

# chicagotribune.com

## FINANCING

### Weathering the storm

#### Looser rules, larger limits put FHA loans back in a favorable light

By Marilyn Kennedy Melia

Special to the Tribune

June 1, 2008

When first-time buyer John Grooms went to arrange financing for his three-bedroom house in Island Lake, he tapped a source that is roaring back in popularity in the wake of the credit crisis: the Federal Housing Authority.

Long an option for the down-payment challenged, FHA-backed mortgages all but disappeared in the heady days of easy money. Tighter conventional lending standards and newly relaxed FHA rules are changing that.

"The only way I was allowed to purchase was with FHA," says Grooms, 26. "Since they changed the rules with conventional loans, I needed a credit score that was way up there and at least 10 percent down. There was no way I could have done that."

Grooms took advantage of the FHA's 3 percent down payment option and the FHA's more stringent appraisal standards caused little problem.

In the past year, lenders have been ratcheting up the credit-score and down-payment requirements for a borrower seeking a conventional mortgage. But FHA rules don't specify a credit score. Many lenders approve FHA loans for borrowers with slightly damaged credit, such as a couple of late credit-card payments, says Steven McCormick, president of First Centennial Mortgage, Aurora.

In the future, FHA may provide an avenue for the many homeowners now in foreclosure to purchase again.

Five years ago, Norma and Anthony Zepada had their home foreclosed on, but bought a home in Montgomery in April with an FHA loan.

"My husband had a settlement from an injury, and we used it to pay off [bills]," relates Norma Zepada. "The loan officer at First Centennial met with us in December, and a few times after that, making sure our creditors got our payments [recorded on their credit reports]. By April, our scores met FHA standards."

Furthermore, FHA has loosened requirements somewhat on what an appraisal report must reveal about the condition of the home, though its rules remain tougher than those for conventional transactions.

Probably the biggest change that promises to make FHA a popular financing option is that the loan is no



longer geared to lower-price neighborhoods. Congress has increased the FHA loan limit on single-family homes (including condos) in the Chicago area to \$410,000 from \$275,200—an increase in effect through at least December, when it's expected to be extended. This brings it more in line with the \$417,000 "conforming" loan limits, which can be securitized by Fannie Mae and Freddie Mac.

"FHA is making a huge comeback," says Rob Schaid, owner of ReMax Plaza, McHenry, and president of the McHenry County Association of Realtors.

In the last quarter of 2007, 10,424 FHA mortgages were made in Illinois, up from 6,071 a year earlier, notes Judy Heaney of the Midwest office of the U.S. Department of Housing and Urban Development, which oversees FHA loans. Those numbers are expected to jump more with the recent boost in the loan limit, she adds.

Then there's the 3 percent down payment. Not only is it substantially less than the minimum 10 percent required for most conventional loans, but it also can be a gift from family, friends or even non-profit organizations. Cash gifts for down payments from family members also are permitted under conventional lending rules, but with limits. Lenders still want a borrower to come up with 5 percent of the purchase price from their own funds, says McCormick.

Schaid points out that it's fairly common in an FHA transaction for sellers to provide the 3 percent down, funneling it, along with a processing fee of a few hundred dollars, through various non-profits.

Though the federal government has tried to halt this, the non-profits have prevailed in the courts, notes Corey Carlisle of the Mortgage Bankers Association, Washington, D.C. The FHA fears the price of the home could be inflated to compensate the seller for the gift to charity, explains Carlisle.

The IRS did rule in 2006, however, that sellers can't deduct the down-payment "contribution" from their taxes.

Eager to spur sales, real estate and banking groups are conducting seminars for their members on the fine points of the FHA program, which insures the loans.

In May, a session at Re/Max Team 2000 in Orland Park drew 180 out of the firm's 208 agents. Bob Groark was there and says he came away with one especially valuable nugget of information: "FHA doesn't approve borrowers, lending companies do. So if a borrower gets turned down by one bank, he can still try another."

Agents aren't the only ones who have to be brought up to speed. For example, only 900 banks and brokerages are authorized to extend FHA mortgages in Illinois (some are based outside the state), with a waiting list of firms seeking FHA approval, notes Judy Heaney, of the Midwest Regional office of HUD, which oversees the FHA.

Many lenders approved to offer FHA loans are listed on its Web site ([www.hud.gov](http://www.hud.gov)). However, some have to refresh their knowledge of FHA loan rules, since the loans weren't popular for many years, says Barbara Zajicek, executive director of the Illinois Mortgage Bankers Association.

The best way for home buyers to find FHA financing is to ask mortgage brokers and banks about the availability of the loans. Lending firms can set their own rate on an FHA mortgage, so borrowers can expect to find slightly different rate offers from different banks.

The FHA insures fixed-rate and adjustable loans and the interest is comparable to that on conventional ones.

But on FHA mortgages of more than \$275,200, the old limit, the interest can be up to a half point more.

Also, borrowers pay the premium for FHA insurance, which pays lenders should the borrower default. An upfront fee of 1.5 percent of the loan amount is charged, but that can be rolled into the total loan

amount, notes Jerry DuPaw Jr. of Carteret Mortgage Corp., Crystal Lake. Every month, an insurance premium of one-half of 1 percent also is charged.

Just as only FHA-approved lenders can offer the mortgages, only FHA-certified appraisers can be used to value properties for these loans. About 2,000 appraisers are certified in Illinois for FHA, says Heaney. This year, HUD amended its regulations to make it much easier for appraisers to be certified. Instead of taking an examination, state-licensed professionals must simply apply for FHA approval.

Copyright © 2008, [Chicago Tribune](#)