Glossary & Terms

ACRONYMS

AMI: Area median income

AUS: Automated underwriting system

CRA: Community Reinvestment Act

DPA: Down payment assistance

DTI: Debt-to-income ratio

DU: Desktop Underwriter® (Fannie Mae)

FDIC: Federal Deposit Insurance Corporation

FHA: Federal Housing Administration

FHLBanks: Federal Home Loan Banks

GSEs: Government-sponsored enterprises (refers to Fannie Mae and Freddie Mac)

HFA: State Housing Finance Agency

HUD: U.S. Department of Housing and Urban Development

IDA: Individual development account

LIHTC: Low income Housing Tax Credit

LLPA: Loan-level price adjustment

LMI: Low and moderate income

Low MI: Low mortgage insurance

LTV: Loan to value

MBS: Mortgage-backed security

MCC: Mortgage tax credit certificate

MI: mortgage insurance

MRB: Mortgage Revenue Bond

No MI: No mortgage insurance

NMTC: New Markets Tax Credit

PAB: Private Activity Bond

TPO: Third-party originator

USDA: U.S. Department of Agriculture

VA: U.S. Department of Veterans Affairs

TERMS

Approved lender: Lenders that apply for and meet requirements established by the entity (i.e., the Federal Housing Administration, U.S. Department of Housing and Urban Development, the U.S. Department of Veterans Affairs, the U.S. Department of Agriculture, the government-sponsored enterprises, and State Housing Finance Agencies) are granted permission to participate in the entity's programs. Approved activities may include origination, underwriting, purchasing, holding, servicing, or selling mortgages, or offering other mortgage-related subsidy programs. Common eligibility requirements include a net worth threshold, a checklist of financial statements, and a quality control program.

Approved seller/servicer: An institution approved to sell mortgages to, and to service mortgages purchased by the entity (i.e., Fannie Mae or Freddie Mac). Common eligibility requirements include a net worth threshold, a checklist of financial statements, and a quality control program.

Area loan limits: Entities establish the maximum loan that can be insured, purchased, or guaranteed by the entity or program. Limits are based on median home values at the county level and entities typically update limits annually. For example, the Federal Housing Finance Agency (FHFA) sets "conforming loan limits" for the government-sponsored enterprises, the Federal Housing Administration sets "statutory loan limits" for approved lenders, the U.S. Department of Agriculture has "area loan limits," and the U.S. Department of Veterans Affairs follows FHFA guidelines.

Automated underwriting system (AUS): A computer generates a loan underwriting decision based on borrower data and algorithms. Compared to manual underwriting, which can take as long as 60 days, the automated process provides a quick decision and avoids human bias. Entities create systems tailored to their programs; for example, Fannie Mae developed Desktop Underwriter®, and Freddie Mac uses Loan Prospector®.

Basis points: A basis point is one hundredth of 1 percent. That is, one basis point equals 0.01 percent or there are 100 basis points in 1 percent. It is a common unit of measure for interest rates.

Certificate of Eligibility (COE): Veterans must meet eligibility requirements and obtain a Certificate of Eligibility from the U.S. Department of Veterans Affairs (VA) to be eligible for a VA Home Loan. The certificate verifies to the lender that the borrower is eligible for a VA-backed loan.

Closing costs: Fees incurred by the borrower and/or seller for costs associated with the closing transaction. Common fees include appraisal fees, tax service provider fees, title insurance, government taxes, and prepaid expenses such as property taxes and homeowner's insurance. Fees are generally paid up front at closing or the lender may roll them into the mortgage, resulting in higher monthly payments.

Combined loan to value ratio (CLTV): A ratio calculated by dividing the sum of (1) the loan amount of the first mortgage, (2) the outstanding principal balance of any home equity loan, and (3) the unpaid principal balance of all other subordinate financing, by the lesser of the sales price or the appraised value of the property. The CLTV ratio is used for a mortgage loan where the borrower has taken out more than one loan for the property.

Conventional loan: A mortgage that is not insured or guaranteed by a federal government agency, i.e., the Federal Housing Administration, U.S. Department of Housing and Urban Development, the U.S. Department of Veterans Affairs, the U.S. Department of Agriculture, and the Bureau of Indian Affairs. Conventional loans include both loans that conform to government-sponsored enterprise (GSE) guidelines and those that do not conform. Conventional mortgages delivered to the GSEs are also known as conforming mortgages.

Cost basis: For real estate, the cost basis includes the original purchase price and certain other expenses like real estate taxes owed by the seller, settlement fees, and closing costs plus any improvements to the property (but not maintenance costs).

Direct Endorsement Authority: Authority granted to Federal Housing Administration (FHA) approved lenders that allow them to underwrite loans and determine their eligibility for FHA mortgage insurance without the prior approval of HUD.

Discount points: Prepaid interest that borrowers can pay at loan origination to lower the amount of interest they have to pay in the future. Each discount point costs 1 percent of total loan amount and lowers the interest rate by ⅛ to ¼ percentage point. Lenders benefit by receiving cash up front instead of waiting for it in future interest payments.

Down payment: A payment made in cash at the onset of the purchase of an expensive asset. Homebuyers typically pay down payments that equal 5-25 percent of the total value of a home although some federal and GSE programs allow lower down payments.

Escrow: In general, escrow is money held by an impartial third party that disburses the funds after specified conditions are met. The lender establishes the account to pay for property-related expenses like property taxes and homeowner's insurance on behalf of the borrower, and the borrower pays in monthly installments. Certain federal programs require lenders to maintain escrow accounts.

FHA loan correspondent: A financial institution approved by the Federal Housing Administration (FHA) to originate and submit applications for guaranteed mortgages; the institution may not hold, purchase, or service guaranteed mortgages. A loan correspondent may be either a supervised or a non-supervised institution. A loan correspondent that is also a supervised institution may service guaranteed mortgages in its own portfolio. Non-supervised loan correspondents, or mortgage brokers, are non-depository financial entities that have as their principal activity the origination of FHA-insured mortgages for sale or transfer to one or more sponsors that underwrite the mortgages.

FICO score: A type of credit score that lenders use to assess a borrower's credit risk. FICO stands for Fair Isaac Corporation, the company that created the FICO score. Scores are calculated using borrower credit reports and range from 300 to 850. A lower score indicates the borrower has poorer credit, and a higher score indicates the borrower has stronger credit.

First mortgage: A mortgage in the first-lien position that has priority over all other liens or claims in the event of default.

Fixed-rate mortgage: The interest rate is defined when the borrower takes out the mortgage and does not change over the loan term.

Funding fee: Generally, veterans using a U.S. Department of Veterans Affairs (VA)-backed loan must pay a funding fee. It is a percentage of the loan amount that varies based on the type of loan, military category, first-time loan user status, and existence of a down payment. VA funding fees may be financed with the mortgage or paid in cash at closing. Veterans with a service-connected disability are exempt from the funding fee.

Ginnie Mae: Short for the Government National Mortgage Association. Ginnie Mae guarantees timely payments on mortgage-backed securities (MBS) backed by federally-insured loans including those insured by the U.S. Department of Veterans Affairs, Federal Housing Administration, U.S. Department of Agriculture Rural Development, and the U.S. Department of Housing and Urban Development Office of Public and Indian Housing. Ginnie Mae securities are the only MBS guaranteed by the federal government.

Guarantee fee: Fee charged to compensate secondary market purchasers for providing a guarantee on a mortgage-backed security. Guarantee fees are structured as a percentage of the total loan amount.

Housing authorities: A legal entity authorized by a state to provide housing strategies for its communities, including management of public housing. Housing authorities are required to follow federal regulations and receive subsidies from the U.S. Department of Housing and Urban Development. There are over 3,200 housing authorities across the country.

Individual Development Account (IDA): Grant funds provided to match a participant's savings contribution designed to help lower-income individuals and families save for a specific goal, such as homeownership, opening a small business, or going to college. Eligible participants contribute their own savings funds to an IDA account that is then matched by the sponsoring organization at an agreed upon ratio (i.e., 1:3) over a specific amount of time, up to a specified amount. Funds from homeownership IDAs are generally used for down payment and closing cost assistance.

Investing lender: A financial institution, including a charitable or nonprofit organization or pension fund, that is approved by the Federal Housing Administration (FHA) to service, purchase, hold, or sell FHA-insured mortgages. This mortgagee type cannot originate or fund FHA loans.

Lien: A claim or charge against property or funds for payment of a debt or an amount owed for services rendered. In real estate, a mortgage is regarded as a lien. If not repaid, the debt can be recovered by foreclosure and sale of the real estate.

LIBOR: Short for London Interbank Offered Rate. A benchmark interest rate that banks use to charge each other for short-term loans. Based on five currencies—the U.S. dollar, Euro, pound sterling, Japanese yen, and Swiss franc—it serves seven different maturities: overnight, one week, and 1, 2, 3, 6, and 12 months.

Loan-level price adjustment (LLPA): Risk-based pricing adjustments that vary based on credit score, loan-to-value ratio, type of product, and various other factors, charged at the time of origination. Fannie Mae and Freddie Mac charge both annual guarantee fees and upfront LLPAs. Most lenders convert LLPAs into the interest rate on the mortgage, which the borrower pays over time. (See also Guarantee fee.)

Loan limit: The maximum allowable mortgage amount under a particular program established by the federal agency or government-sponsored enterprise (GSE), generally according to statutory parameters. For example, the Federal Housing Finance Agency (FHFA) sets "conforming loan limits" for the GSEs, the Federal Housing Administration sets "statutory loan limits" for approved lenders, the U.S. Department of Agriculture has "area loan limits," and the U.S. Department of Veterans Affairs (VA) follows FHFA guidelines.

Loan-to-value (LTV) ratio: A ratio that compares the amount of the first mortgage with the appraised value of the property. It is calculated by dividing the loan amount by the value of the property. The higher the down payment, the lower the LTV.

Low- and moderate-income (LMI) communities: Low-income geographies have a median family income less than 50 percent of the area median income. Moderate-income geographies are those whose median family income is at least 50 percent but less than 80 percent of the area median income. Banks regulated under the Community Reinvestment Act are evaluated on how well they meet the credit needs of low- and moderate-income communities.

Manual underwriting: Instead of using an automated system, a loan officer evaluates a borrower's risk by calculating the various ratios and analyzing other factors. It generally takes longer to process a loan application using manual underwriting, but there is the opportunity for greater flexibility in evaluating the borrower's creditworthiness.

Manufactured home: A structure that is transportable in one or more sections. In traveling mode, it must be 8 feet or more wide, or 40 feet or more long. When the structure is erected on site it must be 320 or more square feet, built on a permanent chassis, and designed to be used as a dwelling (with or without a permanent foundation) when the required utilities are connected. Required utilities include plumbing, heating, air conditioning, and electrical systems contained in the structure. Structures cannot be self-propelled recreational vehicles. The manufactured home must be built in compliance with Federal Manufactured Home Construction and Safety Standards per U.S. Department of Housing and Urban Development (HUD) regulations. Proof of compliance is evidenced by a HUD Data Plate affixed visibly and permanently to the home.

Mortgage insurance: An insurance policy paid for by the borrower with the lender as beneficiary, in which a third party — the insurer — takes some of the loan-default risk. In the event of foreclosure, the insurer pays a set amount to the lender to cover some or all of the outstanding loan balance. Mortgage insurance should be distinguished from hazard insurance, which a homeowner purchases to cover losses from, for example, fire or theft.

Mortgage tax credit certificate (MCC): Certificates issued to qualifying homebuyers that increase the federal tax benefits of owning a home and help low- and moderate- income, first-time homebuyers offset a portion of the amount they owe in mortgage interest by providing a tax credit to recipients to increase housing payment affordability.

Principal, interest, taxes, and insurance (PITI): The four components of a monthly mortgage expense. Principal is the part of the mortgage payment that goes to paying down the balance of the loan, interest is charged by the lender for the privilege of borrowing the money, taxes are to pay property taxes, and insurance includes property insurance and private mortgage insurance (mortgage insurance).

Private mortgage insurance (PMI): An insurance policy that protects lenders against loss if a borrower defaults on a conventional loan. PMI is required for government-sponsored enterprise loans with loan-to-value ratios over 80 percent. Purchasing PMI allows the borrower to make a smaller down payment.

Representations and warranties: Assertions that the seller makes in a purchase and sales agreement about the nature of the loan and which in turn form the basis for due diligence. If lenders are found to violate representations and warranties, secondary market entities may force the lender to repurchase the loan or may refuse insurance or guarantee claims. This is a tool for ensuring loan originators comply with the credit terms required by the secondary market entities.

Secondary mortgage market: Market in which previously issued mortgages and mortgage-backed securities are traded among lenders and investors.

Subordinate lien: A lien other than the first mortgage that will be satisfied in the event of default only after liens that are more senior are paid off. The most common type of subordinate lien is a second mortgage.

Underserved areas: Federal agencies designate defined geographic regions (often specific census tracts) as "underserved" based on median income and minority population levels for purposes of directing federal funds to improve the community or for other purposes, including the assessment of how well Community Reinvestment Act (CRA) regulated lenders are meeting their CRA obligations.