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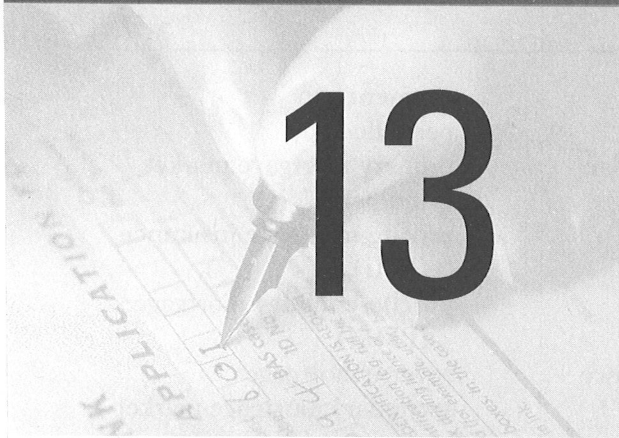

13 TYPES OF MORTGAGES AND SOURCES OF FINANCING

LEARNING OBJECTIVES

When you have completed this unit, you will be able to accomplish the following.

- Explain the process of qualifying for a loan and calculate the qualifying ratios for different types of mortgage loan programs.
- Describe the features of conventional mortgages.
- Describe the features of an amortized mortgage and an adjustable-rate mortgage, including the components of an adjustable-rate mortgage.
- Describe the characteristics of FHA-insured mortgages and common FHA loan programs.
- Identify the guarantee feature of VA mortgage loans and the characteristics of VA loan programs.
- Distinguish among the various types of purpose-specific mortgage products.
- Distinguish among the primary sources of home financing.
- Describe the role of the secondary mortgage market and know the features of the major agencies active in the secondary market.
- Recognize and avoid mortgage fraud.
- Describe the major provisions of the federal laws regarding fair credit and lending.

KEY TERMS

adjustable-rate mortgage (ARM)
amortized mortgage
annual percentage rate (APR)
balloon payment
biweekly mortgage
Closing Disclosure
conforming loan
conventional loan
demand deposit
disintermediation
entitlement
home equity conversion mortgage (HECM)
home equity loan
housing expense ratio (HER)
index
intermediation
level-payment plan
lifetime cap
Loan Estimate
margin
mortgage broker
mortgage fraud
mortgage insurance premium (MIP)
mortgage lender
mortgage loan originator (MLO)
negative amortization
nonconforming loan
nonconventional loan
package mortgage
partially amortized mortgage
payment cap
periodic cap
primary mortgage market
principal
private mortgage insurance (PMI)
purchase money mortgage (PMM)
reverse mortgage
secondary mortgage market
teaser rate
total obligations ratio (TOR)
triggering terms
up-front mortgage insurance premium (UFMIP)

INTRODUCTION

This unit begins by discussing the process of qualifying for a mortgage loan and determining the qualifying ratios for different types of mortgage loan programs. Conforming and nonconforming loans are defined. Conventional fixed-rate amortized mortgages and conventional adjustable-rate mortgages are presented first, followed by nonconventional FHA-insured and VA-guaranteed mortgages. The unit also describes the role of the secondary mortgage market and the major provisions of federal laws regarding fair credit and lending procedures.

13.1 QUALIFYING FOR A LOAN

Loan Application Process

Lenders use the Uniform Residential Loan Application (URLA) form to qualify applicants (borrowers) applying for a one- to four-family residential property. The URLA requests general background information in addition to current and previous employment and monthly gross income (before deductions, including income tax and Medicare deductions). If the applicant has additional income from other sources that the applicant wants considered for the loan, the applicant can list the monthly income and income source. Assets and liabilities are also declared.

The applicant indicates the purpose of the loan and information about the property that the applicant is wanting to purchase or refinance, including whether the property will be used as a primary residence, second home, or as an income-producing property. The URLA also asks specific questions about the source of funding for the loan and past financial history, including, for example, whether the applicant is in default or delinquent on a federal debt, there are any outstanding judgments, or within the last seven years the applicant has had a property foreclosed upon or the applicant has declared bankruptcy.

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The Uniform Residential Loan Application (URLA) form can be downloaded at https://singlefamily.fanniemae.com/media/7896/display.

Credit Evaluation and Credit Scoring. Lenders review the applicant's credit history. A *credit report* is ordered to determine the applicant's debt and credit score. A *credit score* is a number that has been calculated based upon the borrower's repayment history, and the amount and types of debt, and it assists lenders with predicting whether an applicant is likely to make timely credit payments. Lenders use credit scores to measure potential risk of making a loan. Higher credit scores mean that an applicant is more likely to repay the loan and thus be approved and pay a lower interest rate for new credit.

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To learn more about credit scores, go to https://www.myfico.com/credit-education/credit-scores.

Qualifying Ratios. Lenders qualify applicants for a mortgage loan by reviewing how much debt the applicant has in relation to how much income the applicant earns. Lenders review the applicant's total monthly expenses in relation to the applicant's monthly gross income to determine what is called qualifying ratios. Qualifying ratios are important because borrowers who have high debt compared to gross income may run into trouble paying the mortgage payments if something unexpected should occur. Qualifying ratios will be discussed in detail later in this unit.

Qualifying the Property. The lender orders a property appraisal of the property that will be pledged as collateral for the loan. The appraiser estimates the property's value and, in the case of FHA and VA, determines if the overall condition of the structure meets the required minimum standards (FHA and VA mortgage loans are discussed in detail later in this unit).

Preapproval and Prequalification. Prequalifying is less formal. The lender asks the borrower questions concerning income and debt; however, a credit report is not pulled. Preapproval, however, is more detailed. The lender runs a credit report and verifies income and assets. The application is submitted for preliminary underwriting, and the prospective borrower is provided with a *preapproval letter* that defines the loan amount the buyer is approved to receive. Approval letters are usually valid for 120 days.

13.2 CONVENTIONAL VS. NONCONVENTIONAL MORTGAGE LOANS

Mortgage loans can be grouped into two general categories.

1. **Conventional loans** carry no government guarantee or government insurance for the lender if the borrower fails to repay the loan. The lender assumes the full risk of default in a conventional loan. To offset the lender's risk, borrowers are sometimes required to purchase insurance to protect the lender against the borrower's default. Qualifying for a conventional loan is generally more difficult than qualifying for a loan that is guaranteed or insured by a government agency.
2. **Nonconventional loans** are backed by the federal government. Nonconventional loans include FHA-insured and VA-guaranteed loans. Nonconventional loans offer more flexible options for borrowers.

Conventional Mortgage Loan Features

Interest Rate. Private lenders make conventional mortgage loans. Interest rates for conventional mortgages reflect market conditions and are negotiated between the lender and the borrower.

Assumption. Fixed-rate conventional loans include a due-on-sale clause that requires the loan balance to be paid in full when the property is sold, thereby preventing another person from assuming the mortgage loan. Adjustable-rate conventional loans are assumable (see "Adjustable-Rate Mortgage," in this unit).

Prepayment. Fixed-rate conventional mortgage loans contain a prepayment clause that allows borrowers to prepay the mortgage principal (see "Prepayment Clause," Unit 12).

Down Payment and Private Mortgage Insurance. Conventional loans typically require the borrower to make a larger down payment (equity) as compared with nonconventional loans. However, borrowers can make smaller down payments. **Private mortgage insurance (PMI)** is required for conventional loans that finance more than 80% of the purchase price. In other words, if the borrower makes a down payment of less than 20% of the purchase price, PMI is required. Private mortgage insurance protects lenders in case the borrower defaults.

Loan-to-Value Ratio. Recall that the loan-to-value (LTV) ratio is a financial term used by lenders to describe the ratio between the mortgage loan amount and the property's value. To calculate LTV, divide the loan amount by the property's purchase price (or the appraised value if it is less than the purchase price). As part of the lender's underwriting process, it will require that the borrower comply with a particular LTV.

The LTV ratio is also used to determine whether the borrower will have to purchase PMI. PMI is required if the LTV ratio is greater than 80%. The portion of the loan that exceeds 80% of the property's sale price (or appraised value) is insured with PMI. If the borrower defaults and the proceeds from the foreclosure sale are not sufficient to cover the amount that is due the lender, the mortgage insurance covers the difference. The borrower can request the PMI coverage to be cancelled once the outstanding balance of the mortgage drops to 80% of the original value of the home (.80 or 80% LTV).

Qualifying for a Conventional Mortgage Loan

Conventional loans have more stringent qualifying requirements compared with nonconventional loans. To qualify for a conventional loan, the borrower must have a good to excellent credit score and meet certain income requirements, work history, down payment, and qualifying ratios. These qualifying requirements are established by Fannie Mae and Freddie Mac guidelines (Fannie Mae and Freddie Mac are explained in detail later in this unit).

Qualifying Ratios. Lenders consider two qualifying ratios when borrowers apply for a conventional mortgage.

1. The **housing expense ratio (HER)** is calculated by taking the borrower's expected monthly housing expenses divided by monthly gross income. Housing expenses include principal, interest, property taxes, and hazard insurance (PITI) plus the monthly private mortgage insurance premium (PMI) for mortgage loans greater than 80% LTV. Homeowners association fees, condominium fees, and flood insurance, if applicable, are also considered housing expenses (see the following formula). The recommended HER for a conventional mortgage loan is 28%.

Formula: Housing Expense Ratio (HER)

monthly PITI + PMI ÷ monthly gross income = HER

2. The **total obligations ratio (TOR)** is a measure of a borrower's total monthly installment debt divided by monthly gross income. Monthly installment debt includes the expenses that appear on the borrower's credit report, such as credit card payments, auto payments, student loan payments, and child support payments, referred to as long-term obligations (LTO). The monthly installment debt also includes the monthly housing expense used in the HER (see the following formula). The recommended TOR for a conventional mortgage is 36%.

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Formula: Total Obligations Ratio (TOR)

(PITI + PMI + LTO) ÷ monthly gross income = TOR

EXAMPLE: A couple has a combined monthly gross income of $6,737, a monthly mortgage payment of $1,420, a PMI premium of $96, and additional monthly obligations including the following:

- Car payment: $460
- Student loan: $200
- Credit card: $150

a. What is the couple's housing expense ratio?
b. What is the couple's total obligations ratio?
c. Does the couple qualify for a conventional mortgage?

Solution:

a. To determine the couple's HER, determine the total monthly housing expenses:
$1,420 PITI + $96 PMI = $1,516 total monthly housing expense
Next, divide the total monthly housing expenses by the monthly gross income:
$1,516 ÷ $6,737 monthly gross income = .2250 or 22.5% HER

b. To determine the couple's TOR, determine the total monthly obligations:
PITI + PMI + LTO = $1,516 + $460 car + $200 loan + $150 credit = $2,326
Next, divide the total monthly obligations by the monthly gross income:
$2,326 total monthly obligations ÷ $6,737 = .3452 or 34.5%

c. To qualify for a conventional mortgage loan, the borrower must have an HER that does not exceed 28%. The borrower's HER is 22.5%. So, 22.5% of the borrower's monthly gross income pays the borrower's monthly housing expenses. The borrower's HER is below the required threshold. The borrower meets the HER ratio requirement for a conventional mortgage.
To qualify for a conventional mortgage loan, the borrower's TOR must not exceed 36%. The borrower's TOR is 34.5%, which is less than 36%. The borrower meets the TOR ratio requirement for a conventional mortgage.

Practice Questions

1. ______________ loans are NOT insured or guaranteed by a government agency.
2. The total obligations ratio for a conventional mortgage loan may NOT exceed ______________.
3. A borrower has a combined monthly gross income of $5,900, PITI of $1,500, monthly PMI premium of $95, and additional monthly obligations including the following:
   - Car payment: $260

- Student loan: $186
- Credit card: $260

a. What is the borrower's housing expense ratio?

b. What is the buyer's total obligations ratio?

c. Does the buyer qualify for a conventional mortgage?

13.3 COMMON TYPES OF MORTGAGES

The two most common types of conventional mortgage loans are fixed-rate amortized mortgage loans and adjustable-rate mortgage loans. The interest rate of a *fixed-rate* conventional mortgage loan is determined at the time that the loan is originated and does not change over the entire loan period, referred to as the *loan term*. With an *adjustable-rate* mortgage, the interest rate may go up or down during the loan term.

Amortized Mortgage

A fixed-rate **amortized mortgage** consists of a series of fixed, equal monthly payments over the loan *term*. Typical mortgage loan terms are 15-year and 30-year terms. At the end of the loan term, the loan is completely paid off. For example, a loan with a 30-year term will be paid in full in exactly 30 years (360 monthly payments). The monthly payments are constant (same monthly payment) each month for the loan term. Fixed-rate amortized mortgages are sometimes referred to as **level-payment plan** mortgages because the borrower pays the same mortgage payment each month.

Mortgage Amortization Table. An *amortization table* is a spreadsheet that lists each monthly payment for the entire loan term. An amortization schedule allocates each monthly payment into two components:

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1. Interest paid. A portion of each monthly payment is applied to interest. Interest is the amount lender gets paid for making the loan to the borrower. The amount of the mortgage payment allocated to interest in the largest portion of the monthly payment in the early years of the loan term.
2. Principal paid. After the interest charges are allocated, the remainder of the monthly payment is applied to paying off the loan. This portion of the monthly payment is called **principal**. As the loan balance is gradually paid off, the amount allocated to interest gradually decreases, and the amount allocated to principal gradually increases.

The two components of the monthly mortgage payment, principal and interest, are referred to as PI. Recall from Unit 12 that, typically, borrowers also pay the property taxes and hazard insurance premiums as part of their monthly mortgage expense (PITI). One-twelfth of the annual property taxes and hazard insurance are added to the borrower's monthly payment. However, because these expenses are not part of the loan repayment, they are not included in the amortization table.

Amortization tables can be easily created from programmed software. There are three figures that must be inserted into the formula to create an amortization table:

- Loan amount

- Interest rate
- Loan term

Once these values are entered, the monthly PI payment and the amount applied to interest and principal is automatically calculated in the table. Portions of an amortization table for a $200,000 mortgage loan at 4% interest with a 30-year term are presented in Figure 13.1.

FIGURE 13.1 ■ Portions of an Amortization Schedule

Month	Monthly PI Payment	Interest Paid	Principal Paid	Balance
1	$954.83	$666.67	$288.16	$199,711.84
2	$954.83	$665.71	$289.12	$199,422.71
3	$954.83	$664.74	$290.09	$199,132.62
4	$954.83	$663.78	$291.06	$198,841.57
5	$954.83	$662.81	$292.03	$198,549.54
6	$954.83	$661.83	$293.00	$198,256.54
355	$954.83	$18.88	$935.95	$4,726.78
356	$954.83	$15.76	$939.07	$3,787.71
357	$954.83	$12.63	$942.20	$2,845.50
358	$954.83	$9.49	$945.35	$1,900.16
359	$954.83	$6.33	$948.50	$951.66
360	$954.83	$3.17	$948.49	$0.00

The first six monthly payments and the last 6 monthly payments are shown in Figure 13.1. The principal and interest payment (PI) is $954.83 every month for 360 payments. In months one through six, the amount allocated to interest is greater than the amount applied to principal reduction. However, in the last six months of the loan term, most of the monthly payments reduce principal and very little is applied to interest. The reduced amount allocated to interest is because most of the loan balance has been paid off in the last months of the loan term. In month 360 (12 monthly payments × 30-year term), the entire debt is paid in full.

Adjustable-Rate Mortgage

Unlike a **fixed-rate mortgage** that has an interest rate (and monthly payment) that does not change for the entire loan term, an **adjustable-rate mortgage (ARM)** is a loan that has an interest rate that can change at preset intervals, based on a predetermined index. Typically, ARMs feature an initial fixed-rate period for the first three to 10 years. The interest rate then may adjust each year thereafter once the initial fixed period ends. For example, a 5/1 ARM is a 30-year term loan. The first five years of the loan feature a fixed interest rate. Thereafter, the interest rate can adjust each year up or down based on the index. 3/1 ARMs and 5/1 ARMs often provide the lowest interest rates and monthly payments during the first three or five years, respectively. This type of loan can be advantageous for growing families who intend to move to a larger home in a few years. Also, conventional ARM loans do not have a due-on-sale clause and therefore are assumable. ARMs aren't for everyone. Many borrowers want the security of knowing that their interest rate (and their monthly mortgage payments) will remain the same for the entire loan term. ARMs also tend to be more popular when fixed-rate interest rates are high as borrowers are hoping to refinance their ARMs when fixed interest rates decline. The primary components of adjustable-rate mortgages are as follows.

Index. The **index** is an economic indicator that is used to adjust the interest rate in the loan. Lenders legally are allowed to link the interest rate of an ARM with any recognized index. Many indexes are tied to U.S. Treasury securities. The index moves up and down with fluctuations in the nation's economy. The index must not be controlled by the lender, and it must be verifiable by the borrower.

Margin. The **margin** (or *spread*) is the percentage added to the index. The margin represents the lender's cost of doing business plus profit. The margin percentage remains constant over the life of the loan.

Calculated Interest Rate. The calculated interest rate is arrived at by adding the index to the lender's margin.

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Formula: Calculated Interest Rate

index + margin = calculated interest rate

EXAMPLE: Assume the borrower has an ARM tied to the one-year T-bill rate with a margin of 2.25. If the T-bill rate is 4%, the calculated interest rate is:

4% index + 2.25% margin = 6.25% calculated interest rate

Adjustment Interval. The interest rate on an ARM adjusts periodically based on the adjustment interval established in the mortgage loan documents. Some ARMs adjust annually based on the index. A hybrid ARM allows the borrower to lock in a fixed rate for a longer time than the usual one year before the adjustments begin. With a 5/1 hybrid, for example, the initial interest rate is fixed for the first five years and then beginning with year 6, the rate adjusts annually (pegged to the index) for the remaining term of the loan.

Interest Rate Caps. ARMs typically include rate caps to limit how much the interest rate may change per adjustment. Most ARMs have two types of rate caps—periodic cap and lifetime cap. A **periodic cap** limits the amount the interest rate may increase at any one time, usually a year. For example, the interest rate may be capped to not increase more than 2% during an annual adjustment interval. ARMs typically also feature a **lifetime cap** that caps the total amount the interest rate may increase over the life of the loan. For example, the loan might have a lifetime cap or ceiling of 6% over the life of the loan.

Payment Cap. A **payment cap** limits the amount the monthly payments can increase during any adjustment. The purpose of a payment cap is to protect the mortgagor from unaffordable high monthly payments. If interest rates rise sharply but the payments do not because of a payment cap, the unpaid interest is added to the loan balance. **Negative amortization** occurs when the mortgage payments are not large enough to cover the interest expense. The result is the mortgage loan balance increases (instead of decreasing). Negative amortization can result in a mortgagor owing the mortgagee more than the house is worth.

Teaser Rate. Sometimes a lender will offer borrowers an initial below-market interest rate called a **teaser rate**. The low rate is usually offered for the first year of the loan, with a sharp annual rate increase at the next rate-adjustment period to bring the loan in line with the agreed-upon index.

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The Federal Reserve Board's Consumer Handbook on Adjustable-Rate Mortgages is available at https://files.consumerfinance.gov/f/documents/cfpb_charm_booklet.pdf.

Practice Questions

4. In a fixed-rate amortized loan, the portion applied to principal gradually _______________ each month and the portion applied to interest gradually _______________ each month.

5. Another name for a fixed-rate amortized mortgage is a ____________________ __________ mortgage.

6. An economic indicator used to adjust the interest rate on an ARM is called an _______________.

7. A mortgagee's costs of doing business plus profit is called the _______________.

8. The _____________ ________ limits the amount the interest rate may change at each adjustment interval.

9. If the monthly payment on the ARM is smaller than what is required to pay the principal and interest for the period, it will result in ____________ _______________.

13.4 GOVERNMENT-INSURED FHA PROGRAM

Recall that nonconventional loans are backed by the federal government. Nonconventional loans include FHA-insured loans.

Purpose of the FHA

The Federal Housing Administration (FHA) was created in 1934. The FHA is a government agency within the Department of Housing and Urban Development (HUD). Its mission is to stimulate homeownership. FHA loans are fully insured by the government to help increase the availability of affordable housing in the United States.

FHA loans are made by FHA-approved lenders. Lenders must meet certain criteria for their loans to be FHA-approved, after which the FHA insures the loans the lender issues against losses in the event that borrowers default on the loans. FHA loans protect lenders from financial risk. The cost of the mortgage insurance is paid by the borrower. The FHA does not make loans to borrowers, process loans, or build housing.

FHA loans are a good option for first-time homebuyers or for buyers who have challenges dealing with the more stringent requirements of conventional financing because they require a 3.5% down payment and have less stringent credit score requirements and other qualifying criteria compared with conventional loans. There are many types of FHA loan programs; however, the most popular loan program is a Section 203(b) loan, which is a fixed-rate mortgage loan for the purchase or construction of one- to four-family residential property. FHA-insured loan programs also are available for adjustable-rate mortgages and loans to finance the purchase of a condominium unit in condominium communities built to FHA standards. FHA-insured mortgage loans require that the borrower will use the home as a primary residence for at least the first year of ownership.

FHA Mortgage Loan Features

Interest Rate. The interest rate on FHA mortgages is not set by the FHA or HUD. The interest rate is allowed to fluctuate with the market and is negotiable between the lender and the borrower.

Discount Points. FHA-approved lenders may charge discount points on FHA-insured mortgage loans. Discount points may be paid by either the seller or the buyer (see "Discount Points," Unit 12).

Assumption. FHA mortgage loans do not have a due-on-sale clause in the mortgage. The FHA requires complete qualification of the buyer assuming the loan. All assumed loans (and new FHA loans) are for owner-occupied use only (no investor loans). The lender must release the original mortgagor from liability if the assuming mortgagor is found creditworthy and executes an agreement to assume and pay the mortgage debt. By law, FHA loans cannot charge prepayment penalties; the loan may be paid off early without penalty.

Down Payment. A major benefit of FHA-insured loans is that the down payment is much smaller than the amount required for most conventional mortgage loans. A borrower can obtain an FHA-insured loan with a down payment as low as 3.5% of the purchase price or the appraised value, whichever is less. FHA refers to the required down payment as the *minimum cash investment.* Closing costs may not be used to meet the minimum 3.5% down payment requirement. Borrowers must have a good credit history to qualify for maximum financing.

Loan Limit. Recall that FHA loans are a type of nonconventional loan because they are insured by the FHA. FHA sets limits on the amount that can be borrowed. The limits vary significantly, depending on the average cost of housing in different regions of the country. For example, the maximum FHA loan for a one-unit residence is greater in Fort Lauderdale and Miami than in Gainesville or Tallahassee because the average cost of housing is greater in the Fort Lauderdale and Miami markets. Lenders make FHA-insured loans in even $50 increments.

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A schedule of FHA mortgage limits by area is available at https://entp.hud.gov/idapp/html/hicostlook.cfm.

Loan Insurance Premium. FHA loans require two types of mortgage insurance. Borrowers are charged a one-time mortgage insurance fee at closing. This fee is called the **upfront mortgage insurance premium (UFMIP)**. The percentage of the UFMIP is based on the type (new or refinance) and term (15-year or 30-year) of the mortgage. The UFMIP is paid at closing and can be financed into the mortgage amount.

In addition to the UFMIP, the borrower is also charged an annual **mortgage insurance premium (MIP)**. The annual MIP is paid monthly (annual premium divided by 12) as part of the monthly mortgage payment. The MIP must be included in the proposed monthly expenses when calculating the buyer's qualifying ratios. The monthly MIP is paid for the life of the FHA loan when the borrower receives maximum financing. UFMIP and MIP go into an FHA fund for repaying lenders if borrowers default.

Qualifying Ratios. FHA lenders use two qualifying ratios for loan applicants. FHA requirements currently allow up to 31% for the housing expense ratio (HER) and up to 43% for the total obligations ratio (TOR).

EXAMPLE: A prospective borrower is applying for an FHA-insured loan. The borrower's gross monthly income is $3,500. The borrower's projected monthly PITI is $900, the MIP is $150, and based on a credit report, the borrower has the following long-term obligations:

- Car payment: $200
- Student loan: $150
  a. What is the borrower's housing expense ratio?
  b. What is the borrower's total obligations ratio?
  c. Does the borrower qualify for an FHA mortgage?

  Solution:
  a. To determine the borrower's HER, determine the total monthly housing expenses:
  $900 PITI + $150 MIP = $1,050 total monthly housing expense
  Next, divide the total monthly housing expenses by the monthly gross income.
  $1,050 ÷ $3,500 = .30 or 30% HER
  b. To determine the borrower's TOR, determine the total monthly obligations:
  PITI + MIP + LTO = $900 PITI + $150 MIP + $200 car + $150 loan = $1,400
  Next, divide the total monthly obligations by the monthly gross income:
  $1,400 ÷ $3,500 = .40 or 40%
  c. To qualify for an FHA-insured mortgage loan, the borrower must have an HER that does not exceed 31%. The borrower's HER is 30%. So, 30% of the borrower's monthly gross income pays the borrower's monthly housing expenses. The borrower's HER is below the required threshold.
  To qualify for an FHA-insured mortgage loan, the borrower's TOR must not exceed 43%. The borrower's TOR is 40%, which is less than the required threshold of 43%.

Appraisal. The home must be appraised by an FHA-approved appraiser. HUD requires the appraiser to confirm that the property meets HUD's minimum property standards. However, the FHA does not warrant the condition of the property. The FHA encourages buyers to have a home inspection conducted.

Insured Commitment. A developer will sometimes seek an FHA commitment to insure the mortgages on a planned project. The FHA gives a conditional commitment to insure the mortgage loans on the individual homes in the planned project that is dependent on the structures being completed according to verified FHA standards.

Practice Questions

10. List the two types of mortgage insurance charged on FHA mortgage loans.
    1. ______________________________
    2. ______________________________

11. List the two qualifying ratios used for FHA mortgage loans and their standard qualifying threshold.
    1. ______________________________
    2. ______________________________

12. An FHA borrower has monthly PITI of $2,276, MIP of $160, a car payment of $479, a revolving credit card minimum monthly payment of $165 per month, and a student loan of $200 per month. The borrower's gross monthly income is $8,000.

    a. What is the borrower's HER?

    b. What is the borrower's TOR?

    c. Does the borrower's financial ratios qualify for an FHA mortgage loan?

13.5 VA LOAN GUARANTEE PROGRAM

Recall that nonconventional loans are backed by the federal government. Nonconventional loans include VA-guaranteed loans.

A VA loan is a mortgage loan program established by the U.S. Department of Veterans Affairs (VA). VA loans assist service members, veterans, and eligible surviving spouses to become homeowners. The VA issues rules and regulations that set the qualifications and conditions for VA loans. The VA guarantees a portion of the loan referred to as a *partial guarantee*. The partial guarantee covers the top portion of the loan. VA home loans are provided by private lenders, such as banks and mortgage companies. The applicant must plan to use the home as a primary residence.

A major benefit of a VA purchase loan is that the VA does not require a down payment. However, a lender may require a down payment if the appraised value of the home is less than the sale price. Nearly 90% of all VA-guaranteed home loans are made with no down payment. The VA loan guarantee differs from the FHA program that insures loans; VA home loans do not charge a mortgage insurance premium.

VA Mortgage Loan Features

Qualifications for Program. Only veterans, unremarried surviving spouses of veterans, and active military personnel may apply for a VA loan.

Eligibility Requirements. Specific eligibility requirements are based on the period of active duty or the period of continuous service, as applicable. Real estate licensees should rely on a VA lender to determine an applicant's eligibility for a VA loan.

Lending Source and Eligible Property. VA loans are made by VA-approved lenders. However, the VA does have the power to make direct loans to veterans in areas where VA loans are not available. The VA loan program may be used to purchase, refinance, or construct one- to four-unit properties provided the veteran resides in one of the units. The lender, not the VA, sets the interest rate, discount points, and closing costs. The maximum loan term is 30 years. The interest rate on VA loans varies based on market conditions and is negotiated between the borrower and the lender.

Loan Guarantee and Entitlement. The VA establishes loan guarantee limits called the VA loan guarantee or the maximum entitlement. A veteran's **entitlement** is the maximum amount the government guarantees the lender will be paid in the event the borrower defaults. A veteran begins the loan process by applying to the VA for a certificate of eligibility. The *certificate of eligibility* states the amount of entitlement available to the veteran borrower.

Reusing Entitlement. A veteran who has used the entitlement in the past may only now be eligible for a portion of the entitlement. The unused portion is available to the veteran borrower up to the maximum guarantee. When a VA loan is paid off, the veteran's maximum entitlement is reinstated.

Loan Limits. The VA previously used Fannie Mae and Freddie Mac loan limits as the maximum guaranteed loan amount without a required down payment. Effective January 1, 2020, VA loan limits were eliminated for borrowers who have their full entitlement. The removal of loan limits does not mean that veterans have unlimited borrowing power without a down payment. The VA borrower must have sufficient income and meet the lender's credit requirements to qualify for the loan. Eligible military members and veterans can now use the loan amount they qualify for without making a down payment. This is good news for borrowers in high-priced parts of the country. Qualifying VA applicants can avoid significant out-of-pocket expense for a down payment under the new regulation (other closing costs still apply).

Down payments still apply to veterans who have one or more existing VA loans or have defaulted on a prior VA loan. VA borrowers are subject to the loan limits and will be required to make a down payment of 25% of the difference between the purchase price and the loan limit.

Loan Origination Fee. The VA borrower pays a loan origination fee to the lender. The VA allows a 1% origination fee to be charged to veteran borrowers.

VA Funding Fee. The veteran borrower pays a *funding fee* to the VA. The VA loan funding fee is on a sliding scale, with the lowest fees charged to first-time VA borrowers and higher fees for those VA borrowers who have previously used the VA loan program. Funding fee expenses may be added to the loan amount and financed over the life of the loan. If a veteran is a purple heart recipient or has a service-connected disability, the funding fee is waived. VA loans do not require mortgage insurance premiums (MIP).

Qualifying Ratio. To qualify loan applicants, the VA guidelines recommend a total obligations ratio (TOR) not to exceed 41% of the total monthly gross income (see Figure 13.2).

FIGURE 13.2 ■ **Comparison of Qualifying Ratios**

	Housing Expense Ratio (HER)	Total Obligations Ratio (TOR)
Conventional	28%	36%
FHA	31%	43%
VA		41%

Closing Costs. The lender may charge reasonable closing costs. The VA appraisal, credit report, state and local taxes, and recording fees may be paid by the purchaser, the seller, or shared. No commissions, brokerage fees, or buyer-broker fees may be charged to the veteran buyer.

Assumption. Because VA loans do not have a due-on-sale clause, they are assumable (even by nonveterans). Before assuming a VA mortgage loan, the buyer must be approved by the lender and the VA. The VA must also approve the assumption agreement. Processing fees and funding fees are charged on assumptions. Sellers who allow nonveterans to assume their VA loans will not have their VA eligibility restored until the assumer has paid off the VA loan, unless the assumer is also a veteran who agrees to substitute eligibility.

Prepayment. VA mortgage loans do not contain a prepayment penalty clause. Therefore, veterans may prepay all or a portion of the mortgage loan ahead of schedule without penalty. Figure 13.3 provides a comparison of FHA and VA mortgage loans.

FIGURE 13.3 ■ **FHA and VA Comparison**

	FHA Loan	VA Loan
Role of government	Fully government insured; does not originate loans	Partial government guarantee; can make direct loans if needed
Down payment	3.5% minimum investment	0%
Fees	UFMIP and MIP	Funding fee
Loan limit	Set by area	No established loan limit
Assumable	Yes	Yes
Due-on-sale clause	No	No

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Visit the U.S. Department of Veterans Affairs Home Loan Guaranty program online at https://www.benefits.va.gov/homeloans/.

For additional information on VA loan limits go to https://www.va.gov/housing-assistance/home-loans/loan-limits/.

Practice Questions

13. A VA mortgage loan borrower's total obligations ratio (TOR) cannot exceed ______________.

14. The VA mortgage loan borrower pays a ________ ______________ fee to the lender and a ______________ fee to the VA.

13.6 PURPOSE-SPECIFIC MORTGAGE PRODUCTS

Biweekly Mortgage Loan

A **biweekly mortgage** loan is amortized the same way as fully amortized mortgage loans, except the borrower makes a payment every two weeks. The amount paid is equal to one-half the normal monthly payment. Because there are 52 weeks in the year, the borrower makes 26 biweekly payments. Therefore, the borrower makes the equivalent of an extra month's payment each year (26 half-size payments equal 13 full-month payments instead of 12). This saves the borrower considerable interest, and the loan is paid off sooner (see Figure 13.4).

FIGURE 13.4 ■ Purpose-Specific Mortgage Products

Type of Mortgage Loan	Description
Biweekly mortgage loan	26 payments per year
Partially amortized loan	Final balloon payment with monthly payments calculated as if the payments will be paid over a longer term
Purchase money mortgage (PMM)	Owner financing typically used to fill the gap between down payment and first mortgage
Home equity loan	Secured by primary residence and is usually a second mortgage
Package mortgage loan	Pledge both real and personal property as collateral
Reverse mortgage (HECM)	Uses homeowner's equity to provide monthly income for owners 62 and older

Partially Amortized Mortgage Loan

Recall that an amortized mortgage consists of a series of fixed, equal monthly payments and at the end of the loan term the loan is completely paid off. With a **partially amortized mortgage** (also called a balloon mortgage), the monthly payments are calculated for a 20-year or 30-year loan term; however, the payments are paid for a shorter period of time, such as five years. By amortizing the loan over 20 or 30 years, the fixed, monthly payments are smaller than if the loan were amortized over a five-year term. At the end of the stipulated period (in this example, five years), the remaining unpaid loan balance is due. A single large final payment (called a **balloon payment**) becomes due on the loan maturity date. In Florida, a partially amortized mortgage must be clearly identified as such on the face of the mortgage, with the amount of the final balloon payment disclosed (see Figure 13.4).

Purchase Money Mortgage (PMM)

A **purchase money mortgage (PMM)** is a mortgage in which payments are made to the seller (seller financing) rather than to a lending institution. It is typically used in lieu of a portion of a buyer's down payment when the buyer assumes an existing mortgage. The seller conveys legal title to the buyer at closing, and the seller retains a vendor's lien right as security for the debt.

EXAMPLE: The purchase price of a home is $200,000. The buyer is assuming the seller's FHA mortgage loan with an unpaid balance of $120,000.

$200,000 purchase price – $120,000 = $80,000 cash due at closing

The buyer asks the seller to accept $30,000 cash at closing and the remaining amount due to be paid to the seller over five years. The buyer is asking the seller to take back a purchase money mortgage at a specified interest rate and loan term in lieu of $50,000 cash at closing. This may be a good arrangement for both the buyer who does not have sufficient savings available for the entire amount of cash due at closing and the seller who can receive an income stream over time at a favorable interest rate. The buyer will sign a note and a mortgage with the seller. The assumed FHA mortgage was recorded as a first mortgage, so the PMM will be recorded as a second mortgage.

Home Equity Loan

Homeowners use **home equity loans** to finance consumer purchases; consolidate existing credit card debt; and pay for college tuition, medical expenses, or home improvements. If the home equity loan is used to make home improvements, the interest is tax deductible (certain limits exist).

The borrower (homeowner) may access the equity in the residence with a home equity loan or a home equity line of credit (HELOC). A home equity loan is a lump sum one-time equity draw. Home equity loans feature a fixed interest rate and equal monthly payments for the loan's term. A HELOC is a line of credit against the equity in the home, and the borrower accesses money from the line of credit as needed. HELOCs feature an adjustable interest rate. Borrowers only pay interest on the actual amount of money accessed from the line of credit. The LTV of both mortgages combined is typically limited to 80% of the property's value (see Figure 13.4).

Home Equity Conversion Mortgage (HECM) or Reverse Mortgage Loan

Homeowners age 62 and older who have paid off their mortgage or have only a small mortgage balance remaining are eligible to participate in HUD's **reverse mortgage** program. The only reverse mortgage insured by the federal government is called a **home equity conversion mortgage (HECM)** and is only available through an FHA-approved lender. The program allows homeowners to borrow against the equity in their homes. Homeowners can receive payments in a lump sum, on a monthly basis (for a fixed term or for as long as they live in the home), or on an occasional basis as a line of credit. The size of reverse mortgage loans is determined by the borrower's age, the interest rate, and the home's value.

Unlike ordinary home equity loans, a HUD reverse mortgage does not require repayment as long as the borrower lives in the home. Lenders recover the principal and interest when the home is sold. The remaining value of the home goes to the homeowner or to the homeowner's heirs. If the sale proceeds are insufficient to pay the amount owed, HUD will pay the lender the amount of the shortfall. The Federal Housing Administration (FHA), which is part of HUD, collects an insurance premium from the borrower to provide this coverage (see Figure 13.4).

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The American Association of Retired Persons (AARP) offers comprehensive information about reverse mortgages at https://www.aarp.org/money/credit-loans-debt/reverse_mortgages/.

Package Mortgage Loan

A **package mortgage** loan includes both real and personal property as security for the debt. A buyer uses a package mortgage, for example, when purchasing a restaurant complete with cooking equipment and other personal property that serve as a part of the collateral for the debt (see Figure 13.4).

Practice Questions

15. The final large payment in a partially amortized mortgage loan is called a __________ __________.

16. A mortgage loan that pledges real and personal property as collateral is called a ______________ mortgage.

13.7 PRIMARY MORTGAGE MARKET

Depository Lenders

The **primary mortgage market** consists of lenders that originate new mortgage loans for borrowers. These lenders make money available directly to borrowers. Three major depository lenders originate mortgages (see Figure 13.5):

1. Savings associations (SAs) invest the bulk of assets in residential mortgages and home equity loans.
2. Commercial banks (CBs) specialize in construction loans for residential and commercial projects.
3. Credit unions (CUs) are nonprofit organizations that provide services to their members, providing financing for residential loans and home improvement loans.

SAs, CBs, and CUs are depository lenders, meaning that they accept savings deposits and **demand deposits** (checking accounts). These depository lenders are also called *portfolio lenders* because they can hold mortgage loans permanently in their portfolios.

EXAMPLE: A couple finances the purchase of their home by taking out a 30-year fixed-rate mortgage loan from their local credit union. The credit union is a portfolio lender because it will hold the mortgage and promissory note in its portfolio of investments.

The demand deposits and savings deposit accounts provide depository lenders with a relatively stable funding source. Lenders who accept deposits are called financial intermediaries because they make loans with the deposited funds. The flow of funds into deposits held by primary lenders, thereby increasing the mortgage money supply, is called **intermediation.**

FIGURE 13.5 ■ **Primary Mortgage Lenders**

Mortgage Lenders	Type of Primary Lender	Types of Loans Offered	Focus
Savings association	Depository	Prefer conventional residential and home equity loans Also offer FHA and VA	Historically, largest source of residential mortgage loans
Commercial banks	Depository	Conventional, FHA, and VA mortgage loans	Largest source of short-term commercial; construction loans
Credit unions	Depository	Conventional, FHA, and VA Home improvement loans	Largest source of short-term consumer loans Nonprofit organizations that offer loans to members only
Mortgage lenders	Non-depository	Residential and commercial mortgage loans	Primarily make FHA and VA loans

Nondepository Primary Lenders

Mortgage lenders are full-service mortgage companies that process, close, and sell the loans they originate. Mortgage lenders fund the loans they originate with either their own funds or borrowed capital. Mortgage lenders are non-depository primary lenders because they do not accept savings deposits and demand deposits. Mortgage lenders package loans they originate and sell them to institutional investors and to secondary-market participants. The principal activity of mortgage lenders is to originate and service loans for residential and income properties. They primarily make VA and FHA loans.

A **mortgage broker** license is required for an entity conducting loan originator activities through one or more licensed loan originators employed by the mortgage broker or as independent contractors to the mortgage broker. Mortgage brokers do not make loans. Instead, mortgage brokers arrange loans for prospective borrowers with various mortgage lenders. Mortgage brokers do not service loans.

A **mortgage loan originator (MLO)** is a person who holds a state MLO license for the purpose of soliciting mortgage loans, accepting mortgage loan applications, and negotiating the terms or conditions of new or existing mortgage loans on behalf of a borrower or a lender. MLOs process mortgage loan applications and negotiate the sale of existing mortgage loans to noninstitutional investors for compensation.

The Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act) sets minimum standards for licensing and registering of mortgage loan originators. The SAFE Act requires employees of commercial banks, savings associations, and credit unions that are regulated by a federal banking agency and who are engaged in residential mortgage loan origination, to register with the Nationwide Mortgage Licensing System (NMLS). Mortgage loan originators must submit fingerprints for a criminal background check.

Mortgage loan originators (MLOs) who are not employed by agency-regulated institutions are licensed by the states. Employees of mortgage lenders, including bank holding companies and their nonbank subsidiaries, who act as MLOs are subject to state licensure and state regulation, in addition to registration with the NMLS.

Practice Questions

17. List four major entities that originate mortgages.

    1. ______________________________

    2. ______________________________

    3. ______________________________

    4. ______________________________

18. The primary mortgage market is where loans are ______________.

19. Lenders that prefer to hold mortgages rather than sell them are called ______________ lenders.

20. The flow of funds into deposits held by primary lenders, increasing the mortgage money supply, is called ______________.

13.8 SECONDARY MORTGAGE MARKET

Most lenders do not hold a mortgage that it originated for the entire loan term. It is common for a borrower's loan to be sold to one of the major mortgage investors within a few months of closing the loan. The **secondary mortgage market** is an investor market that buys and sells existing mortgages. The existence of a secondary mortgage market allows lenders to have stable cash flow so that they can originate more new loans. The borrower will continue to make monthly payments to the lender that originated the loan if the lender continues to service the loan.

The secondary mortgage market accomplishes two important objectives:

1. *Circulates the mortgage money supply*. The secondary mortgage market helps lenders raise capital to make additional mortgage loans. Prior to the existence of the secondary market, portfolio lenders had to rely on deposits flowing into their financial institutions. However, when depositors chose instead to invest their savings in other types of investments, such as the stock and bond markets, **disintermediation** led to a shortage of mortgage funds. With a secondary mortgage market, in times of disintermediation, lenders can sell more of their loans and use the cash to originate new mortgage loans.
2. *Standardized loan requirements*. The key to an efficient secondary market was the creation of standardized loan instruments. Standardized mortgage loan documents, appraisal forms, closing disclosures, and promissory notes make it possible for secondary market participants to better evaluate the mortgage loan packages being sold.

Fannie Mae and Freddie Mac

Fannie Mae and Freddie Mac are not government agencies. They are known as government sponsored enterprises (GSEs). GSEs are publicly traded corporations that are sponsored by the U.S. government. Fannie Mae and Freddie Mac are regulated under the conservatorship authority of the Federal Housing and Finance Agency (FHFA). Fannie Mae and Freddie Mac operate in the secondary mortgage market. They purchase about two-thirds of all U.S. mortgages. Fannie and Freddie set guidelines for the types of loans they will purchase. Mortgages that meet Fannie and Freddie guidelines are called **conforming loans**. Conforming loans meet, or conform to, loan amount limits set by the FHFA. Loans sold to Fannie and Freddie also must be written on uniform forms approved by Fannie and Freddie, including loan applications, appraisals, and mortgage instruments, in addition to meeting specific qualifying guidelines.

Loans that are for a larger loan amount that exceed the conforming loan limits are referred to as **nonconforming loans** or *jumbo* loans. Because Fannie Mae and Freddie Mac do not purchase nonconforming loans, these loans are more difficult to sell as investments, and lenders often have to hold these loans for long periods of time.

Fannie and Freddie buy conforming loans from local lenders and package them into mortgage-backed securities (MBS). MBSs are created by bundling thousands of mortgage loans together. The MBSs are sold worldwide to investors, providing funds to the financial institutions to make new consumer loans.

Fannie Mae. Fannie Mae (sometimes referred to as the Federal National Mortgage Association and FNMA) was created by Congress in 1938. It created the secondary market as a way to stimulate the housing market after the Great Depression. Fannie Mae and Freddie

Mac's guidelines vary somewhat from each other; however, both Fannie and Freddie have strict guidelines for the loans that they will purchase. For example, Fannie and Freddie limit the size of the individual mortgage loans they will purchase called the *loan limit*. Loan limits are subject to change annually and vary depending on the property's location.

Today, Fannie Mae purchases primarily conforming conventional mortgages from large commercial banks. Fannie Mae can also purchase FHA loans and VA-guaranteed mortgage loans. It is the largest secondary market participant (see Figure 13.6).

FIGURE 13.6 ■ **Secondary Market**

Fannie Mae	Not a government agency Buys conventional conforming loans from large commercial banks Purchases some government-insured and government-guaranteed loans Packages loans into mortgage-back securities and sells to investors
Freddie Mac	Not a government agency Buys conventional conforming loans from small banks, credit unions, and savings associations Packages loans into mortgage-back securities and sells to investors
Ginnie Mae	Government corporation under HUD Does not buy loans from lenders Guarantor of government-insured and government-guaranteed loans Has the full faith and credit guarantee of the federal government

Freddie Mac. Freddie Mac (sometimes referred to as the Federal Home Loan Mortgage Corporation and FHLMC) was created by Congress in 1970. Freddie Mac was originally created to provide competition to Fannie Mae. The goal was to reduce borrower's financing costs by providing more competition and liquidity. Freddie Mac provides a secondary market for conforming conventional mortgage loans purchased from smaller banks, credit unions, and savings associations (formerly called savings and loans). The loans are then pooled together and sold to investors as MBSs. Like Fannie, Freddie Mac purchases mortgages that meet their underwriting and product standards, package the mortgage loans into securities, and sell the securities to investors on Wall Street.

Ginnie Mae

Ginnie Mae (also referred to as Government National Mortgage Association and GNMA) provides a secondary market exclusively for government-insured and government-guaranteed loans, including FHA, VA, Rural Development, and American Native Indian Housing loans. Ginnie Mae, unlike Fannie and Freddie, is a government corporation housed within the Department of Housing and Urban Development (HUD). Ginnie's purpose is to provide liquidity for low- to moderate-income homebuyers. Ginnie is the only secondary participant backed by the *full faith and credit guarantee* of the federal government.

Unlike Fannie and Freddie, Ginnie Mae does not participate in determining eligibility for loans. Ginnie exists to solely guarantee the security of federally insured loans and federally guaranteed loans. Ginnie, unlike Fannie and Freddie, does not purchase mortgage loans from lenders. Once a lender makes a government-insured or government-guaranteed loan commitment to buyers, the lender obtains a guarantee from Ginnie. The lender pools similar mortgages together and delivers the pool of loans to a securities dealer. Securities dealers sell the Ginnie Mae guaranteed MBSs to investors. The securities dealers advise Ginnie Mae of the sales. The lender that originated the loans continues to service the loans and forwards the payments to Ginnie Mae. Ginnie disburses payments to investors. Ginnie's guarantee means that it makes the disbursements even if the payments have not been received from the borrower.

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To learn more about the secondary mortgage market, visit these websites:

- Fannie Mae: www.fanniemae.com
- Ginnie Mae: www.ginniemae.gov
- Freddie Mac: www.freddiemac.com

Practice Questions

21. List the two important objectives of the secondary mortgage market.

    1. ______________________________

    2. ______________________________

22. ______________ ____________ is the only secondary participant backed by the full faith and credit guarantee of the federal government.

13.9 FEDERAL REGULATORY BODIES AND MORTGAGE FRAUD

Federal Reserve System

The Federal Reserve System, also known as the Federal Reserve or just the Fed, is the central bank of the United States. It was established by Congress in 1913 to provide the nation with a safer and more stable monetary system. The Fed consists of a seven-member Board of Governors and 12 Reserve Banks located in major cities across the nation. The members of the Board of Governors are appointed by the president and confirmed by the U.S. Senate.

Today, the Fed's duties include (1) conducting the nation's monetary policy, (2) supervising and regulating banking institutions and protecting the credit rights of consumers, and (3) maintaining the stability of the financial system. *Monetary policy* refers to the actions undertaken by the Fed to influence the availability and cost of money and credit to promote national economic goals. The Fed is charged with the responsibility for setting monetary policy.

The Fed also has regulatory and supervisory responsibilities over banks that are members of the Fed. Additionally, the Board is responsible for the development and administration of regulations that implement major federal laws governing consumer credit, such as the Truth in Lending Act and the Equal Credit Opportunity Act.

Using a Straw Buyer

A *straw buyer* is someone whose credit is used to purchase a property and secure financing but who isn't actually going to own the property. Straw buyers never intend to live on the property and only lend their credit information for a fee. At other times, the straw buyer is a victim of identity theft. The victim's credit profile is stolen and used as a straw buyer. The true buyer cannot qualify for the mortgage, so someone (a straw buyer with better credit) fraudulently applies for the mortgage. The true buyer is deceiving the lender for the purpose of getting a better loan than the buyer would be able to obtain if the loan application contained accurate financial information.

Recall the elements for fraud: (1) a misstatement of facts or failure to disclose facts; (2) the individual who made the misstatement or omitted the true facts knows the facts to be untrue; (3) the lender relied on the facts and extended financing; and (4) the lender was damaged as a result. In many cases, the loans were not repaid and the properties were foreclosed. In other cases, the loans were sold on the secondary market and packaged in security instruments valued on erroneous risk characteristics (see "Misrepresentation and Fraud," Unit 11).

No Documentation Loans

No documentation loans were very popular before the mortgage crisis. Unlike the stated income/stated asset loan application process, this type of loan program allowed a borrower with a certain minimum credit score to qualify for a mortgage without disclosing employment information, income, and assets. The lender approved the loan application without verifying the borrower's financial information. It was convenient for borrowers who qualified for the loans they applied for; however, other borrowers lied about their income and assets to qualify for mortgage loans that they would not otherwise be able to obtain. As a result, many homeowners found themselves with mortgages they could not repay.

Red Flags

Another type of **mortgage fraud** involves inflating the appraised value of property for the purpose of obtaining more financing. Unscrupulous appraisers altered or fabricated information and/or used inappropriate comparable sales. Some cases of fraud involved using fake photos of the property under contract to substantiate a higher value. In other situations, real estate licensees entered inaccurate data into the MLS database. The appraiser did not verify the information (as required) through another independent source. The appraiser and licensee working in tandem created huge financial losses for lending institutions. For example, if the MLS erroneously indicated that a house closed for $100,000 in a neighborhood where the most recent sale was only $80,000 and the next buyers coming into the neighborhood saw the inflated closed sale price and thought they must pay the inflated price, it would cause all future sale prices in the neighborhood to artificially increase. The inflated contract prices resulted from inflated appraisals. The dollar amount difference between the inflated sale price and the actual property value was the money used to compensate the fraudulent activity.

Licensees should be aware of red flags that might indicate fraudulent activity. For example, if a sale contract states "owner of record" rather than identify the seller's name, it should be a red flag to the selling real estate agent that a property flip might be occurring and to be aware of other irregularities. A property flip is a transaction in which one party contracts to buy a property with the intention of quickly transferring (flipping) the property over to the ultimate buyer. Another red flag is when a seller has taken title to the property via a recently recorded quitclaim deed. A prudent sales associate who sees potential red flags should immediately present such concerns to the employing broker for guidance on how to deal with the issue before going any further.

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Ethical Practices. Florida law stipulates that committing mortgage fraud is a third-degree felony. The mortgage fraud increases to a second-degree felony when the stated value in the loan documents exceeds $100,000. Charges of mortgage fraud can extend to the borrower, mortgage loan originator, and the real estate licensee. If a real estate licensee obtains information that the buyer is less than truthful regarding intent to occupy the property, assets, or income, it is very important that the real estate licensee speak up and not become a participant in the fraud.

Practice Questions

23. A _________ _________ is someone whose credit is used to purchase a property and secure financing, but who isn't actually going to own the property.

24. ______ _______________ loans allowed a borrower with a certain minimum credit score to qualify for a mortgage without disclosing employment information, income, and assets.

13.10 CONSUMER CREDIT PROTECTION ACT

The Consumer Credit Protection Act (CCPA) is an encompassing law that contains several acts with more precise scopes. Among the specific federal laws under the CCPA are the Equal Credit Opportunity Act and the Truth in Lending Act. Each of these laws will be discussed in detail in this unit.

Equal Credit Opportunity Act (ECOA)

The Equal Credit Opportunity Act (ECOA), implemented by Regulation B, applies to all consumer and commercial credit, without regard to the nature or type of the credit or the creditor. Congress gave the Consumer Financial Protection Bureau (CFPB) the authority to supervise and enforce compliance with ECOA. If a transaction provides for the deferral of the payment of a debt, it is a form of credit covered by Regulation B.

The ECOA prohibits creditors from discriminating against a Regulation B protected class in any aspect of a credit transaction. Financial institutions and firms engaged in extending credit must make credit available with fairness and without discrimination on the basis of race, color, religion, national origin, sex, marital status, age, or receipt of income from public assistance programs (see Figure 13.7).

FIGURE 13.7 ■ Summary of Protected Classes

Law	Race	Color	Religion	Sex	Disability	Familial Status	National Origin	Marital Status	Age	Public Assistance Income
Civil Rights Act 1866	✔									
Fair Housing Act (as amended)	✔	✔	✔	✔	✔	✔	✔			
Equal Credit Opportunity Act (Lending)	✔	✔	✔	✔			✔	✔	✔	✔

Marital Status. A lender cannot require an applicant's spouse to join in (sign) a loan application.

Source of Income. The ECOA prohibits discriminatory treatment of income from alimony, child support, public assistance, or part-time employment.

Childbearing Plans. The ECOA prohibits inquiry about, or consideration of, childbearing plans or the potential for child bearing.

The ECOA also requires creditors to provide applicants with free copies of appraisals or other written valuations developed because of a credit application secured by a first lien (for example, a first mortgage) on a dwelling. Creditors must notify applicants in writing that copies of appraisals will be provided to them.

Truth in Lending Act

The Truth in Lending Act (TILA) is a federal law designed to promote the informed use of consumer credit. The TILA regulates what information lenders must make known to consumers about their products and services. It requires disclosures about its terms and costs and standardized the manner in which costs associated with borrowing are calculated and disclosed.

The TILA outlines rules that apply to closed-end credit, such as home loans and auto loans. Closed-end credit is a loan or type of credit where the funds are disbursed in full at closing and must be repaid in full, including the interest and finance charges, by the end of the loan term. The TILA also outlines rules that apply to open-end credit, including credit cards and home equity lines of credit (HELOCs). The TILA does not put restrictions on how much interest they may charge or whether they must grant a loan. It does not attempt to regulate interest rates. The rules are designed to make it easier for consumers to comparison shop when the want to borrow money.

Regulation Z is often used as another name for the TILA. While the two names are often used interchangeably, they are not the same thing. The TILA was enacted by Congress and is a federal law. Regulation Z is a Federal Reserve Board rule that implements how the TILA is applied. The Dodd-Frank Reform Act transferred the rule-making authority from the Federal Reserve Board to the Consumer Financial Protection Bureau (CFPB).

Required Credit Costs Disclosures Under TILA. The TILA required lenders to provide a Truth in Lending disclosure (TIL) to borrowers who made loan application and a final TIL disclosure statement prior to the loan closing. A major accomplishment of the TILA was to establish the requirement to disclose the **annual percentage rate (APR)**. The APR presents the annual cost of credit expressed as a rate. TILA also required disclosure of other facts about the full cost of the credit, including the total cost of the loan, the amount financed, and the total of payments.

Bait-and-Switch Advertising. TILA makes *bait-and-switch* advertising a federal offense. For example, if a subdivision developer advertises homes for sale with a down payment of $1,000, the seller must accept $1,000 as the complete down payment or be in violation of the law.

Triggering Terms. TILA is also concerned that consumers may be misled by being given truthful but inadequate information in advertising. While it does not require creditors to advertise credit terms, it does provide that if they advertise certain credit terms, called **triggering terms**, they must include additional disclosures. Trigger terms include the following:

- amount or percentage of any down payment,
- number of payments,
- period (term) of repayment,
- amount of any payment, and
- amount of any finance charge.

Advertisements containing any of the triggering terms must also disclose the following:

- Amount or percentage of down payment
- Terms of repayment
- Annual percentage rate, using that term, and if the rate may be increased in the future, that fact must also be disclosed

TILA allows general phrases such as "owner will finance" and "favorable financing terms available." Such expressions are too general to trigger additional disclosure requirements.

Right of Rescission. Consumers who are refinancing residential mortgage loans have the right of rescission, which is a cooling-off period of three business days during which they may cancel the loan without losing any money. The right of rescission applies to most consumer loans but does not apply to loans to purchase or construct a home. The three-business-day right of rescission applies to:

- home equity lines of credit,
- second mortgages, and
- refinance loans.

Real Estate Settlement Procedures Act (RESPA)

The Real Estate Settlement Procedures Act (RESPA) is a federal law administered by the Consumer Financial Protection Bureau (CFPB) and implemented by Regulation X. The law is designed to ensure that borrowers are informed regarding the amount and type of charges they will pay at closing. RESPA requires the lender to disclose to the borrower an advance estimate of closing costs and an information booklet. RESPA also attempts to eliminate kickbacks from vendors of closing-related service providers. The act applies to most closings that involve a "standard" home mortgage loan. Specifically, RESPA applies to closings where a federally related mortgage loan is secured by a one- to four-family residence.

Affiliated Business Relationships. Sometimes, several businesses that offer settlement (closing) services are owned or controlled by a common corporate parent. These businesses are called *affiliates*. When a lender, real estate broker, or other closing participant refers a borrower to an affiliate for a settlement service (for example, when a real estate broker refers a buyer to a mortgage broker affiliate), RESPA requires the referring party to give the borrower an affiliated business arrangement (AfBA) disclosure. This form explains to borrowers that they are not required, with certain exceptions, to use the affiliate and are free to shop for other providers. The AfBA must include an estimate of the affiliated business provider's charges. Except in cases where a lender refers a borrower to an attorney, credit reporting agency, or real estate appraiser to represent the lender's interest in the transaction, the referring party may not require the consumer to use the affiliated business.

Purchase of Title Insurance. RESPA prohibits a seller from requiring the homebuyer to use a particular title insurance company as a condition of sale. Generally, the lender will require title insurance. The borrower can shop for and choose a company. However, if the seller is paying for the owner's title insurance policy, the law does not prohibit the seller from choosing the title company.

Escrow for Taxes and Insurance. RESPA limits the amount that lenders can require borrowers to place in escrow for property taxes and hazard insurance. The lender must perform an annual escrow account analysis. An excess of $50 or more must be returned to the borrower.

Kickbacks, Fee-Splitting, and Unearned Fees. It is illegal under RESPA for anyone to pay or receive a fee, kickback, or anything of value in exchange for referring a settlement service business to a particular person or organization. For example, a mortgage lender may not pay a real estate broker a fee for referring a buyer to the lender. It is also illegal for anyone to accept a fee or part of a fee for services if that person has not actually performed settlement services for the fee. For example, a lender may not add to a third party's fee, such as an appraisal fee, and keep the difference. RESPA does not prevent title companies, mortgage loan originators, appraisers, attorneys, closing agents, and others who actually perform a service in connection with the mortgage loan or the closing from being paid for the reasonable value of their work.

It is a crime for someone to pay or receive an illegal referral fee. The penalty can be a fine, imprisonment, or both. The borrower may also be entitled to recover, by bringing a private lawsuit, three times the cost of charges for settlement services (also called triple or treble damages) that were illegally referred or charged with no actual service provided.

TILA-RESPA Integrated Disclosure Rule (TRID)

Over time, TILA and RESPA regulations were expanded to require four separate disclosures when a borrower sought a mortgage loan. Much of the information in the four disclosures was repetitive and confusing to borrowers. Therefore, in 2015, Congress directed the Consumer Financial Protection Bureau (CFPB) to publish an integrated disclosure for mortgage transactions, called the TILA-RESPA Integrated Disclosure rule (TRID). Under the new TRID rule, the mortgage disclosure requirements under the Truth in Lending Act and RESPA were condensed into two disclosure forms. The borrower receives a loan estimate disclosure form shortly after applying for a loan, and a closing disclosure is received shortly before closing (see Figure 13.8).

FIGURE 13.8 ■ Disclosure Documents Timing

TRID RULE

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Document	Timing Requirement
Loan Estimate	Delivered or placed in the mail no later than the third business day after receiving the borrower's loan application.
Closing Disclosure	Provided to the borrower at least three business days before the loan closing.

TRID applies to consumer loans secured by real property, including refinance loans. Most closed-end consumer mortgage loans to finance home construction secured by real property are also covered by TRID. Figure 13.9 features a list of the types of loans for which TRID rules apply and a list of TRID Exemptions.

FIGURE 13.9 ■ TRID Transactions and Exemptions

TRID Applies	TRID Exemptions
Consumer loans secured by real property	Commercial loans for building more than four units
Mortgage loans	Reverse mortgages
Refinance loans	Home equity line of credit (HELOCs)
Construction loans	Mobile home loans
Vacant land loans	Loans for dwellings not attached to real property
Loans secured by 25 or more acres	Loans for agricultural purposes

Loan Estimate. The **Loan Estimate** merged the Truth in Lending disclosure statement required under the TILA as well as the Good Faith Estimate form required under RESPA. The Loan Estimate clearly presents the information considered most important to consumers: the interest rate, monthly payment, total closing costs, and cash required to close. There is no obligation to work with a lender just because the prospective borrower submits a mortgage loan application. The borrower receives a Loan Estimate from each lender to whom the borrower submits a loan application, allowing the borrower to compare loan programs and find the lender that offers the lowest rates and best terms.

Under the TRID rule, the lender is prohibited from charging the borrower any fees until the borrower has received the Loan Estimate and indicated a desire to proceed with the loan. This prohibition includes fees for application, appraisal, and underwriting. The only fee that a lender may charge before issuing the Loan Estimate is a fee to obtain the borrower's credit report.

TRID replaced RESPA's requirement to give consumers a special information booklet with a smaller consumer-friendly booklet, *Your Home Loan Toolkit* (*Toolkit*). The *Toolkit* helps borrowers determine how much house they can afford, suggests questions to ask the lender, and features worksheets and checklists to fill out during the loan process. The booklet also describes the Loan Estimate and Closing Disclosure forms. Lenders are required to give borrowers the *Toolkit* within three business days of loan application.

WEBLINK @

Download the information booklet, *Your Home Loan Toolkit*, at https://www.consumerfinance.gov/owning-a-home/explore/home-loan-toolkit/.

Closing Disclosure. Lenders are required to provide borrowers with a written Closing Disclosure at least three business days before closing the loan. The Closing Disclosure replaced the TILA's final Truth-in-Lending Disclosure and the HUD-1 Settlement Statement. The Closing Disclosure presents much of the same information as the Loan Estimate so that borrowers can compare the Loan Estimate with the Closing Disclosure. If the rates, fees, or principal amount changes drastically from the Loan Estimate, the *Toolkit* instructs borrowers to ask the lender to explain the discrepancies. The guidelines were designed to prevent lenders from attempting to use bait-and-switch schemes. A bait-and-switch scheme is a deceptive plan where a mortgage lender offers a borrower an attractive loan with low closing costs or interest rates, or a no-fee loan estimate and then switches their offer and presents the buyer with a different set of terms and conditions when it is time to close.

Important loan calculation information is presented in the Closing Disclosure. The first four calculations (total of payments, finance charge, amount financed, and annual percentage rate) are required by the TILA's Truth in Lending disclosure. TRID added a fifth calculation called total interest percentage (TIP). The five calculations and the explanation of each calculation is presented in Closing Disclosure Loan Calculation.

FIGURE 13.10 ■ Closing Disclosure Loan Calculation

The Closing Disclosure loan calculations are for a fixed-rate loan with a sale price of $180,000, loan amount of $162,000, 30-year loan term, and a fixed interest rate of 3.875%.

Total of payments. The total amount the borrower will have paid after making all scheduled payments of principal, interest, mortgage insurance, and loan costs.	$285,803.36
Finance charge. The amount financed expressed as the total dollar amount the loan will cost the borrower over the loan's term.	$118,830.27
Amount financed. The amount financed is expressed as the total amount of credit provided to the borrower.	$162,000.00
Annual percentage rate (APR). This includes the interest rate and other loan costs (e.g., origination fees, discount points, etc.) and represents the annual cost of credit expressed as a rate.	4.174%
Total interest percentage (TIP). The total amount of interest that the borrower will pay over the loan term as a percentage of the loan amount.	69.46%

Download the completed Closing Disclosure for a fixed-rate loan. The sale price, loan amount, loan term, and interest rate have not changed from the estimates provided on the Loan Estimate (see the Loan Estimate web link presented earlier in this unit) at https://files.consumerfinance.gov/f/201403_cfpb_closing-disclosure_cover-H25B.pdf (scan QR code).

FIGURE 13.11 ■ **Comparison of Disclosures, Forms, and Prohibitions Under TILA, RESPA, and TRID**

Truth in Lending Act (TILA)	RESPA	TRID
Truth in Lending Disclosure (TIL) and Final TIL Disclosure Statement	Good Faith Estimate (GFE) and HUD-1 Settlement Statement	Loan Estimate (replaced TIL and GFE) no later than third business day after receiving application Closing Disclosure (replaced HUD-1 and Final TIL) at least three business days before closing
TILA Credit Disclosures: 1. Total of payments 2. Finance charge 3. Amount financed 4. Annual percentage rate (APR)	Affiliated business relationship disclosure	Added fifth Credit Disclosure: 5. Total interest percentage (TIP)
Makes bait-and-switch advertising a federal offense	Prohibits kickbacks or referral fees for closing	Further prohibits lenders from using bait-and-switch loan schemes by comparing Loan Estimate with Closing Disclosure
Established triggering terms in advertising to require disclosure of: 1. Amount or percent of down payment 2. Terms of repayment 3. APR		
		Restricts lender from charging fees (except credit report) before borrower indicates desire to proceed with the loan
	Required special information booklet	Replaced special information booklet with *Your Home Loan Toolkit*
	Prohibits seller from requiring buyer to purchase title insurance from a particular company	
	Exempted construction-only loans secured by vacant land and loans secured by 25 or more acres	Removed exemption for construction loans and loans secured by 25 or more acres
	Limits amount lenders can require in escrow for taxes and insurance	
Three business day right of rescission for HELOCs second mortgages and refinance loans on a primary residence		

Practice Questions

25. TRID replaced HUD's special information booklet with a booklet titled __________ __________ __________ *Toolkit.*

26. TRID requires the lender to provide the Loan Estimate no later than the __________ __________ __________ after receiving the loan application.

27. Circle protected classes under the Equal Credit Opportunity Act (ECOA).

    a. Age

    b. Marital status

    c. Familial status

    d. National origin

28. The Equal Credit Opportunity Act prohibits discriminatory treatment of income from __________, __________ __________, __________ __________, or part-time employment.

13.11 SUMMARY OF IMPORTANT POINTS

- Conventional loans are written by private lenders and are not guaranteed or insured by the federal government. Conventional loans typically require a larger down payment, compared with FHA and VA loans, and therefore have a lower LTV. Borrowers must pay for private mortgage insurance (PMI) for the portion of the loan above 80% LTV. Fixed-rate conventional mortgage loans have a due-on-sale clause, so they are not assumable.
- The recommended maximum qualifying ratios for a conventional mortgage are 28% HER and 36% TOR.
- A *fixed-rate amortized mortgage* is one with regular payments each month of principal and interest. The monthly payment remains the same each month; however, the amount applied to principal increases each month, and the amount applied to interest decreases each month. Fixed-rate amortized mortgages are sometimes referred to as level-payment plan mortgages.
- A *purchase money mortgage* is a new mortgage accepted by the seller as part of the purchase price. The mortgage is taken back by a seller from a buyer.
- An *adjustable-rate mortgage (ARM)* is a loan that has an interest rate that can change at preset intervals based on a recognized and verifiable index. The margin is the percentage added to the index to cover the lender's costs plus profit. The index plus the margin equals the calculated interest rate.
- The Federal Housing Administration (FHA) is a government agency that insures mortgage loans made by approved lenders. FHA does not make loans nor does it regulate interest rates. Borrowers pay an up-front mortgage insurance premium (UFMIP) and an annual mortgage insurance premium (MIP). The annual premium is paid monthly as part of the monthly mortgage payment. Borrowers are required to make a down payment of at least 3.5%. The Section 203(b) FHA program insures fixed-rate loans on one- to four-family residences.
- The Department of Veterans Affairs (VA) partially guarantees mortgage loans. Private lenders provide VA loans to veterans, surviving spouses of veterans,

and active military personnel. The VA also has the power to make direct loans to veterans. A veteran's entitlement is the maximum amount the government guarantees the lender will be paid in the event the borrower defaults. A veteran's certificate of eligibility states the amount of entitlement available to the veteran borrower. Down payments are not required on VA loans if the borrower qualifies. The VA charges a funding (user) fee to help the government defray the cost of foreclosures. VA loans do not have due-on-sale clauses; therefore, they are assumable (even by nonveterans).

- With a *partially amortized mortgage*, the buyer makes regular payments smaller than what is required to completely pay off the loan by the date of termination. A single large final payment, called a balloon payment, of accrued interest and remaining unpaid principal is made at loan maturity.
- A *primary market* is the market where securities or goods are created. The primary mortgage market consists of lenders that originate new mortgage loans for borrowers.
- Mortgage loan originators (MLOs) do not make loans. They are middlemen (intermediaries) between borrowers and lenders. MLOs take loan information from a prospective borrower and "shop" for a lender offering the best rates and terms. Once a successful match is made and the loan is approved, the MLO earns a fee.
- A mortgage broker employs licensed loan originators. Mortgage brokers do not make or service loans. They work with lenders to arrange loans for prospective borrowers.
- A mortgage lender originates loans and packages them to investors. Mortgage lenders may use their own money or money borrowed from other lenders. Mortgage lenders also service loans.
- *Intermediation* is the process of consumers depositing funds into savings accounts at financial institutions. Lenders serve as intermediaries using borrowers' savings to provide funds to others for investment and borrowing.
- *Disintermediation* occurs when savers withdraw funds from intermediary financial institutions, bypassing them to invest elsewhere, thereby reducing the amount of funds available to the financial institutions.
- A *secondary mortgage market* is an investor market that buys and sells existing mortgages. Secondary market participants include Fannie Mae, Freddie Mac, and Ginnie Mae. Conforming loans are loans that meet Fannie Mae and Freddie Mac guidelines. Ginnie Mae is a government corporation under HUD. Ginnie Mae is a guarantor of government-insured and government-guaranteed loans and has the full faith and credit guarantee of the federal government.
- The Truth in Lending Act is implemented by the Federal Reserve's Regulation Z and requires lenders to disclose the annual percentage rate (APR) and all costs associated with credit. The law gives borrowers three business days to cancel most consumer loan contracts, except loans to purchase or construct a home.
- The Equal Credit Opportunity Act (ECOA) ensures that financial institutions make credit available without discrimination on the basis of race, color, religion, national origin, sex, marital status, age, or receipt of income from public assistance programs.
- The TILA-RESPA Integrated Disclosure Rule combined the TILA and RESPA disclosures into the Loan Estimate and the Closing Disclosure.

UNIT 13 EXAM

1. Which individual must be state licensed as a mortgage loan originator?
   a. Employee who processes loans for First National Bank of Orlando
   b. Employee of Bank of Florida who works as a bank teller
   c. Employee who works as a loan originator for a mortgage brokerage company that is not federally regulated
   d. Employee who works as a loan originator for First USA Credit Union

2. A commercial bank sold a group of 2,000 mortgages directly to Fannie Mae. This is an example of
   a. primary market activity.
   b. secondary market activity.
   c. loan correspondence.
   d. intermediation.

3. Which statement does NOT apply to Fannie Mae?
   a. Loans that meet Fannie Mae guidelines are called conforming loans.
   b. Fannie Mae purchases mortgages from local lenders and issues mortgage-backed securities.
   c. Fannie Mae is the largest participant in the secondary market.
   d. Fannie Mae is a government agency under HUD.

4. The market where mortgage loans are created, supplying funds to finance real estate purchases directly to borrowers, is called the
   a. primary market.
   b. secondary market.
   c. capital market.
   d. real estate market.

5. A home equity conversion mortgage (HECM) is also called a
   a. partially amortized mortgage.
   b. purchase money mortgage.
   c. reverse mortgage.
   d. home equity loan.

6. When investors bypass thrift institutions for direct investment elsewhere, the process is called
   a. loan correspondence.
   b. intermediation.
   c. disintermediation.
   d. capital-deficit area support.

7. Which set of maximum standard qualifying ratios is used to qualify a borrower for a VA mortgage loan?
   a. 28% HER; 36% TOR
   b. 30% HER; 36% TOR
   c. No HER; 41% TOR
   d. No HER; 43% TOR

8. An FHA loan is a
   a. government-insured loan.
   b. government-guaranteed loan.
   c. conventional loan that is insured with mortgage insurance.
   d. loan in which the mortgagor is protected against financial loss in the event of default.

9. A potential FHA borrower's monthly housing expense is $504, the total monthly gross income is $1,800, and the total monthly obligations are $648. What is the monthly housing expense ratio for the borrower?
   a. 28%
   b. 36%
   c. 38%
   d. 43%

10. In a fixed-rate amortized mortgage, the portion of the monthly payment that goes to reducing the principal
    a. remains constant throughout the loan term.
    b. gradually increases with each payment throughout the duration of the loan term.
    c. gradually decreases with each payment throughout the duration of the loan term.
    d. fluctuates based on the prevailing interest rates.

11. Which characteristic applies to both FHA and VA mortgage loans?
    a. Assumable
    b. Mortgage insurance required
    c. No established loan limits
    d. No down payment required

12. Which characteristic applies to VA loans?
    a. Government insured
    b. Minimum cash investment required
    c. Loan limit set by geographic area
    d. Funding fee charged

13. A man wants to buy a small restaurant and is considering financing the restaurant equipment in addition to the real estate. If the man pledges the personal property in addition to the real estate as collateral for the mortgage, the man's mortgage is
    a. an equipment mortgage.
    b. a package mortgage.
    c. an all-inclusive mortgage.
    d. a chattel mortgage.

14. A new mortgage accepted by the seller as part of the purchase price is
    a. a wraparound mortgage.
    b. an assumption of the mortgage.
    c. a chattel mortgage.
    d. a purchase-money mortgage.

15. Which protected class is covered under the Equal Credit Opportunity Act?
    a. Disability
    b. Familial status
    c. Occupation
    d. Marital status

16. The Truth in Lending Act (TILA)
    a. does not affect real estate financing credit.
    b. attempts to regulate maximum interest rates charged consumers.
    c. requires disclosure of finance charges, as well as annual percentage rates of interest.
    d. requires an affiliated business relationship disclosure.

17. Which regulation is NOT covered under RESPA?
    a. Prohibits the payment of a kickback in exchange for referring a settlement service business.
    b. Prohibits a seller from requiring the buyer to use a particular title insurance company as a condition of sale.
    c. Made bait-and-switch advertising a federal offense.
    d. Limits the amount lenders can require borrowers to escrow for property taxes and hazard insurance.

18. The TILA-RESPA Disclosure Rule requires that the borrower be provided with which item at LEAST three business days before closing?
    a. Closing Disclosure
    b. *Your Home Loan Toolkit*
    c. Guaranteed amount of settlement costs
    d. Loan Estimate

19. As part of the preparation for a closing, a listing broker referred a property owner to an appraiser. The appraiser completed the appraisal and charged the owner $250, which was entered on the Closing Disclosure. The appraiser gave the listing broker $50 for the referral, which the broker accepted. According to RESPA,
    a. the listing broker also must be licensed as an appraiser.
    b. the appraiser has not violated the law as long as the appraiser is state certified.
    c. both the broker and the appraiser have violated the law.
    d. the arrangement is entirely legal.

20. The Truth in Lending Act's right of rescission does NOT apply to which type of loan?
    a. Refinance loans
    b. Bank loan used to purchase a home
    c. Second mortgages
    d. Home equity line of credit (HELOC)