own funds, mortgage broker must notify Department of Real Estate annually in writing

Exemptions from licensing apply for a person who deals only with his or her own property and other persons identified by Real Estate Law

Trust fund accounts—required for broker to hold funds belonging to others in connection with transaction and must be in a neutral escrow depository

Document retention required for three years starting on the date a transaction closes of the date of loan application if transaction is not completed; broker pays for any required audit of accounts

- Failure to disburse funds makes broker liable for license suspension or revocation
- Delay to increase charges to borrower is prohibited and violation can include suspension or revocation of broker's license

Real Property Loan Law is Article 7 of the California Real Estate Law

- provides limits on loan amount and commission on specified loans of broker's own funds or funds of third party
- requires mortgage loan disclosure statement when loan is made or negotiated by a broker, with three business days after receipt of a completed written loan application or before borrower becomes obligated on note, whichever is earlier

### **Exercise 1.2**

California Residential Mortgage Lending Act, found in California Financial Code, covers licensing of mortgage bankers by California Department of Corporations

California Finance Lenders Law covers loan brokerage activities that do not involve real estate

### **Exercise 1.3**

#### **Summary**

#### **Open for Discussion**

#### **Review Questions**

## **Chapter 2 The Mortgage Marketplace**

### Introduction

- Adjustable rate mortgages at below-market interest rates and interest-only loans created high rate of loan defaults and property foreclosures
- Home buyers benefit from services of a knowledgeable loan agent

### Historical Perspective traces modern home mortgage industry to 1930s

The Central Bank of the United States—Federal Reserve System, the Fed, with 12 regional banks led by the Federal Reserve Board

- lends money to member banks at the discount rate and banks loan funds to borrowers at prime rate
- requires banks to meet reserve requirements

The Great Depression and the Federal Response after stock market crash of October 24, 1929

Federal Home Loan Bank System has 12 Federal Home Loan Banks under supervision of Federal Housing Finance Board

Federal Deposit Insurance Corporation (FDIC) insures deposits at financial institutions up to \$100,000 per account (\$250,000 for certain retirement accounts)

Home Owners' Loan Corporation, created by the Home Owners' Loan Act of 1933, used federal bond money to make 15-year mortgage loans at 5 percent interest to refinance existing loans; initiated color coding of metropolitan areas based on now-prohibited classifications, such as race and religion

Federal Housing Administration (FHA) was created in 1934 to insure home loans and also allowed 30-year mortgage terms

Veterans' Benefits provided by GI Bill of Rights (1944) and administered by Department of Veterans Affairs (VA) include guarantees on mortgage loans made to qualified veterans

Fannie Mae (1938) and Freddie Mac (1970) provide secondary mortgage market that makes more money available to lenders who sell them loans and are supervised by the Office of Federal Housing Enterprise Oversight (OFHEO)

Department of Housing and Urban Development (HUD) was created in 1965 to create housing programs and enforce Fair Housing Act

Ginnie Mae (1968) backs securities consisting of loans insured by FHA or guaranteed by VA

Real Estate and the Economy—relies on availability of goods and services that consumers want and can afford to buy; elements of production are demand, utility, scarcity, and transferability (DUST)

Real Estate Marketplace—not like other markets in some ways because real estate is *immobile* and every parcel of real estate is *unique*

## **Exercise 2.1**

### Real Estate Financing

Primary Mortgage Market—includes lenders who work on a retail (direct to consumers) or wholesale (through mortgage brokers) basis

- banks
- thrifts,
- mortgage companies,
- credit unions,
- commercial banks, and
- state and local housing finance agencies

California Housing Finance Agency (CalHFA) created by state in 1975

- assists first-time buyers with below-market interest loans
- provides mortgage insurance and
- makes loans on multifamily properties

### Obtaining Credit

Truth in Lending Act (TILA) implemented by Regulation Z of Federal Reserve Board requires disclosure of annual percentage rate (APR) of a loan and

- helps consumers compare loan terms and rates
- protects consumers against inaccurate and unfair credit billing and credit card practices
- provide rescission rights
- imposes rate caps on certain variable rate home loans
- imposes limits on home equity lines of credit and certain closed-end home mortgages

Community Reinvestment Act (CRA) created by Congress in 1977 to encourage financing in neighborhoods of low- and moderate-income residents

Equal Credit Opportunity Act (ECOA) of 1974 prohibits discrimination in consumer lending based on age, sex, race, color, marital status, religion, national origin, or receipt of public assistance

Home Mortgage Disclosure Act (HMDA), passed by Congress in 1975, requires lending institutions to report public loan data and is implemented by Regulation C of the Federal Reserve Board

California Fair Employment and Housing Act (FEHA) prohibits discrimination in the sale, rental, lease, or financing of housing on the basis of

- race,
- color,
- religion,
- sex (including gender identity),
- sexual orientation,
- marital status,
- national origin,
- ancestry,
- familial status,
- disability (physical or mental),
- medical condition, or
- source of income

A complaint alleging a violation of the law can be filed with the Department of Fair Employment and Housing

## **Exercise 2.2**

Credit Reporting

- Equifax
- Experian
- TransUnion

Credit Scores—Fair Isaac Corporation produces the FICO score, which can range from 300 (lowest credit score) to 850 (highest credit score), which is affected by

- number of borrower's new accounts
- length of time since borrower opened a new account
- number of recent requests for credit
- length of time since credit report inquiries were made by lenders
- whether borrower has good recent credit history following past payment problems

California Consumer Credit Reporting Agencies Act (CCRAA) requires notice to every applicant for a home loan

Fair Credit Reporting Act (FCRA) created by Congress in 1970 to protect privacy of consumer information by limiting access to credit history and payment information and amended by Fair and Accurate Credit Transactions Act of 2003 (FACTA) to protect against identity theft

California Housing Financial Discrimination Act of 1977 (Holden Act) prohibits financial institutions from discriminating in real estate loan decisions on the basis of

- race
- color
- religion
- sex
- sexual orientation
- marital status
- national origin
- ancestry
- familial status
- disability (physical or mental)
- medical condition
- source of income or
- conditions, characteristics, or trends in the neighborhood or geographic area surrounding the subject property (redlining)

### **Exercise 2.3**

#### **Summary**

#### **Open for Discussion**

#### **Review Questions**

## **Chapter 3 Getting Started as a Loan Agent**

### Introduction

- The principal broker must be licensed by the California Department of Real Estate
- The mortgage brokerage is the conduit between borrower and lender

The Loan Agent's Job—loan agent works for principal broker in soliciting and procuring loans, usually on a commission basis; should be “people person” and enjoy helping consumers

### Selecting the Mortgage Brokerage

Brokerage reputation in community, verified by friends, associations, companies in the industry and DRE, which will indicate any disciplinary actions

Length of time in business indicates community reputation; employee turnover indicates whether or not brokerage is a good place to work

Loan activity indicates likelihood of brokerage success

Media presence indicates knowledge of brokerage in the community

Training can assist new loan agent in acquiring skills necessary for success

### The Job Interview

Setting up the interview, either directly with principal broker or through office manager

Conducting the interview to determine if brokerage and prospective loan agent are a good fit: Will the employment relationship benefit both?

The Employment Decision—California Real Estate Law requires a written employment agreement between mortgage broker and loan agent

Compensation can be commission, salary, or combination of both

Office expenses paid by broker and expenses paid by agent should be indicated in the employment agreement

Term is typically for one year, renewing automatically unless terminated by either broker or loan agent

Work Responsibilities—may be specified in an employee handbook

Floor time

Dress

Safety considerations

Training should include updates in all legal and agency requirements

The Right Agent for the Client—the loan agent will not be the right person to work with every client

### **Exercise 3.1**

Success as a Loan Agent—include goal-setting to define the benchmarks that will indicate success

Business Plan—daily, weekly, and monthly schedules of activities that work toward the loan agent's goal(s)

Marketing Plan—deciding on the loan agent's client base and how best to reach prospective clients

DRE requires agent's identification in any advertising

Regulation Z enforces the federal Truth-in-Lending Act and requires that real estate loan advertising of loan terms include

- annual percentage rate (APR)
- any increase in interest rate over life of loan
- amount of down payment
- number of payments
- term of repayment
- amount of payment
- finance charge over the loan term

Advertising should never indicate a preference for clients that would violate protections against discrimination on the basis of

- race
- national origin
- religion
- sex
- age

## *California Mortgage Loan Brokerage*

- marital status
- familial status
- disability
- and any other state and local protected classes

Flyer can promote agent's background and services offered

Advertising should focus on AIDA—attention, interest, desire, and action

Web site can be a good marketing tool, if updated with information of use to consumers

Events and other media—being active in the community can benefit loan agent both personally and professionally, and also benefit the community

Mortgage trade groups

- California Association of Mortgage Brokers (CAMB)
- National Association of Mortgage Brokers (NAMB)  
Certified Residential Mortgage Specialist (CRMS)  
Certified Mortgage Consultant (CMC)

Realtor® associations provide opportunities for training, networking with other loan agents and real estate licensees, and participating in professional and community events

- California Association of Realtors®
- National Association of Realtors®
- Local association(s)

Multiple listing system will provide information on local property listings and sales

Appraisers in the local area should be known by the loan agent

- Northern California Chapter of the Appraisal Institute
- Southern California Chapter of the Appraisal Institute

### **Exercise 3.3**

#### **Summary**

#### **Open for Discussion**

#### **Review Questions**

## Chapter 4 The Primary Mortgage Market

### Introduction

- Promissory note is purchaser's promise to repay
- Security instrument places lien on property until debt is repaid and is referred to a mortgage although it can be a *mortgage* or *trust deed*

### Institutional and Non-institutional Lenders

Institutional Lenders—make most home loans

Commercial banks are members of the Federal Reserve System

- Federal banks are subject to National Bank Act and supervised by Comptroller of the Currency
- State-chartered banks are subject to the California Banking Law

Thrifts (savings and loan associations) in California are all required to insure accounts through the Savings Association Insurance Fund (SAIF) administered by FDIC

- Most thrifts are federally-chartered and may become members of the Federal Home Loan Bank System and are supervised by the Office of Thrift Supervision (OTS)
- Federal or state-chartered thrift can be owned by stockholders, with income distributed as dividends
- Mutual savings associations and banks distribute net earnings to depositors as dividends
- Loan by a thrift for more than 100 percent of property's appraised value must treat amount over 100 percent of value as unsecured
- Thrifts required to maintain *at least* 10 percent of all assets in residential loans

Credit unions keep majority of loans they make in their own portfolios, allowing them to be more flexible with lending criteria

- Organized under the National Credit Union Administration (NCUA)
- Limited to defined group called field of membership
- Deposits insured by National Credit Union Share Insurance Fund (NCUSIF) up to \$100,000 per account and \$250,000 for a retirement account

Insurance companies typically handle large commercial projects and are subject to California Department of Insurance (CDI) headed by elected California Insurance Commissioner

## Non-institutional Lenders

Private individuals make most second mortgages (junior loans)

Mortgage companies (mortgage bankers)

- Lend their own funds or funds borrowed from commercial banks, sell the loans to investors, and may service them
- Important source of funds for government-backed loans and conventional loans

Mortgage loan brokers

- Covered by California Real Property Loan Law
- Law applies to hard money (cash-out) loans but not to soft money (purchase money) loans

Non-financial institutions

- Own real estate or loans on real estate as business or investment activities
- Mortgage investment companies, pension funds, college and university endowments, trusts, estates, and others

## Types of Loans

Conventional v. Nonconventional Loans

- Conventional loans do not include any form of government backing
- Nonconventional loans are government-insured or guaranteed or have some other form of government backing

Conforming and Nonconforming Loans

- Conforming loan meets the underwriting criteria of Fannie Mae
- Conforming loan limits set by Office of Federal Housing Enterprise Oversight (OFHEO)
- Conforming loan limits based on mean (average) home price announced by Federal Housing Finance Board
- As a result of the Economic Stimulus Act of 2008, conforming loan limits for a one-unit property were raised effective April 1, 2008 for fixed-rate mortgages (May 1, 2008 for adjustable-rate mortgages) to
  - 125 percent of area median home price in high-cost areas, not to exceed \$729,750 except in Alaska, Hawaii, Guam and U.S. Virgin Islands;
  - if 125 percent of area median home price is less than \$417,000, the loan limit on a one-unit property will remain at \$417,000 (\$625,000 for Alaska, Guam, Hawaii, and U.S. Virgin Islands)

Jumbo Loans are loans in amount greater than conforming loan limits

Fixed Rate Mortgage (FRM)—interest rate stays the same over the life of the loan, 15 to 40 years

#### **Exercise 4.1**

Adjustable Rate Mortgage (ARM)—interest rate paid can change at stated intervals over the life of the loan

Initial loan rate may be “teaser” of discounted index rate

Index could be

- London Interbank Offered Rate (LIBOR)
- Certificate of Deposit Index (CODI)
- 11<sup>th</sup> District Cost of Funds Index (COFI)
- Cost of Savings Index (COSI)
- Constant Maturity Treasury (CMT) securities
- Lender’s cost of funds

Margin is number of percentage points added to index rate to determine applicable loan interest rate; fully indexed rate is the index plus the margin

Frequency of adjustment may be monthly, quarterly, biannually, annually, or at the end of three or five years, as agreed

Maximum adjustment usually determined by periodic adjustment cap and lifetime cap; if full amount of indexed rate is not charged because of a cap, increase will carryover to next adjustment period

#### **Exercise 4.2**

Payment cap limits amount of increase in loan payment

Negative amortization results when payment amount does not cover indexed rate

- Payment-option ARM gives borrower choice of making full payment or adding part of payment amount to loan balance
- Borrower who owes more than property’s market value is upside down
- Recast at specified intervals to reamortize at current balance

Hybrid ARMs (3/1, 5/1, 7/1, or 10/1 ARMs) typically offer fixed interest rate for first few years of loan and annual adjustment after that

#### Interest-only ARMs

- Interest rate adjusts but payment is interest-only
- May convert to a fully amortized loan at certain point with increase in loan payment to cover principal and interest

#### Prepayment penalties

Hard prepayment penalty is an extra fee

Soft prepayment penalty is imposed if loan is refinanced, but not if the property is sold

Conversion of ARM to fixed-rate loan maybe permitted by loan terms but may require conversion fee

Future of ARMs probably will not include the riskier products, such as the 2/28 ARM, and borrowers will have to qualify for loan payment based on full interest rate, not teaser rate

#### Fannie Mae requirements include

- Lender verification of borrower's income, assets, and liabilities
- Borrower debt-to-income (DTI) ratio that includes total monthly housing payments (PITI) as percentage of gross monthly income
- Borrower's loan qualification based on fully indexed interest rate and not initial rate

Balloon Payment—any loan payment more than twice the lowest payment

Reverse Mortgage—information available from DRE, HUD, FTC, and National Reverse Mortgage Lenders Association

- Carries substantial fee originate, depending on source
  - Single-purpose reverse mortgage is offered by some state and local agencies and nonprofits
  - Federally insured home equity conversion mortgage (HECM) is backed by HUD
  - Proprietary reverse mortgage is provided by a private company
- Provides regular payments to homeowner aged 62 or older
- Payment amounts based on value of property, homeowner's life expectancy
- Payments are tax-free and may have no income restriction

- Amount paid to homeowner accrues interest and become lien on home
- Total amount paid plus interest is repaid when homeowner/borrower moves, no longer uses the home as the principal residence, or dies
- If married couple initiates reverse mortgage, only one needs to occupy the home as the principal residence
- Amount repaid is limited to proceeds of sale of the property

### **Exercise 4.3**

Impound Account—also called escrow account, reserve account, or trust account

- Provides for monthly addition to loan payments that is held by lender to make payments for property taxes and insurance when due
- Required if loan-to-value ratio (LTV) more than 90 percent on origination, and may be required for LTV between 80 and 90 percent
- Borrower should verify that payments are made as required

Private Mortgage Insurance (PMI) required by lender if LTV is more than 80 percent

- Regulated by federal Homeowner's Protection Act of 1998 (HPA)
  - Borrower has right to request cancellation of PMI when remaining mortgage no more than 80 percent of original purchase price or appraised value at time of purchase, whichever is less
  - Lender must automatically cancel PMI when mortgage paid down to 78 percent of original loan amount
- PMI payments on loans originated after January 1, 2007, are tax deduction

Government-Sponsored Loan Programs

- Federal: FHA-insured loans and VA-guaranteed loans
- State: CalVet loans and CalHFA loans

### **Exercise 4.4**

#### **Summary**

#### **Open for Discussion**

#### **Review Questions**

## **Chapter 5 The Secondary Mortgage Market**

Introduction to secondary mortgage market

- Started with creation of Fannie Mae in 1938
- Freddie Mac created in 1970

The Market for Negotiable Instruments—enables lender to sell loans to generate funds to make more loans, while typically receiving a fee for servicing the loans sold

Negotiable Instruments make modern mortgage marketplace possible

- Promissory note serves as evidence of underlying debt
- Maker of note is promissory
- Holder of note is one to whom debt is to be paid

Creating a negotiable instrument requires

- Unconditional promise
- In writing
- To pay a specified amount of money on demand or at a stated or determinable future time
- Payable on the order of a designated person or the bearer of the note
- Signed by the maker of the note

Defenses to Payment

- Lack of consideration
- Prior payment
- Cancellation by the original note holder
- Set-off or reduction in amount owed
- Fraud in the inducement

Holder in Due Course who takes negotiable instrument for value, in good faith, and without notice of any defense against its enforcement

- Will not be subject to defenses to payment by promissory against original note holder
- Can transfer note to new assignee
- Note not enforceable if promissory lacked legal capacity, note was forged, or instrument involves an illegal activity

Mortgage-Backed Securities (MBS)—subject to rules of Securities and Exchange Commission (SEC)

### **Exercise 5.1**

Government-Sponsored Enterprises (GSEs)—supervised by Office of Federal Housing Enterprise Oversight (OFHEO) and subject to Federal Housing Enterprises Financial Safety and Soundness Act of 1992

Fannie Mae

- Federally chartered, shareholder-owned, private corporation
- Contributes to funding of OFHEO
- Purchases loans that it retains in its portfolio
- Issues MBS in exchange for pools of mortgages from lenders
- Guarantees principal and interest payments to MBS investors
- Establishes guidelines for lenders

Freddie Mac

- Federally chartered, shareholder-owned, private corporation
- Contributes to funding of OFHEO
- Issues MBS backed by conventional mortgages and other debt securities it issues
- Does *not* guarantee principal and interest payments

Ginnie Mae

- Government-owned corporation within HUD
- Provides secondary market for government-backed loans
- Guarantees payment of principal and interest on pools of eligible FHA, VA, RHA (Rural Housing Service) and PIH (Office of Public and Indian Housing) mortgages

Farmer Mac (Federal Agricultural Mortgage Corporation)

- Federally chartered but owned by shareholders
- Provides secondary market for agricultural real estate and rural housing mortgage loans
- Purchases the guaranteed portions guaranteed by the U. S. Department of Agriculture and first-lien loans that are senior to loans insured or guaranteed by federal or state agencies
- Issues long-term standby purchase commitments (LTSPCs) for new and seasoned mortgage loans
- Exchanges its Farmer Mac Guaranteed Securities for newly originated and seasoned mortgage loans in swap transactions
- Purchases and guarantees AgVantage bonds secured by eligible mortgage loans

Government Intervention—could be necessary if Fannie Mae and Freddie Mac are in financial difficulty

Non-Government Mortgage-Backed Securities

Collateralized mortgage obligations (CMOs) issued by investment banks and may be backed by subprime mortgage loans

Collateralized debt obligations (CDOs) include mortgages and other financial obligations

- Debt instruments separated into classes called tranches according to level of risk
  - Senior tranches rated AAA are paid first
  - Mezzanine tranches rated AA to BB paid next
  - Equity tranches are unrated and are paid last
- Collateralized loan obligations (CLOs) are backed primarily by leveraged bank loans
- Structured finance CDOs (SFCDOs) are backed by MBS and other asset-backed securities
- Commercial real estate CDOs (CRE CDOs) are backed primarily by assets of real estate investment trusts (REITs)
- Collateralized bond obligations (CBOs) are backed primarily by corporate bonds
- Collateralized insurance obligations (CIOs) are backed by insurance or reinsurance contracts

Secondary Mortgage Market Volatility—subprime lending crisis in U.S. has affected financial markets around the world

### **Exercise 5.3**

#### **Summary**

#### **Open for Discussion**

#### **Review Questions**

## **Chapter 6 First Interview with the Loan Applicant**

Introduction—most real estate transactions are completed with borrowed funds, which means that buyer must qualify for a loan

Loan Preapproval

- Conditional loan approval based on applicant's credit status
- Indicates buyer is ready, willing, and able

Initial Contact with the Client—loan agent's first opportunity to establish rapport with client

Telephone—preferred by most borrowers because easy and fast

Client questionnaire asks

Sales price of property

Borrower's income

Borrower's debts or other financial obligations

Initial phone interview should

Commit borrower to in-person appointment

Direct borrower to bring in documents to verify verbal statements

Have borrower come in to fill out loan application

Email—similar to phone contact but provides written record

Fax—not used very often

In-Person—best form of initial contact, taking no more than 15 minutes

Whom Does the Loan Agent Represent?

Loan agent represents borrower in dealings with lender

Loan agent owes client fiduciary duties

Loyalty

Good faith

Honesty

Obedience

Full disclosure

The Loan Application Interview—loan should be organized and work to establish rapport with client

Gathering the Necessary Information—need sheet will help determine documents borrower should bring to loan agent

Length of the Loan Application Process—initial answer within a day and loan commitment from lender usually within a week, subject to loan approval conditions

Questions That Are Not on the Loan Application

- Does applicant intend to occupy property as principal residence?
- Would applicant consider interest-only product?
- Will there be an escrow account for taxes and insurance?
- How long is the borrower likely to own the home?
- Does borrower want to pay off the mortgage before retirement?
- Is home stick-built or is it manufactured home?
- If applicant first-time homebuyer?
- When did applicant last own a home?
- Is applicant a candidate for a fixed rate, adjustable rate, government-sponsored, no-doc, or interest-only loan?
- What will be source of down payment money? If gift, statement from donor required.

**Exercise 6.1**

Avoiding Payment Shock

- Loan agent assists borrower in determining realistic level of housing expense for borrower
- Borrower typically pays up-front for credit report and possibly appraisal report

Worksheet will serve as checklist of documents required for loan application

Non-Permanent Resident Alien Home Loans

- Borrower must have valid Social Security Number (not ITIN)
- Copy of borrower's visa must be provided
- Borrower's verification of authorization to work in US required
- Minimum 10 percent down payment required
- Borrower must have two-year work and credit history
- Borrower's assets must be verified and must be in a U.S. account
- No diplomats
- Foreign nationals may qualify, probably with minimum 20 percent down payment

**Case Study**

**Exercise 6.2**

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 7 Taking the Loan Application**

Introduction—applicant will want to know the who, what, where, why, and how of the loan application process

### Uniform Residential Loan Application (URLA)

- Fannie Mae Form 1003
- Freddie Mac Form 65

- I. Type of Mortgage and Terms of Loan
- II. Property Information and Purpose of Loan—primary residence, secondary residence, or investment?
- III. Borrower Information
- IV. Employment Information
- V. Monthly Income and Combined Housing Expense Information
  - Income
    - Gross monthly income
    - Base employment income
    - Overtimes
    - Bonuses
    - Commissions
    - Dividends/interest
    - Net rental income
    - Other income
  - Housing expense
    - Rent
    - First mortgage principal and interest, if any
    - Other financing, such as second mortgage
    - Hazard insurance premium
    - Real estate taxes
    - Mortgage insurance
    - Homeowner association dues
    - Other housing expense, such as utilities

### **Exercise 7.1**

- VI. Assets and Liabilities—reported in single statement for co-borrowers, if appropriate
  - Assets
    - Liquid assets
    - Other assets

- IRS Schedule K-1 (Form 1065) required for real estate owned by borrower

Liabilities

- Borrower's outstanding debt, including account number, unpaid balance, and name and address of each creditor
- Subtracted from assets to determine borrower's net worth

VII. Details of the Transaction—final purchase price of property, including closing costs and funding fee, entered on loan application prior to submission

VIII. Declarations

Outstanding judgments

Bankruptcy

Foreclosure—including deed in lieu of foreclosure

Lawsuit

Direct or indirect loan obligation

Loan delinquency

Alimony, child support, and separate maintenance

Borrowed down payment

Piggyback loan is second loan used as down payment  
Collateralized loan obligations (CLOs) can make risky nature of some loans less obvious

Co-maker or endorser

U.S. citizenship

Permanent resident alien

Primary residence

Ownership interest in property owned in last three years, whether principal residence (PR), second home (SH), or investment property (IP)

- IX. Acknowledgement and Agreement—Loan applicant’s signature indicates awareness of following 11 items
- Penalties for failing to complete the form truthfully
  - Loan will be secured by a mortgage or deed of trust
  - Property will not be used for any illegal or prohibited activity
  - Information of purpose of acquiring home mortgage loan
  - Property will be occupied by borrower
  - Lender, related company, or loan services entitled to copy of application
  - Borrower must notify lender of any change to a material fact in loan app
  - If borrower delinquent in loan payments, report will be made to consumer credit reporting agency
  - Ownership of loan may be transferred by lender to another party
  - Lender and broker, agent, related company, or loan servicer make no representations of property condition
  - Signature of borrower in electronic or facsimile form considered as valid as original signature on printed form
- X. Information for Government Monitoring Purposes—regarding borrower’s ethnicity, race, and sex, and is voluntary, but if not provided loan interviewer is asked to supply information based on observation

Continuation Sheet/Residential Loan Application—for any supplementary explanation required by any part of the loan application, then signed and dated by borrower(s)

**Exercise 7.2**

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 8    Loan Application Disclosures**

Introduction—both federal and state law provide protections for home loan borrowers and the mortgage broker and loan agent must act in the client’s best interest

Add-ons to Complete the Loan Package

Schedule of Real Estate Owned

How Title Will Be Taken

- Joint tenancy
- Community property (husband and wife only)
- Community property with right of survivorship (husband and wife with right of survivorship as of July 1, 2001, in California)
- Tenants in common
- Single (never married)
- Unmarried (divorced)
- Widow (surviving wife)
- Widower (surviving husband)

Information Authorization—form gives mortgage broker authority to acquire information regarding loan application

Loan Pricing Notice—alerts borrower that interest rate has not yet been locked

Housing Financial Discrimination Act of 1977—requires notice and acknowledgment of fair housing law provisions

Fair Lending Notice—applies to any loan to purchase, construct, rehabilitate, refinance, or perform a home improvement on one- to four-unit residence

Privacy Policy Notice—in compliance with Privacy of Consumer Financial Information Act

Patriot Act Disclosure—in compliance with USA PATRIOT Act

Impound Authorization

Borrower’s Certification and Authorization

Notice to Applicants—disclosures required by Right to Financial Privacy Act of 1978 and borrower certifies that

- Special Information Booklet and Good Faith Estimate received

- Loan application made as of date notice is signed
- No commitment by the mortgage brokerage or lender to make a loan
- All information provided is accurate
- Permission given to concerned parties to verify information; federal crime to knowingly make false statements
- All questions on loan application apply to all borrowers
- Income received from alimony, child support, or maintenance payments need not be disclosed and income from part-time or temporary employment will be considered by lender based on stability and probable continuity of the income
- Equal Credit Opportunity Act (ECOA) prohibits creditors from discriminating against credit applicants based on race, color, religion, national origin, sex, marital status, age, income derived from any public assistance program, or exercise of any right under Consumer Credit Protection Act
- Flood insurance under Flood Disaster Protection Act of 1978 may be required
- ECOA prohibits creditor from using courtesy titles in correspondence except at borrower's request

### **Exercise 8.1**

Mortgage Broker Fee Disclosures—Mortgage Loan Disclosure Statement/Good Faith Estimate contains both state and federal disclosures

- Line 800: Items Payable in Connection with Loan
  - Lender's loan origination fee and loan discount fee
  - Appraisal fee
  - Credit report
  - Lender's inspection fee
  - Mortgage broker commission fee
  - Tax service fee
  - Processing fee
  - Underwriting fee
  - Wire transfer fee
- Line 900: Items Required by Lender to Be Paid in Advance
  - Interest
  - Mortgage insurance premiums paid at closing
  - Hazard insurance for one year
  - County property taxes prepaid by seller
  - VA funding fee, if applicable
- Line 1000: Reserves Deposited with Lender
  - Hazard insurance
  - Mortgage insurance
  - County property taxes
- Line 1100: Title Charges

- Settlement or closing escrow fee
- Document preparation fee
- Notary fee
- Title insurance
- Line 1200: Government Recording and Transfer Charges
- Line 1300: Additional Settlement Charges
- Subtotals of Initial Fees, Commissions, Costs and Expenses
- Compensation to Broker (Not Paid Out of Loan Proceeds)—yield spread premium
- Additional Required California Disclosures
  - Proposed loan amount and total of costs
  - General information about loan
  - Prepayment penalty, if any
  - Impound account, if any
  - Credit life or disability insurance not a requirement of the loan
  - Any liens that will be paid before closing
  - Applicability of Real Estate Law, depending on loan amount
  - Good faith estimate is not a loan commitment

Nontraditional Mortgage Products—separate disclosure form for interest-only, payment option, or other loans

Truth-in-Lending Act (TILA)—enforced through Regulation Z of Federal Reserve Board

#### Truth-in-Lending Terms

Annual percentage rate—loan cost considering all loan charges, including interest rate

Prepaid finance charges

Finance charge

Amount financed

Total of payments

Payment schedule

Submission of Truth-in-Lending Disclosure Statement

#### **Exercise 8.2**

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 9 The Art of Packaging a Loan**

Introduction—loan package must meet the lender’s requirements

### Required Documents

Cover Letter—explains why the lender will want to make the loan

### Completed Submission Sheet

Registration and confirmation—submission may include rate lock

Applicant and property information

Product information using lender’s code for the type of loan

Pricing Information including interest rate and lender’s cost/points

Second Mortgage, if applicable, indicating type of loan

Loan Information Change Request

### Uniform Underwriting and Transmittal Summary

- Fannie Mae Form 1008
- Freddie Mac Form 1077

### Automated Underwriting (AU)

- Desktop Originator® (DO) from Fannie Mae
- LoanProspector® (LP) from Freddie Mac

Credit Report—may be merged credit report with information from Equifax, Experian, and TransUnion

Typed Application—all information included on handwritten report

Handwritten Application—submitted to lender at first stage of application process

### Income Documentation

- Tax returns, signed and dated
- Bank statements
- Current pay stubs for last 30 to 60 days, including year-to-date total
- Current W-2

Preliminary Title Report—outstanding loans, property taxes, easements of record, and anything else that affects the property title

Purchase Contract—entire purchase contract including addendums and counteroffers, initialed by real estate principal broker or sales manager of listing office

Appraisal—Uniform Residential Appraisal Report (URAR) form prepared by appraiser licensed or certified by state of California

Disclosures

- Loan Pricing Notice
- Truth in Lending Statement
- Privacy Notice
- PATRIOT Act Disclosure
- Borrower’s Certification and Authorization
- Authorization to Release Information
- Financing Freedom Act
- Mortgage Broker Fee Disclosure
- Notice of receipt of disclosure
- Right to copy of appraisal
- Credit report disclosure
- Good-faith estimate
- Impounds
- Lock-in notice

Exercise 9.3

Final Submission Procedures

Loan Agent—dates and signs typed loan app

Broker Review

- Broker double checks figures and documents
- Loan agent makes one copy of submission package for brokerage file
- In automated system, turnaround time is
  - Two to four business days for purchase loan
  - Six to eight business days for refinance
  - Ten or more days for handwritten application

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 10 Closing the Loan**

Introduction—loan agent can submit loan package in a way that will highlight creditworthiness of loan applicant and assist lender in handling documentation efficiently

### Loan Submission

- Lender's preferred stacking order of documents in loan package will assist loan consideration
- Borrower's credit worthiness will rely on
  - Credit score
  - LTV down payment
  - Verifiable accounts
  - Verifiable income
  - Low debt to income ratio
  - Verifiable ID
  - Intent to occupy property
  - Excellent rental history

Rate Lock—makes timing critical if loan is to be closed during lock period

### Escrow

- Loan documents emailed to escrow officer, who prepares escrow instructions
- Borrowers notified by mortgage broker of signing date and time
- Final approval faxed or emailed by lender subject to any prior-to-document conditions
- Loan documents emailed from lender to escrow company after loan processor verifies figures
- Escrow officer prepares documents for signing and itemizes prior-to-funding conditions
- Escrow officer prepares audit sheet on day title is recorded
  - Borrower's name and vesting
  - Legal description of property
  - Insurance endorsement
  - Sales price and appraised value
  - Fees and charges, names or recipients, and disburseable amounts
- Escrow officer may send closing cost estimate to loan agent for review

### The Signing

- Figures based on estimated closing date
- Special loan instructions sent to escrow company by lender
  - Borrower's name
  - Loan number and amount
  - Interest rate and per diem interest
  - Payment amount and first payment date

- Maturity date
- Sales price
- Administrative fee
- Tax service
- Mortgage broker fee
- Rebate fee to mortgage broker
- Wire fee
- Flood certification fee
- Fannie Mae 1003 corrected
- Fannie Mae mortgage info
- Fannie Mae note, fixed or adjustable
- Compliance documentation
- Tax information
- W-9s
- Truth-in-lending statement
- Miscellaneous items

### **Exercise 10.1**

#### Additional Instructions—Conventional

- Borrower to present valid ID at settlement signing
- Borrower to sign final 1003 application
- Borrower to sign and date all documents
- Title policy endorsements provided, such as EPA
- Title policy to show lender's coverage at 110 percent of loan amount
- Documents reviewed for accuracy
- Legal description provided for deed of trust

#### Conditions Prior to Loan Documents

- Broker provides corrected 1003 for signing
- Broker provides page 2 of tax returns for original signature
- Broker provides signed 4506
- Cash back not to exceed \$2,000
- Valid photo ID provided by all borrowers
- Title for vesting verified
- Escrow provides HUD 1 with borrower's estimate of closing costs
- Evidence of insurance with lender listed as additional insured
- Explanation to borrower of all fees
- Evidence of appraisal report payment
- Evidence of credit report payment

#### Purchase Transactions—documents borrower will receive at closing

Note—property address, loan amount, and payment terms

Deed of Trust—security instrument preferred in California

Grant Deed—signed by seller

Mortgage Loan Application Disclosure Statement—DRE RE 885

Occupancy Affidavit—will be verified later

Fair Lending Notice—affirmation that there will be no discrimination

Compliance Agreement—allows lender to correct clerical errors

Notice of Availability of the Real Estate Appraisal—borrower has right to request copy of the appraisal at no charge within 90 days of close of escrow

Flood Certification—if property in flood plain, flood insurance required

IRS W-9 Form—necessary for borrower to deduct loan interest

IRS Form 4506—gives lender access to borrower's current tax return

Loan Servicing Disclosure Documents

Impound Account Authorization, if applicable

Title Insurance Policy—Request for change to new assignee—clauses

- Acceleration in event of sale, transfer of title, nonpayment of taxes, hazard insurance, or neglect of premises
- Alienation—name other than borrower on the note
- Assumption—only FHA/VA for fixed rate loan
- Foreclosure—no deficiency clause in California deed of trust
- Prepayment—no penalty in most Fannie/Freddie fixed rate loans
- Subordination—if seller carry back on building lot
  - Interim loan for short-term financing during construction
  - Take-out loan is permanent financing after construction finishes

Funding—in California, before 2 PM lender's local time (central time if lender's home office is in Midwest)

After Closing

- Escrow department audits file
- Checks issued after recording of title to mortgage broker, real estate agent, pest control company, and other service providers
- Lender makes sure details accomplished before selling the loan

## **Exercise 10.2**

Summary

Open for Discussion

Review Questions

## **Chapter 11 Government-Sponsored Financing**

Introduction—Government-sponsored programs have helped millions of families achieve the goal of home ownership

### CalVet Loans

Administered by California Department of Veterans Affairs (CDVA)

Oldest government-backed loan program in California

Financed by bond issues approved by California voters

### Eligibility

Residency—veteran who will live in property purchased in California

Veteran status—minimum active duty service of 90 days, evidenced by DD 214

### CDVA Training Programs

- Allow mortgage brokers to originate CalVet loans
- Only certified mortgage brokerage companies receive 1% CalVet loan origination fee
- Loan officers must attend CalVet training and sign CalVet Mortgage Broker Agreement
- Brokerage must originate three completed CalVet loans in two years to finalize certification
- CDVA limits number of participating brokers

CalVet Loan Features—current info available at [www.cdva.ca.gov](http://www.cdva.ca.gov)

- CalVet home loan interest rates
- Adjustable annually for all loans
- Lowest rate for honorably discharged veterans for single-family homes, condominiums, and manufactured homes on land—following *effective 2-07-2008*
  - 5.45% Qualified mortgage bonds
  - 5.50% Qualified veterans mortgage bonds
  - 6.10% Unrestricted funds

Maximum loan amount—\$521,250

Vesting is in CDVA until completed contract of sale, at which time title is transferred to the veteran

### Insurance

- Mandatory life insurance, special hazard insurance against flood and earthquakes, taxes, and liability insurance added to loan payment
- If veteran dies before loan paid off, debt is forgiven

Prepayment penalty--none

General information—most loans for 30 years

Special conditions

- No refi except for take-out loans after construction
- Junior financing allowed if combined loans not more than 90% of property value
- Property must be owner-occupied within 60 days of closing
- Property can be rented on prior approval of CDVA but not more than four years over life of the loan

California Veterans Homes—available to California veterans who are retired or disabled

### **Exercise 11.1**

FHA-Insured Loans—FHA-approved lenders are direct endorsers

Characteristics of FHA Loans

- Loan term usually 30 years
- Interest rate negotiable
- 1% loan origination fee plus discount points that can be paid by borrower, seller, or another party

How FHA-Insured Loans Differ from Conventional Loans

- Less stringent qualification standards
- Secondary financing restrictions prohibited
- Maximum loan amount depends on local limits and LTV rules
- Mortgage insurance required on all loans for duration of loan term
- No prepayment charges
- Home usually must be owner-occupied, but can be second home

FHA Programs based on fiscal year of October 1 through September 30

Title I—light or moderate property rehabilitation

Title II—two programs

- Section 203(b) for FRMs on owner-occupied dwellings of one to four units
- Section 203(b)(2) for single-unit residences for veterans

- Section 203(k) for purchase, refinance, and rehabilitation of residence of one to four units
- Section 234(c) for owner-occupied condos
- Section 245 for graduated payment mortgages
- Section 251 for ARMs

NEW—FHA Maximum Loan Amounts for High-Cost Areas as of April, 2008

One-Unit	\$729,750
Two-Unit	\$934,200
Three-Unit	\$1,129,250
Four-Unit	\$1,403,400

Loan to Value Ratio Limits

FHA Rule Opens Door—family members can loan funds for down payment

FHA Reform Legislation

**Exercise 11.2**

FHA Insurance Premiums—1/2 percent of loan amount for life of loan

Income Qualification—analysis of applicant’s income, net worth, and credit history

- Down payment at least 10%
- Proposed housing expense 10% or less over current housing expense
- Applicant has at least three months reserve mortgage payments
- Applicant has potential for increased earnings

Allowable Closing Costs

- Appraisal and inspection fees
- Credit report
- Lender’s origination fee
- Deposit verification fee
- Home inspection fee up to \$200
- Cost of title examination and title insurance
- Document preparation by third party
- Property survey
- Attorney fees
- Recording fees, transfer stamps, taxes
- Water test and certification fees

Allowable Costs in Refinance

- Courier fees
- Wire transfer fees
- Fees to pay off bills
- Reconveyance fees

Assets for Closing

- Minimum cash investment
- Prepays
- Discount points borrower will pay
- Upfront MIP, if not financed
- Any closing costs, repair costs, or other expenses

VA-Guaranteed Loans

Eligibility—based on length of service in U.S. armed forces during wartime or peacetime and honorable discharge

The VA Guarantee

- Protects lender against loss
- Can be used for purchase, refinance, or construction of owner-occupied dwelling of one to four units

Characteristics

- No down payment
- No maximum loan amount
- No maximum income limits
- Underwriting standards more liberal than FHA's
- Usually 30-year FRM, but ARMs can be guaranteed until 10-01-2008
- No mortgage insurance required
- No maximum/minimum interest rate set by VA
- Lender may only charge 1% origination fee and reasonable discount points that can be paid by borrower, seller, or third party
- No prepayment penalty
- Forbearance extended to homeowners with temporary financial difficulties
- VA-guaranteed loans assumable by any qualified buyer but veteran's entitlement not restored unless there is a full release of liability
- Lender handles loan
- Seller can pay for closing costs if concessions no more than 4% of loan amount and limited to certain items
- Veteran does not have to be first-time homebuyer
- Benefit may be reused if loan repaid

Funding Fee

- 1.25% of loan amount with down payment of 10% or more
- 1.5% of loan amount with down payment between 5% and 10%
- 2.15% of loan amount if down payment less than 5%
- Exemption from funding fee for
  - Veterans with service-connected injuries
  - Surviving spouses of veterans who died as result of service-connected disability

Entitlement Amount--\$36,000 or up to 25% of Freddie Mac conforming loan limit

Loan Amount—generally the limit for conforming loans

Qualifying Requirements—include debt-to-income ratio of 41%

Certificate of Reasonable Value (CRV)—appraiser’s opinion of property value

- Amount of guarantee based on CRV or sales price, whichever is less
- If property appraises for less than sales price:
  - Buyer can make up difference in cash or
  - Seller can accept lower amount as sales price or
  - Buyer and seller can compromise or
  - Transaction can be canceled

Steps in Processing a VA-Guaranteed Home Loan

- Veteran must have Certificate of Eligibility
- Veteran selects home
- Contract must contain escape clause referencing CRV
- Veteran contacts lender
- Lender processes credit and income information
- On receipt of appraisal and other documentation, lender/mortgage broker underwrites the loan and, if it qualifies, sends it to investor/lender underwriter for final approval
- Closing that meets all legal requirements held by title and escrow company

Closing Costs

Lender 1% loan origination fee

Discount points

VA funding fee

Appraisal

Credit report

Recording fees

Taxes/assessments chargeable to borrower

Title insurance and escrow accounts  
Hazard insurance including flood insurance  
Survey, if required

Additional VA Loan Guarantee Programs

- VA streamline finance
- Cash-out refinance
- Conventional to VA mortgage

**Exercise 11.3**

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 12 Tax Advantages of Home Ownership**

Introduction—tax advantages of home ownership depend on homeowner's income and amount of deductible interest

### **How Home Ownership Can Benefit Taxpayers**

Deductibility of Home Mortgage Interest—depends on taxpayer/homeowner's tax bracket

- Applicable law—IRC § 163
- Interest deductible on loan value of no more than \$1 million secured by borrower's principal residence and/or second home
- Loan must be acquisition financing or no later than 90 days from date homeowner takes title
- Loan may not exceed original purchase price of home; on refinance, only interest paid on remaining balance of original is deductible unless
  - New loan or refi is for capital improvements to the home *or*
  - Interest on part of a new loan or refi is used for allowable medical or educational expenses *or*
  - Homeowner borrows home equity loan of up to \$100,000 secured by the home over the term of ownership

Who benefits—depends on homeowner's income and amount of deductible interest

Points are deductible if

- Loan secured by main home
- Paying points is established practice in the area
- Points were not more than what is usually paid in the area
- Taxpayer uses cash method of accounting
- Points were not paid for separately stated items
- Not paid with borrowed funds
- Loan used to buy or build main home
- Points computed as percentage of loan principal
- Points clearly shown on settlement statement

### **Exercise 12.1**

Deductibility of Property Taxes

- Special assessments (benefit assessments) do not qualify
- Mello-Roos assessments do not qualify
- Prop 13 limited property tax to no more than 1% of a property's base year value plus indebtedness incurred by the taxing authority and bonded indebtedness approved by voters after July 1, 1978

- Base year value increased to property's market value at time of reassessment event
- Homeowner's exemption from taxation of first \$7,000 of property's cash value;
- Veteran's exemption of \$4,000 of value on property not already subject to homeowner's exemption
- No reassessment event if property transferred between spouses
- No reassessment event if principal residence and up to \$1 million in assessed value of other real property is transferred between parents and children; if no surviving parents, grandparents can take the place of parents
- Homeowners age 55 or older (or severely disabled) can buy or build another home in the same county and transfer the assessed value of the old home
- Homeowners age 55 or older (or severely disabled) can sell property in one county and transfer assessed value to new property, if new county allows transfer
- No reassessment for property improvements for accessibility by severely disabled person
- Property Tax Postponement Law for taxpayers age 62 or older, or who are blind or disabled
- Homeowner Assistance Program provides tax rebate to taxpayer age 62 or older, or blind or disabled, who meets income limit
- Renter Assistance Program

#### Property tax payments

- Two installments, with 10% penalty for late payment
- First installment overdue after December 10
- Second installment overdue after April 10
- Nonpayment can result in tax lien placed on property

#### Property tax lien procedure

- Property taxes become lien on property on January 1 of tax year
- Delinquent tax list published in newspaper on June 8 of tax year
- 10% penalty added to delinquent tax payment
- Past due amounts can be paid over five years
- If amount owed are not paid within five years, property is sold within the next two years at public auction to allowed parties
- Highest bid at public auction must be at least 50% of property's fair market value
- Sale must be approved by County Board of Supervisors
- High bid must be paid in cash, negotiable paper, or combination

- High bidder receives a tax deed

Other tax liens--federal, state, or loan

Documentary transfer tax—required at time deed to new owner is filed with county recorded

## **Exercise 12.2**

Exclusion from Taxation of Profit on Sale of Home

- \$250,000 maximum profit exclusion for single person
- \$500,00 maximum profit exclusion for married couple
- If spouse dies, survivor can use full \$500,000 exclusion on sale of the principal residence that takes place within two ears of date of spouse's death
- If tenancy in common, each owner entitled to full \$250,000 exclusion, or \$500,000 for share owned by married couple
- Property must be occupied as principal residence for at least two of the five years preceding the sale
- Deduction taken in proportion to part of two years of residency if home seller had to sell before two years of residency if move from home required by
  - Change in employment, with new job at least 50 miles farther to travel than old job
  - Health reasons
  - Unforeseen circumstances, such as natural disaster or divorce

## **Exercise 12.3**

Private Mortgage Insurance (PMI)—usually required if down payment less than 10% of loan amount and may be required if down payment 10-20% of loan amount

How PMI Is Cancelled or Terminated—Homeowner's Protection Act (HPA) applies

- Homeowner can request cancellation when equity at least 20% of original purchase price or appraised value of home
- PMI must be cancelled automatically by lender or loan servicer when mortgage paid down to 78% of value; 77% for some high-risk loans
- HPA does not define "high risk"
- Lender must terminate PMI within 30 days of borrower's cancellation or date of automatic termination and cannot collect PMI premiums after that date

- If not cancelled or terminated earlier, PMI must be removed when the borrower has reached midpoint of amortization period

Disclosures required by HPA include written amortization schedule for FRMs

Tax Deductibility of PMI Payments

Allowed by Mortgage Forgiveness Debt Relief Act of 2007

Applies to loans originating from January 1, 2007, through December 31, 2010

Phases out when household adjusted gross income (AGI) exceeds \$100,000, at 10% per year until deduction eliminated at AGI over \$110

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 13 Property Appraisal and Insurance**

Introduction—accurate property valuation helps all parties to a transaction

Appraisal: The Key to Successful Loan Closure

- Business and Professions Code prohibits real estate licensees from performing any appraisal activity that affects the licensee's compensation
- Civil Code prohibits persons with an interest in a real estate transaction from improperly influencing or attempting to improperly influence the development, reporting, result, or view of a real estate appraisal sought in connection with a mortgage loan

Federal Role in Appraiser Licensing—initiated by savings and loan crisis of 1980s and passing of Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA)

- Appraisal Subcommittee of House of Representatives makes recommendations to Congress
- Appraisal Foundation is independent, nonprofit association of industry groups
  - Appraiser Qualifications Board sets education and experience standards for appraisers
  - Appraisal Standards Board determines Uniform Standards of Professional Appraisal Practice (USPAP)

Appraiser Licensing in California—enforced by Office of Real Estate Appraisers (OREA)

- Trainee license
  - 150 classroom hours including 15-hour course in USPAP
  - No experience
  - Can only work under supervision of licensed appraiser
- Residential license
  - 150 classroom hours including 15-hour course in USPAP
  - Minimum of 2,000 hours of acceptable appraisal experience over at least 12 months
  - Performs appraisals of noncomplex 1-4 unit residential property up to \$1 million value and nonresidential property up to transaction value of \$250,000
- Certified residential license including 15-hour course in USPAP
  - 200 classroom hours and associate's degree (or 21 semester credits in specific subjects in lieu of degree)
  - Minimum of 2,500 hours of acceptable appraisal experience over at least a 30-month period
  - Performs appraisals of all 1-4 unit residential property and nonresidential property to transaction value of \$250,000
- Certified general license including 15-hour course in USPAP

- 300 hours of classroom instruction and bachelor's degree (or 30 semester credits in specific subjects in lieu of the degree)
- Minimum of 3,000 hours of acceptable appraisal experience over at least a 30-month period, with at least 1,500 hours in nonresidential property appraisal
- Performs appraisals of all real estate without regard to transaction value or complexity
- Renewal of any license requires 7-hour USPAP course every two years and 14 classroom hours for every year of licensing

### **Exercise 13.1**

#### The Language of Appraisal

- Appraisal—act or process of developing opinion of value
- Appraiser—one who performs objective valuation services
- Market value—presumes transfer of property in arm's-length transaction
- Arm's-length transaction
  - Buyer and seller act without duress
  - Buyer and seller know property's assets and defects
  - Property marketed for reasonable length of time
  - Financing terms typical for similar property sales
- Duress—results from unusual conditions
- Opinion of market value—provides supporting data
- Price—amount asked, offered, or paid for a property
- Real estate—in California, means same thing as real property, so both can be used to refer to the land or the rights of ownership of land

#### The Appraisal Process—includes the appraiser's scope of work

#### Three Approaches to Value

- Sales comparison approach considers recent sales and listing process of comparable properties
- Cost approach considers cost to construct at today's prices, less depreciation, added to land value
- Income approach capitalizes income generated by property; gross income multiplier offers simplified version that uses ratio of income to market value

#### The Appraisal Report

- Defined by USPAP
  - Complete appraisal includes full data
  - Limited appraisal provides only information requested by client

- Self-contained report includes all pertinent data and appraiser's reasoning
- Summary report provides most important data and appraiser's reasoning; example is Uniform Residential Appraisal Report (URAR) used by Fannie Mae and Freddie Mac
- Restricted use report contains none of appraiser's research and reasoning

Desktop Underwriter—software that includes automated valuation model (AVM)

#### Fannie Mae

- Requires appraisal by only a licensed or certified appraiser
- Sets strict guidelines

#### Definition of market value

- Buyer and seller typically motivated
- Both parties well informed or well advised, acting in their own best interests
- Reasonable time for marketing property
- Payment in cash in U.S. dollars or comparable financial arrangements
- Price represents normal consideration for property sold

#### Precautions against property flipping

- Confirmation that property seller (purchase money transaction) or borrower (refinance transaction) is legal owner of the property
- Lender analysis and review of sale and sales price to confirm that appraiser's opinion of value is "reasonable and representative of the market"

Date of appraisal report—no more than 12 months prior to date of note and mortgage, with market influence noted if more than 4 months prior

#### Unacceptable practices

#### Freddie Mac requires

- Written appraisal report
- Written inspection report or
- Property Inspection Alternative (PIA)

Loan Prospector® software

Property Inspection Alternative

- Property owned in fee simple
- Property fully completed and occupied as of date of promissory note
- Property not undergoing rehabilitation or renovation
- No appraisal or inspection performed
- Lender is unaware and could not have been aware of conditions that would adversely affect market value, condition, or marketability
- Borrower not affiliated or related to builder, developer, or seller
- Cannot be used for manufactured homes, leaseholds, seasoned mortgages, mortgages with potential for negative amortization, A-minus mortgages, newly constructed homes, or initial interest mortgages

Notice About Appraisal of Your Property—required for purchase money mortgages using LoanProspector®, Condition and Marketability Report, or PIA in lieu of property appraisal

Who Pays for the Appraisal? Typically, the borrower, who must be provided with a copy of the appraisal, if requested

### **Exercise 13.2**

Homeowner's Insurance—covers

- Damage to property from natural disaster or accident
- Damage or loss to personal possessions in the home
- Liability caused by injury to someone hurt while on the property
- Temporary living expenses while the home is being repaired or replaced

Insurance Licensing

- Fire and casualty broker-agent
- Life agent
- Personal lines broker-agent

Underwriting criteria determine insurer's level of acceptable risk

- Full replacement value coverage pays full dollar amount needed to repair or replace damaged structures or personal possessions
- Actual cash value coverage covers only fair market value of goods prior to damage or destruction

Flood Insurance

- Typically excluded from homeowners' insurance policies
- Required if property located in flood plain
- Available through National Flood Insurance Program administered by Federal Emergency Management Agency (FEMA)

Mortgage Insurance—covers remaining loan balance if borrower suffers death or severe disability (provided by CalVet automatically), but typically more expensive than comparable amount of life insurance

**Exercise 13.3**

**Summary**

**Open for Discussion**

**Review Questions**

## **Chapter 14 Mortgage Fraud and Foreclosure**

Introduction—the loan agent should be able to recognize the most common types of mortgage fraud and assist a homeowner who is facing foreclosure

### **Mortgage Fraud**

Sometimes difficult to detect because of the number of times a mortgage changes ownership in the secondary mortgage market

A federal crime investigated by the Federal Bureau of Investigation (FBI)

### **Types of Mortgage Fraud**

Fraud to acquire property—also called fraud for housing

- Homebuyer lies about income, debt, or other loan app info
- Loan agent should verify that funds required for down payment and closing costs are on hand or from a known source
- Does buyer have funds to make necessary renovations?
- Is buyer's income sufficient to pay projected expenses?
- Intent to occupy should be verified

Fraud to acquire cash—also called fraud for profit

- Property flipping involves purchase, fraudulent appraisal at higher value, and quick resale
- Silent second--buyer borrows some or all of down payment but doesn't tell lender about the loan
- Nominee loan with straw buyer conceals identity of borrower so lender makes loan to unqualified borrower
- Fictitious or stolen identity involves use of personal information without person's knowledge or consent
- Inflated appraisal is performed by appraiser who is part of the scam
- Equity skimming uses a straw buyer, false income documents, and false credit reports to obtain funds and no payments are made on loan
- Air loan is one in which non-existent property is financed by fictitious borrower using fabricated appraisal

### **Case 1**

### **Case 2**

Predatory Lending—foreclosure fraud

- Involves homeowner at risk of default or already in foreclosure
- California Civil Code covers abuses of mortgage foreclosure consultants

- Notice and other steps must be followed if assistance offered in foreclosure by someone other than attorney or real estate licensee
- Violation of law punishable by both fine and imprisonment

### **Exercise 14.1**

The Foreclosure Process—different depending upon whether security instrument is mortgage or deed of trust (though both are commonly referred to as a mortgage)

Judicial Foreclosure of a Mortgage—mortgage is lien on property given by mortgagor (borrower) to mortgagee (lender)

Court action—judicial foreclosure typical of mortgage, though mortgage could include a power of sale

Reinstatement right of borrower to cure default before foreclosure sale by paying all past due amounts and fees

Foreclosure sale results in certificate of sale from sheriff or commissioner to purchaser at sale

- Certificate of sale should be recorded immediately
- Foreclosed borrower has redemption period of three months in which to buy back the property unless lender seeks deficiency judgment, which makes redemption period 12 months
- Lender executes certificate of discharge to clear cloud on title created by the mortgage lien

Deficiency judgment

- Legal action by lender if foreclosure sale does not pay entire debt
- Not allowed in California if
  - Mortgage was a purchase money debt held by property seller *or*
  - Debt was undertaken to pay all or part of purchase price of owner-occupied residential dwelling of 1-4 units

Debt forgiveness cannot be taxed by IRS as income for three years following passage of Mortgage Forgiveness Debt Relief Act of 2007 in December, 2007

Trustee's Sale in California—possible under deed of trust in which trustor (borrower) transfers title to trustee (third party) for benefit of beneficiary (lender)

Notice of default

- Sent to borrower, junior lienholders, and anyone who files request for notice
- Must be in Spanish, Chinese, Tagalog, Vietnamese, or Korean if loan agreement was negotiated in that language
- Newspaper notice required if anyone other than trustor receives notice

Declaration of default from beneficiary to trustee states basis for the default

Trustee's sale (nonjudicial foreclosure)

- Notice of trustee's sale no sooner than 90 days after notice of default recorded
- Trustor has right of reinstatement
- Beneficiary can credit-bid up to amount of debt owed
- Trustor has *no* right of redemption
- Purchaser can take possession of property immediately after sale

Alternatives to Foreclosure

What a consumer can do

- Contact lender immediately
- Give mortgage payment priority over other debts
- See financial counseling

How mortgage brokers can help—assist homeowner with the above steps

Deed in lieu of foreclosure—possible only if acceptable to lender

**Exercise 14.2**

Bankruptcy

- Should be considered last resort only
- Subject to Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)

Chapter 13—The Wage Earner's Plan

- Available to individual who receives regular income, even if self-employed or owner of unincorporated business
- Individual's unsecured debts must be less than \$207,675 and secured debts less than \$922,975 (amounts adjusted to track consumer price index)

The petition includes schedules of assets and liabilities and other documents

The plan to pay all or part of debts owed is subject to court approval

Procedure includes meeting of creditors who file claims with the court

Discharge from indebtedness will be given to debtor when all payments have been made as required by plan

Advantages—allows debtor opportunity to save home from foreclosure

#### Chapter 7—Liquidation of Assets

- Provides for liquidation of debtor's assets to pay creditors
- Debtor may be individual, partnership, corporation, or other business entity

The petition includes individual's assets, liabilities, and outstanding contracts

Procedure includes meeting of creditors and sale of debtor's nonexempt assets to maximize amount available to repay creditors

Discharge only available to individuals and may not clear all debts (such as property liens)

California Homestead Protection exempts certain amount of homeowner's equity from forced sale

- \$50,000 for homeowner
- \$75,000 for homeowner who is member of family unit
- \$150,000 if homeowner or spouse who resides with homeowner is 65 years of age or older
- \$150,000 if homeowner or spouse who resides with homeowner is physically or mentally disabled and unable to work
- \$150,000 if homeowner is 55 or older and has gross annual income of no more than \$15,000, or combined income of homeowner and spouse if no more than \$20,000 and homestead is subject to involuntary sale

### **Exercise 14.3**

#### **Summary**

#### **Open for Discussion**

**Review Questions**

## **Chapter 15 Transaction Calculations**

Introduction—facility with calculator will enable loan agent to work efficiently and accurately

Selecting a Calculator—should be easy to use, be designed for real estate calculations, and have easy-to-follow documentation

### **Exercise 15.1**

Putting It into Practice

Percentages

- Interest rates
- Property taxes
- Prorations and other calculations

Down Payment expressed as percentage of purchase price

### **Exercise 15.2**

Points—a point is the same as 1%

- Discount point is loan fee
- Basis point is one hundredth of 1%

Qualifying ratios—percentage of loan applicant's income that is maximum allowed by lender for either housing expense or all debts

### **Exercise 15.3**

Converting Fractions to Decimals

Annual Interest—loan amount  $\times$  interest rate = annual interest

### **Exercise 15.4**

Monthly Payment

### **Exercise 15.5**

### **Exercise 15.6**

Remaining Loan Balance

Prorations

Property tax

**Exercise 15.7**

Interest

**Exercise 15.8**

Refinance

**Exercise 15.9**

**Exercise 15.10**

**Summary**

**Review Questions**