It's All About the Math – No Wiggle

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That little ditty from the radio playing "It's all about the Bass – no Treble" keeps playing over in my head as I've had to tell more than a few people that qualifying for a real estate mortgage loan these days is all about the math – no wiggle room as it might have been in the past. And when I talk about the math, I mean totals of debt obligations to income, or DTI as it's referred to in the business.

Some folks know how much they think they can afford to spend on a mortgage payment based upon what they earn. In fact, a great many people in the last decade bought a home thinking they could afford the payment without much regard for increases in expenses like taxes and insurance over the course of loan. If you factored an increase in their interest rate on an adjustable rate mortgage, it further complicated what had seemed like an affordable deal in the beginning. Therefore, our government has stepped in with regulatory requirements for mortgage loan qualification.

As a result, we now must adhere to a very rigid computation of debt payments in proportion to gross income, or a loan request is declined, period. There are still different DTI ratios for different loan products, but the base "Qualified Mortgage" loan, or QM loan has a maximum 43% DTI requirement. There's no wiggle room on this deal in order for the loan to be a QM loan. A great many community banks utilize the QM loan for their real estate lending portfolio, which provides the lender with some regulatory assurances when it comes to the compliance with law and litigation support.

Included in the total debt payments are installment loans, credit card payments, student loans, the calculated mortgage payment including taxes and homeowners insurance, and court-ordered child support or alimony. That monthly payment total is divided into the gross monthly income as determined from a paystub which must show current and year-to-date earnings. The resulting figure must be less than 43% or the loan request is denied, even if the customer has shown a history of paying a much larger installment on a rent payment.

Like most underwriting procedures, however, it can be a little more complicated. There's actually an 18-page guide for what constitutes income and how to calculate income, and just what types of debt payments are to be included in the calculation as well. Those applicants who are self employed, receive commission income, rental income, farm income, have seasonal employment or job-related expense account income are all evaluated differently than a strictly W-2 wage earner, and there's a lot of calculation involved in that evaluation.

Debt payments seem to be pretty self explanatory, but also must include contingent liability if one has co-signed for a loan for someone else. For example, if a parent co-signs for a car or a student loan for their college student, those payments must be included in the DTI calculations for the loan applicant, even if the college student has historically paid those loans on time or if payments are deferred until completion of college.

My underwriting time on loan applications has significantly increased with the onset of new regulations this past year, not because we weren't previously considering all of these factors in our loan decision. But now that we have to physically document every calculation and the source of the figures in our loan file, it really "is all about the math, and there is no wiggle!"