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VA HOME LOANS

THE VA HOME LOAN FIELD MANUAL

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PREFACE

I'm a Marine. I am a Marine therefore in most cases I like getting information in a way that allows me to take swift action. If you tell me what to do I execute. If you give me too many options, decision points, forks in the road or useless information – good luck. (Just ask my wife when we are deciding on where to eat.) I was effective in the Marine Corps because I took orders well and had little patience for meaningless information not directly affecting the outcome of the mission.

An amazing product of military training is the ability to think very tactically. To complete a mission, you first define the desired outcome, then strategize and develop a game plan, and execute accordingly. Yet, in matters related to money, including processes such as buying a home, military and veteran families still tend to make decisions emotionally. The purpose if this VA Home Loan Field Manual is simply to give tactics to those who operate so well in tactical situations.

When I got out of the Marine Corps in 2004 and started working to advocate for military and veteran homeownership, I quickly learned the key ingredient to take veterans away from emotional decision-making back to tactical execution. That key ingredient is EDUCATION. When you don't fully grasp the reason why you are moving in one direction or another, you have to rely on how you feel about the situation, instead of concise decision points. A lack of information breeds indecision and can produce a less than optimal outcome.

When decisions are made that are rooted in a clear vision and understanding of not just *what* should be done, but *how* and *why* it should be done a certain way, peace of mind exists. Under those circumstances, service members and veterans excel. There is nothing a trained member of the U.S. Military cannot do with a mission, and a well-defined plan. Apply that on mindset the battlefield and you have the most powerful military on earth. Apply it to your personal financial situation, and the sky is the limit.

So that is why I wrote this guide. In this manual I will not bore you with long, drawn out details. I will not give you the history of the Veterans Administration or explain to you how inflation impacts the bond markets and drives interest rate fluctuation. You don't care at this point. Trust me. You probably never will care about that level of detail. My aim with this handbook is to give you quick, concise, useful information, and creates the shortest distance between where you are now and homeownership. Homeownership as a means to build financial security and hopefully, increased wealth for you and your family.

I separated from the Marine Corps as a Sergeant in 2004. I was 22 years old at the time, had about 50 bucks in my pocket, a wife and 3-month-old son. I lost my parents early on in life, so I sought out and leaned on the advice and information from successful people, books, tapes, and just about whatever else I could get my hands on. The concept of sharing information in this way is very personal to me because I have benefitted so much in the past from books and mentors.

In addition to my wife and son, I now have two daughters, and in the last decade we have been able to use the tactics that I've learned over time in an overwhelmingly beneficial way. We own several homes and have built a great life for ourselves. But it all started by learning how to take information and apply it tactically to our financial situation.

There is also something very personal to me about teaching and advocating for military and veteran homeownership. Most people think the reason is because it is such an amazing financial instrument. Owning a home opens up benefits like appreciation, tax reduction, leverage, ability to rent the home out in the future and earn passive income. Studies show that the difference in net worth between the average American homeowner vs. a renter is approximately 200,000 dollars. Aside from that, a home is the only financial asset that provides shelter. You have to live somewhere, and you can't live in a stock or bond. $2500 BAH paid in rent for a 3-year tour at Camp Pendleton is 90,000 dollars guaranteed to go in someone else's pocket.

But even with all of that said, there is a bigger reason than the financial one. My fundamental belief is – if you have served your country, you *deserve* to own a piece of it. If you chewed the dirt in Iraq or Afghanistan, or Vietnam or Iwo Jima for that matter, you deserve to own a piece of the dirt back home. Work in your garage. Paint your walls. Walk your kids to school and have a place where they can call home. So that's become my personal mission now. Luckily, the Veterans Administration agrees with me and the VA Home Loan is the absolute best weapon in your arsenal to build a foundation for financial security.

So, listen - there will be no longwinded information about stuff that doesn't matter in this manual. If the content doesn't directly result in a situation where you are closer to buying your first home or the next home in your portfolio, it will be cut out. This manual will not be heavily edited. I am going to speak to you like I would speak to any of my clients, friends, family, or anyone else. I will do my best to keep it somewhat coherent, but if I go off the rails, I apologize in advance.

Bottom line is – this manual is being written to take you from zero to home buying hero in as little time as possible with as little distraction as possible. My hope is that you use this information like I did to create a great life for you and your family. Then, pass the information on to someone else that would benefit so that we can move the needle and create wealth for veterans and their families through homeownership.

As you read through this guide, if you have any questions or need anything related to any of this, just reach out and let me know what I can do to help. My team and I still serve military and veteran clients on a daily basis and are ready whenever you want some help getting to the next step. Whether you are looking at buying now, or 5 years from now, planning is key. It may be too early to buy but it is never too early to plan.

In addition, this book is very much a tactical introduction to the concepts of the VA Home Loan. If you want more ongoing information, much more can be found including online courses, live seminar schedules, and you can reach out and ask questions, schedule a consult with me and my team and a lot more at www.vahomeloanbook.com .

Thanks so much for reading, sharing, and helping me move the military and veteran community closer to financial literacy and success.

Semper Fi,

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SECTION I - EDUCATION

CHAPTER 1 - HOME LOAN BASICS

The first important thing to understand is that the VA does not do home loans themselves. The VA guarantees home loans on behalf of banks, which actually do the lending. So, that being the case, the first thing to do if you are going to understand VA loans is get some basic knowledge of home lending and home lending in general.

This information is relatively standard. It doesn't change from bank to bank. Because of the way that the mortgage market works, the banks really have little to do with guidelines, therefore, if you understand what I am about to show you, you will have a really good understanding of how to get any kind of loan.

The goal of this section is to understand three main qualifying characteristics of a buyer or buyers: Credit, Income, and Assets; as well as two main lending concepts: Debt-to-Income Ratio (DTI) and Loan-to-Value Ratio (LTV).

Let's get started…

1-1. BUYER QUALIFYING CHARACTERISTICS

CREDIT

When you apply for a home loan, lenders are going to pull a credit report and look at two things related to your credit. Those two things are your:

- Credit score (FICO Score)
- Monthly debt payments.

Your ***Credit Score*** (FICO score) is used to take evidence of your past performance and project how you are likely to pay in the future. If you have late payments in the past, the credit bureaus will have that on file and your score will be lower, therefore the bank will take that risk into account. The higher your credit score, the lower the perceived risk to the bank and the lower the interest rate. Think about it. If you lend your buddy money and he doesn't pay you back, that is similar to what a bank sees when they review a credit report that has a bad credit history. Similarly, if your friend does pay you back, you remember it and are more likely to feel good about lending to them in the future. From a bank's standpoint, no credit is almost as bad as bad credit, since really no determination can be made of whether or not someone is likely to pay back the money that they are going to borrow if they have no history of borrowing. See Image 1.1 for a breakdown of what goes into a credit score.

Monthly Debt Payments refers to the amount of money you pay on a monthly basis to debts that show up on your credit report. So, a lender doesn't care so much about the 30,000-dollar *balance* on the auto loan but will look at the

500-dollar per month *payment*. This number is used when calculating the "debt to income ratio", which I will show you later in this section, and does not include things that are not on your credit report such as utilities, rent, and other similar expenses. The most typical expenses included on a credit are things like car payments, credit cards, student loans, and mortgages. Typically, anything that requires a vendor do a credit check on to qualify for, will be on your credit report.

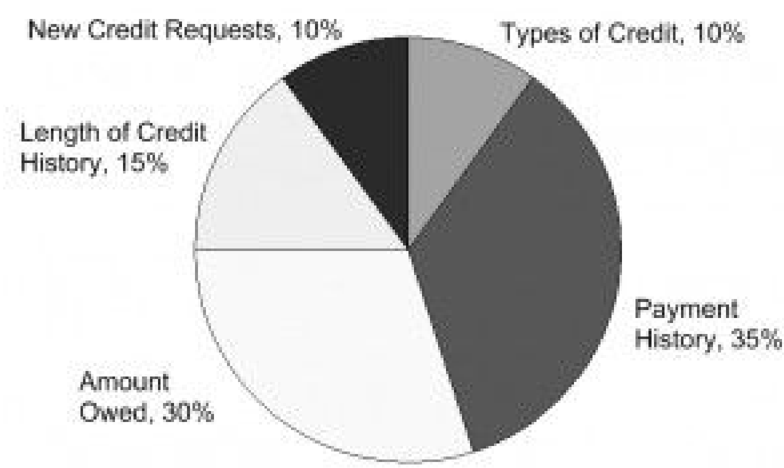


Figure 1-1. Make-up of a Credit Score

For some best practices, tips, tricks and resources should you want to improve your credit, or best understand how to get your credit in the best possible position to qualify for a home, see APPENDIX A – CREDIT BEST PRACTICES. If you want a free copy of your tri-merge credit, reach out to us at www.vahomeloanbook.com and we will be glad to pull your consumer copy for you and help you analyze it as well.

INCOME

In today's market, when it comes to qualifying for a home loan, income is king. Income in combination with debt is what determines how much you are able to qualify for. Credit determines your risk and affects your interest rate, but income determines whether or not you can get a loan to begin with. It is really important to make sure to clarify that when I say the word "income", I am talking about verified, qualified income. Generally, for a bank to consider income "qualified income" it has to have two things: history, and a probability of continuance. Once income is considered qualified income, it is important to note that banks use GROSS income, meaning income *before* taxes and other deductions and allotments are taken out.

To properly evidence income "history" the key is that you need to be in the same *type of job* for at least 2 years. Notice, I didn't say the same job; I said the same *type of job*. If you are an engineer at Boeing, and Northrop Grumman pulls you over to work for them in the same capacity, even if you are only one day on the job, your income history is still intact. If you are a Navy Corpsman and separate from the Navy and get into the medical field, you can use your salary on day one with sufficient documentation. Even if you were in school and graduated with a degree in the field you ultimately start working in, your school can count as the industry experience necessary to use the income.

Income “continuance” when you are using earned income like a salary is implied. There is nothing you have to do to prove it other than possibly get a letter from your employer stating that they don’t plan on firing you anytime soon. The question of continuance comes into play if you have income like child support, or anything not guaranteed to continue. You have to document that you are going to receive the income for at least 3 years after the loan is closed. So, if child support ends when the child is 18 years old, you would just have to document that the child is younger than 15 at the time the loan closes to utilize that income on a loan application.

Here is the thing: Depending on the SOURCE of income, the income can be calculated in different ways. Income from a stable, fixed source like a salary can be counted in full. Even if someone was to receive a raise, 100% of the increased salary can be used with no need to document anything further than the income amount itself. However, some income sources don’t work like a salary. Some income sources fluctuate from week to week, month to month, and year to year. Things like bonuses, overtime, commissions, real estate rental income, and business income are items that fluctuate and therefore a 2-year average of the income has to be taken in most cases to qualify.

For example – if you have 20,000 dollars in business income the first year, and 30,000 dollars the second year, a 24-month average would come out to 2083 dollars per month qualified income. (20,000+30,000) / 24 mos. = 2083 dollars per month. In order to use business income, you would need 2 years in the business. You can go from a business owner to a similar position as a W2 employee and use 100% of your new salary, but if you go from a W2 position and open a similar business, you need 2 years history in the industry, as well as 2 years in the business to qualify.

Here is my advice related to income sources: If you have more than one income source, LESS IS MORE. If you have a salary with bonuses, the salary is very easy to quantify. The bonuses require some documentation. If you need that bonus income to qualify for the home that you want, great, you can go down that road. But more income does not equal better rates. So, if you can use fewer sources of income and buy the home that you want with less documentation, it will make your life a hundred times easier, with no change in outcome.

For a list of income types and ways that they are quantified, take a look at APPENDIX B – INCOME SOURCES AND QUALIFICATION.

ASSETS

The term "assets" refers to the things of value that you own or have currently. Assets can be real estate, or automobiles, or anything else that is valuable for that matter. However, in lending, if you hear assets you should think *amount of money in the bank, in retirement accounts, stock accounts, etc.* Assets are used primarily for down payment and to pay for closing costs. The concept of assets is relatively simple, but they can be a huge pain if you handle them the wrong way.

The bank is going to request 2 months' worth of asset statements. Simple enough, right? However, if any of those statements have any large deposits the bank is going to require that they be fully explained and sourced. If the explanation involves the money being transferred from a separate account, the bank is going to request 2 months' worth of THOSE accounts as well. That can go on and on, and there is little that the bank can do since these guidelines are just as much about guarding against money laundering as it is about making sure that you have the funds required to close escrow.

With assets, my advice is the same as with income. Less is more, and rates and terms do not improve due to higher asset balances. Ask your lender how much you have to come to the table with to buy your home, including down payment and closing costs. Then, figure out which of your asset statements has sufficient funds, with very little activity. If you are able to get a statement with sufficient funds to qualify and little activity, the rate and terms of the loan are the same, but you can rest easy as opposed to dying a death of a thousand paper cuts from a thousand bank statements during the home buying process. Trust me, this is one of the biggest frustrations that people have during the home buying process. In my office our staff is trained to get the best possible terms for the least stress. Terms are always discussed, but people forget that they have to actually do a loan. A stress-free home loan transaction is a beautiful thing…

1-2. BASIC LENDING CONCEPTS

DEBT TO INCOME RATIO (DTI)

Now that you understand the three main characteristics that the bank is going to judge you by – credit, income, and assets - it is important to understand how the bank *uses* that information. The first thing to really grasp is the concept of the "Debt to Income" ratio or "DTI Ratio". DTI determines the amount of loan that you qualify for based on a combination of your *income* and your *monthly debt*. The equation itself is very simple, but understanding it is very important. Here is the equation:

(PROSPECTIVE HOME PAYMENT + MONTHLY DEBT) / GROSS INCOME = DTI

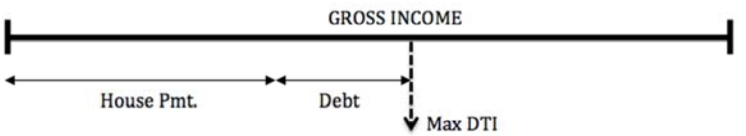


Figure 1-2. Debt to Income Ratio

So, let's break that down. Basically, your new prospective house payment plus any monthly debt payments from your credit report have to be under a prescribed percentage of your gross monthly income. Those maximum percentages, or "Max DTI Ratios" vary depending on the type of loan that you are applying for. Generally speaking, conventional loans allow for a maximum of 45% debt to income ratio, FHA loans allow for a 55% max, and VA is the most flexible, as the VA loan allows for up to a 60% maximum Debt to Income Ratio to get an automated approval. So, if you are doing a VA loan, your house payment plus any debt from your credit report has to be under 60% of your gross monthly income to get an automated approval. *VA is NOT a DTI based loan fundamentally*, as the VA is more interested in "residual income" which will be discussed later – but the banks do look at DTI, and approvals come easier when clients fit these DTI standards.

Once you understand the ratio itself, you can start to work with it. Debt to Income Ratio is just a math equation. With that math equation you can solve for several variables. The easiest way to explain this is to use a few typical questions that we get from clients and explain how we answer the questions.

QUESTION #1: "What is the maximum payment that I qualify for?"

> METHOD: Take gross income and multiply it by the prescribed maximum Debt to Income Ratio (45%, 55%, or 60% depending on loan type). That will give you the maximum for the house payment AND debt. Then, subtract all debt from the remaining amount and you will come up with the maximum payment allowable, which can be used to determine maximum sales price and loan amount, etc.
>
> EQUATION: (Income x Max DTI) – Debt = Max Payment

EXAMPLE: Family has a gross income of 10,000 dollars. On a conventional loan, 45% DTI is the maximum therefore they have 4500 dollars available to pay for the new home, and all debts. If they have 800 dollars in car payments and credit cards, that leaves 3700 dollars in disposable income to qualify for a home loan. Their max payment is 3700 dollars per month. That payment will line up with a price, depending on factors such as rate, down payment, loan term, etc.

QUESTION #2: "Do I qualify for a loan to buy a home with a payment of X?"

METHOD: Take the target monthly payment and add the monthly debt from the credit report. Divide that sum into the gross income and you will get your Debt to Income Ratio. If it is under the prescribed maximum ratio allowed by the loan type that you are trying to qualify for, you are good to go.

EQUATION: (Payment + Debt) / Gross Income = DTI

EXAMPLE: Jim wants to qualify for a home that has a prospective payment of 2,200 dollars per month including all taxes, insurance, etc. He has 650 dollars in monthly debt payments including cars, credit cards, and student loans. He is trying to do an FHA loan, so the max DTI is 55%, and his gross income is 7,500 dollars per month. 2200 dollars plus 650 dollars equals 2850 dollars in total prospective monthly payments. 2850 divided into his gross income of 7500

is .38 or 38% DTI. Jim would have no problem qualifying for this home under those circumstances.
QUESTION #3: "How much income would I need to make to qualify for X payment?"

METHOD: Take the prospective payment and add debt to it. Then, take the sum and divide it by the max DTI allowable under the loan program. That will tell you how much income you would have to make at a minimum to qualify at the maximum Debt to Income Ratio.

EQUATION: (Payment + Debt) / Max DTI = Income necessary to qualify.

EXAMPLE: Jane is getting out of the military and wants to know how much she has to make in the civilian world to qualify for a home that will cost 3,000 dollars per month. She has 450 dollars in car payments and credit cards. She is doing a VA loan, so the max DTI is 60%. 3,000 dollars in her prospective loan payment plus 450 in debt payments equals 3,450 dollars. 3,450 dollars divided by the VA max DTI figure of 60% equals 5,750 dollars per month. So, Jane would have to find a job that paid her 5,750 dollars per month, or just under 70,000 dollars per year to qualify for that loan on her own.

So, I don't mean to get super technical on this, and it is not important to memorize the equations, I just wanted to give real life examples to illustrate the way that you work within the equation to solve for different variables. Once you understand those concepts, you also understand how to solve for issues within the equation. If your debt to income is too high and you don't qualify, what can you do? There are only two things you can do to any equation, and it involves changing either side of the equation. In this case, if you don't qualify you can only INCREASE INCOME, or DECREASE DEBT. That's it. Increasing income may be adding a co-borrower, showing rental income, or getting a raise. Decreasing debt may be paying down credit cards, and other debt or it may simply mean having to adjust expectations relate to how much home you can really afford.

One last thing about Debt to Income Ratio: It does not matter whether you barely qualify or qualify with flying colors. In other words, your rate and terms are not going to change depending on your debt to income ratio. If you have a high ratio or a low ratio, your terms are the same. That means there is no need to show all sources of income if one source does the job and keeps your file easy to document. This is what I was alluding to when talking about documenting income and assets in the simplest way possible.

LOAN TO VALUE RATIO (LTV)

The other bank concept to understand is the ratio known as "Loan to Value Ratio", or "LTV". Loan to value is another pretty simple thing to understand but an important thing to understand if you are going to understand the VA loan. The LTV ratio is a measure of the amount of exposure a bank has on a certain loan. It is a far simpler equation even than the DTI ratio. Here is the equation:

LOAN AMOUNT / PURCHASE PRICE (or Value) = LOAN TO VALUE

If you have 400,000-dollar loan on a 500,000-dollar property, you have an 80% Loan to Value. 400,000 dollars makes up 80% of 500,000 dollars. If you have a 100,000-dollar loan on a 500,000-dollar property, you have a 20% Loan to Value Ratio. If a high loan to value loan was to go into foreclosure, it would be far more difficult for the bank to recoup its investment than if you were to have a low loan to value loan. Therefore, generally speaking, banks see loans with high loan to value ratios as higher risk than those loans with lesser loan to value ratios.

From the bank's standpoint, they need at least 20% wiggle room on a loan to consider it acceptable. That is why people try to save 20% down when they are buying homes using conventional loans. With a 20% down payment there is nothing else needed to satisfy the bank's requirement that there be some room in case a loss was to occur. That being said, not everyone has a 20% down payment.

For conventional borrowers (remember, this is just to teach the system. We will get to VA, I promise) that don't have a 20% down payment, there is an insurance requirement called "Mortgage Insurance". Mortgage Insurance insures the bank on the difference between the required down payment and the available down payment. So, if someone puts 10% down payment, they pay an insurance premium so that if the home goes into default, the bank collects on the policy in the amount of the loss. From a client standpoint, people with less than 20% down can buy a home, but there is an additional cost in order to do so.

VA deals with this in an entirely different way, which you will learn in the next section of this handbook. See Figure 1-3 for a visual representation of LTV and where Mortgage Insurance comes into play.

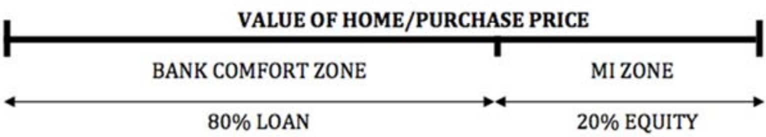


Figure 1-3. Example of 80% Loan to Value Ratio

CHAPTER 2 – VA LOAN BASICS

OK, now for the nitty-gritty. From Chapter 1 you should have a very solid understanding of lending principles that are the building blocks of all home loans. The next step is to get a solid understanding of the characteristics specific to the VA loan. Remember – the focus of this guide is to give you a working, tactical knowledge of the important elements of the VA loan, not to make you an expert on all of the small details. So, keep that in mind. Start with the basics, and then when you are ready, you can move on to a game plan for yourself that takes into account all of the small details.

2-1. VA ELIGIBILITY

The first step in understanding the VA home loan is to understand who is eligible to receive the VA home loan. It is also important to point out the difference between ELIGIBILITY and QUALIFICATION. You can be eligible for the VA home loan, but if you don't have a job, you won't qualify for much. Or, if you have a great income, but don't have the necessary VA eligibility, you are going to have to look at a different type of loan.

So, who is eligible for a VA loan? The Department of Veterans Affairs has set forth some basic requirements to establish eligibility. To be eligible for the VA home loan, active military, veterans, reservists, national guardsmen and spouses must have served under the following conditions:

a) 90 days consecutive active duty service during a period of war
b) 181 days consecutive active duty service during a period of peace
c) 6 years' service in the Reserves or National Guard
d) Reservists and Guardsmen activated under the above circumstances
e) An un-remarried spouse of an eligible military member or veteran who either died in the line of duty, or as a result of service-related disabilities

Once you have an eligible military member or veteran, unlike other loan programs, there are limits to who can go on the loan with you. With conventional financing, you can put just about anyone on the loan with you to qualify. VA is slightly different.

Here is who can go on a VA loan:

a) Veteran (Active Military Counts)
b) Veteran and Spouse
c) Veteran and another Veteran
d) Veteran and certain non-veterans*
    a. This requires VA prior approval and a down payment
    b. Most typical is a fiancée
e) Non-remarried widowed spouse of a veteran who dies on active duty, or as a result of a VA service-connected disability.

The last question is, "How can I verify my eligibility?" The answer is that you need to pull a VA "Certificate of Eligibility". There are several ways to do this, but the easiest way is to do it through the VA Portal system that lenders have access to. If you reach out to us at www.vahomeloanbook.com we can pull your VA Certificate of Eligibility in about 5 minutes, send a copy and break it down for you. See APPENDIX C – CERTIFICATE OF ELIGIBILITY for a sample Certificate of Eligibility.

2-2. VA ENTITLEMENT

Once you verify that you are eligible for the VA loan, the next step is to check your entitlement amount. This figure also comes from your Certificate of Eligibility. Everyone who is eligible starts out with full entitlement, so if you have never done a VA loan before, it is likely that you have full entitlement. That just means that you have the full benefit of the VA loan intact.

Your VA loan benefit is like a rechargeable battery. *You can use it multiple times*, and *you can even have more than one VA loan at a time as well*. As long as you don't use all of the bandwidth, you can use what is available. Although the VA loan is only available for the purchase of primary residences, there are many cases where military members and veterans do a VA loan on a home and then PCS move and are able to use remaining eligibility to purchase another property.

The VA loan is really not from the VA at all. The VA provides a GUARANTEE to the bank who does the loan. In the case of a veteran with full eligibility prior to 2020, the VA would guarantee **25%** of the purchase price up to the *maximum loan limit* in the county where the purchase is taking place. In 2020 the VA changed their guidelines and removed the limit for veterans with full eligibility. If you think back to the LTV section, conventional loans with less than 20% equity (or down payment) required mortgage insurance. In Figure 1-4 you can see how VA addresses that situation:

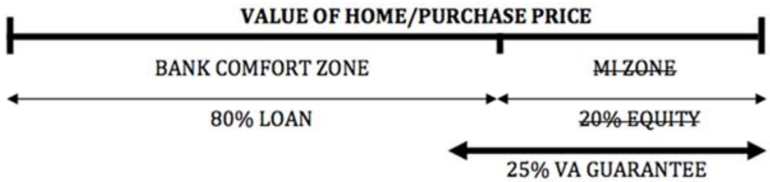


Figure 2-1. VA Guarantee

So, as the diagram indicates, the VA Guarantees 25% of the purchase price on behalf of the veteran. Doing so negates any need to put a down payment or cover the banks risk with mortgage insurance. This is one of the biggest benefits of the VA loan over conventional lending. Think of the VA as a rich uncle who promises to pay the bank if you don't.

If your VA eligibility is tied up in another property you have to use your Certificate of Eligibility to determine how much eligibility you have left to work with in your particular situation. If you sell, pay off, or refinance your home out of a VA loan your eligibility can be restored, and you can use 100% of it once more.

2-3. VA LOAN LIMITS

In the previous section I mentioned that the VA really doesn't do the home loan but provides a 25% guarantee to the bank on behalf of the eligible veteran. I said that if a veteran has 100% eligibility remaining, (no other outstanding VA loans), the VA will give the 25% guarantee up to the *county loan limit* where the property is located. What this means is that the VA keeps a list of counties in the U.S. and largely based on the median home prices in the county, establishes a maximum amount that they would guarantee in each county.

In 2020, however, this changed a bit. Among other things, the "Blue Water Navy Vietnam Veterans Act of 2019 (H.R. 299)" effectively removed the VA Loan Limit for those veterans who have full eligibility. So, in essence, if a Veteran has sufficient income and qualifies for a million-dollar loan, they don't need a down payment at all. They are not subject to county loan limit restrictions. If a Veteran's eligibility is tied up partially, then there is a calculation based on the county loan limits that dictates how much home the veteran can purchase with zero down payment. The county loan limits are updated each year and generally match limits set by Fannie Mae and Freddie Mac for conventional loan limits.

So, just to make this a little bit clearer, here are three quick scenarios to drive this concept home:

SCENARIO #1: Typical 100% Financed VA Home Loan

Client lives in a county where the max VA county loan limit is 424,100 dollars and has full eligibility because they have never used their VA home loan benefit. Purchase price of the home is 330,000 dollars and their income is sufficient to qualify. Since the veteran has full eligibility, after Jan 1, 2020 there is no loan limit, and the VA will guarantee 25% of the 330,000 for the bank so they will have no down payment or mortgage insurance premium necessary. Easy day.

SCENARIO #2: Service member has used and paid off VA loan

Service member gets out of the military and lands a good job with a good income. They had a small property several years back on a VA loan, but they sold it, so their VA eligibility has been *restored* to 100% full eligibility. The veteran wants to purchase a home for 800,000 dollars in San Diego where the county loan limit is lower than 800,000. In the past, the VA would require a down payment if the price exceeded the county loan limits. But – with the 2020 law change due to H.R. 299, the veteran is able to do 100% financing on the 800,000-dollar purchase price. The option of a down payment always exists, but zero down payment is an option.

SCENARIO #3: Purchasing Home with VA Loan Outstanding

HR 299 removed the VA Loan Limits for veterans and military members with free and clear eligibility. But what if a client has a home on a VA loan and wants to purchase another home without selling or refinancing the first home?

Here is the example: Client owns a home that they purchased while stationed in Virginia. They pull their certificate of eligibility and it shows 44,695 dollars already "charged" against their eligibility due to the outstanding loan. This is due to the outstanding home loan on their current property (equal to 25% of their original purchase price – the VA "guaranty").

The buyer CAN purchase another home using the VA loan as long as he or she has enough eligibility left to do so. For example – since the original home was relatively inexpensive, it is likely that there will be a good portion of their eligibility available to use towards a new purchase. The certificate of eligibility will show the amount of eligibility used, and based on that figure listed, as well as the county loan limit where the buyer intends to purchase, a good VA savvy lender can calculate remaining eligibility.
Basically, if the property that one intends to purchase exceeds the maximum amount determined by that calculation, that person can still buy the home, but will be required to make a down payment equal to 25% of the difference between the established limit, and the purchase price. If your lender says 350,000 dollars is your maximum to do a VA loan with zero down, you can still buy a home for 450,000, but would have to put 25% of the difference as a down payment. In this case, 25,000 dollars.

Even with the new law removing the loan limits – County Limits still do apply to purchases for veterans without full eligibility. VA loan limits can be found at:
http://www.benefits.va.gov/homeloans/purchaseco_loan_limits.asp

2-4. THE VA FUNDING FEE

The VA Funding Fee is how the Veterans Administration earns revenue to keep the program alive and sustainable. Depending on your type of service and your situation, the VA charges a fee in the form of a percentage of your loan, which is rolled into the balance of the loan itself. In other words, the VA charges a fee and then allows you to finance it as part of the loan balance to be paid back. This is partially why rates are lower on VA loans than on conventional loans.

There are a few most common funding fee examples. For *first time use* of the VA loan, the VA funding fee is 2.3% if you put less than 5% down payment. So, for a 100,000-dollar base loan amount, you would end up with a total loan amount of 102,300 dollars. For any *subsequent use* of the VA loan the funding fee increases to 3.6% of the loan amount with less than 5% down payment. So, the same 100,000-dollar base loan amount would end up at 103,600 dollars to be paid back.

If there is a down payment those percentages can potentially drop substantially, so work with your lender to structure your loan so that it makes the most financial sense. Rate is one thing, but the right loan structure can really save you a lot of money.

<u>THIS IS IMPORTANT:</u> If a veteran is awarded service-connected disability, a purple heart, or one of a few other less common circumstances, the VA funding fee is *waived entirely*, forever. So, when you start talking about waiving a 3.6% funding fee on a 500,000-dollar purchase, it starts to make a lot of sense to get your disability claims processed. If

you have a VA disability claim outstanding, you will be charged the VA Funding Fee up front. However, if once the claim is processed you are awarded service-connected disability; you can request that the VA refund you the fee in full.

The entire VA Funding Fee Table is listed in **APPENDIX D – FUNDING FEE TABLE.**

2-5. RESIDUAL INCOME

Another unique characteristic of a VA Home Loan is the concept of Residual Income. Most loan types like conventional and FHA only use Debt to Income Ratio to verify that income is sufficient to qualify for the loan. The problem with this is that it only accounts for gross income and debt from the credit report. As previously mentioned, banks use Debt to Income Ratio as a means by which they qualify a veteran for a VA loan quickly and easily, but the VA is a residual income loan. The VA's main objective is to take it a step further and look at how much money you have left to live on after paying typical bills and debts. Many people believe this is why the banks allow for a much higher DTI ratio which gives far more flexibility but have very few borrowers who default.

Because generally if you have a good Debt to Income Ratio residual income is not something that you have to worry about too much, it's not going to be a huge topic here. That being said, it is important to have a basic understanding. The residual income calculation takes your gross income and subtracts things like federal and state taxes, maintenance costs on the home, as well as your debts and makes sure that you still have a sufficient amount of income remaining at the end of the month. Unlike DTI, the residual income calculation has less to do with *how much* you qualify for, and more verifies that you have the ability to repay the loan and still have money left to eat. Go figure.

2-6. MISCELLANEOUS VA TERMS

Different loan types, for the most part, are relatively similar. They may have different guidelines and uses, but for the most part have a lot of common elements around how income is calculated, how credit is analyzed, etc. However, VA has a few little quirky elements that don't deserve their own chapter, but definitely warrant a mention because you may hear about them during your transaction. If any of these are confusing or don't make sense, I wouldn't spend too much time on them.

NON-ALLOWABLE FEES

> The VA has defined fees related to loan transactions that the veteran is technically not allowed to pay. To list them all would be overkill, but they include some of the third-party fees involved in the processing of the loan. If fees categorized by VA as "non-allowable" exceed 1% of your loan amount, someone else needs to pay those fees. This may put you at a disadvantage when negotiating if the seller doesn't want to pay any costs.
>
> Here is the key: If the fees add up to less than 1% of your loan amount, you are allowed to pay them, which give you flexibility should the seller not be willing to cover that cost. Be careful of lenders who charge a 1% origination fee, because that automatically eats up all of your bandwidth for non-allowable fees. Non-allowable fees should not impede your ability to get your offer accepted.

Lesson: Don't work with lenders who charge a 1% Origination Fee. I'm looking at you, Navy Fed.

TIDEWATER INITIATIVE

When you buy a home, an appraiser is going to be called to verify that the sales price is justified by the value of the home. When the appraiser cannot justify the value, he gives notice to the real estate agents that they have to supply more information to support the value, or the appraiser is going to say that the home is not worth the contract price. That act is called initiating "Tidewater".

Lesson: If a Real Estate Agent asks you "What do you want to offer?" – Run. Tidewater doesn't mean the home is not worth what you are paying, as the area may just lack comparable sales. But a good agent should be able to make sure comps are in line with what you are paying.

TERMITE CLEARANCE

The VA requires that properties in certain states prone to termite issues get a full Section 1 termite clearance. "Section 1" refers to an active termite infestation. "Section 2" means that there could be some infestation in the future, but this is not required as long as it doesn't create any other health or safety issues to the buyer of the home. VA requires only

Section 1 clearance, where FHA and Conventional do not require it as a contingency of the transaction.

Lesson: No lesson here. VA will make sure that your home is termite-free when you move in when you live in states prone to have issues with termites.

2-7. THE VA HOME LOAN vs. OTHER LOAN OPTIONS

A question that we receive all the time relates to how the VA Home Loan stacks up against other conventional and government loan programs. Many people think that even though they are eligible, conventional loans are cheaper, or easier to do, or because their realtor told them so, etc. In this section I will give some examples and characteristics of other loan programs to illustrate just how good the VA benefit is. There are circumstances where the VA option is not the best, but they typically involve clients with very specific goals are those situations are few and far between. In our office, the vast majority of the time we recommend, and eligible veterans choose to use the VA Home Loan because it is the best option for them.

Here is the way that I typically explain the loan programs from most beneficial to least:

VA > Conventional > FHA > Renting

So, VA loans (if you are eligible) are better than conventional loans, which are better than FHA loans, which are better than renting and throwing your money away, as long as you have the financial stability necessary to handle costs associated with home ownership.

Here are some more in-depth differences that will illustrate the reason why I think the above chart is accurate:

VA vs. Conventional –

- **DTI -** The VA home loan allows for more flexibility than the conventional loan. This is because with the VA loan, banks allow for a maximum of 60% DTI ratio to get an automated approval, and conventional loans cap at around 45%. So, if you remember back to the last chapter, DTI tells you how much you qualify for – to a certain extent. Higher max Debt to Income Ratio equates to more potential buying power. You don't have to use all of it, but it gives you more flexibility than conventional.

- **Credit -** Conventional loans are VERY credit sensitive. Far more credit sensitive than government loans like FHA and VA. In other words, with conventional lending, if your credit is about 740+, great, you are top tier. However, as your credit drops into different tiers (720, 700, 680, 660, etc…) you start to see massive increases in rate to offset investor risk. With VA, the government is giving the bank a guarantee and there is very little difference in rate between 720 and 620 credit scores.

- **LTV -** The VA requires zero down payment and requires no monthly mortgage insurance. Conventional loans require at least 3-5% down payments with potentially large mortgage insurance premiums due, and mortgage insurance is only avoided once you hit 20% down. Consumers with a large down payment, stellar credit, and those who don't qualify for the VA home loan typically utilize conventional loans.

- **Interest rates –** Rates on government loans such as the VA loan typically run about .25% to .5% lower than conventional loans due to the guarantee provided by the VA to the bank. There are situations where it makes sense to consider conventional. Remember, VA has a funding fee, so if you have 20% down and great credit, conventional should be a consideration.

- **Costs –** The cost difference between VA and conventional loans can vary depending on the client. As previously discussed, VA loans may or may not require a "Funding Fee" that is charged by the VA and rolled into the cost of the loan. This has to be taken into account and is an important topic in itself, so I will go over this in detail later in this section. I will also give a couple of the limited situations where conventional lending MAY be a good fit for an eligible veteran over VA, just to give some context. Just hang tight for a sec.

<u>VA vs. FHA</u> –

- **DTI -** From a debt to income standpoint, FHA allows for more flexibility than a conventional loan. That being said, FHA still does not allow for they debt to income ratio that VA does. With an FHA loan you can typically expect to qualify when your housing payment and monthly debt stays under 55% of your gross monthly income. As previously mentioned, VA has a max limit of 60%.

- **Credit -** FHA is similar to VA when it comes to credit. Since they are both government programs whose sole purpose is fostering homeownership, and because they have an element of a government guarantee associated with them, consumers are far less likely to be hammered for credit blemishes. Unlike conventional loans where interest rate is heavily impacted by credit score, FHA and VA are relatively kind to consumers with imperfect credit.

- **LTV -** As mentioned, VA requires zero down payment up to the county loan limit where the property is located. FHA requires a minimum down payment equal to 3.5% of the purchase price.

- **Interest Rates –** Again, similar to the VA home loan, the FHA loan is a government program aimed at fostering homeownership. For this reason, FHA and VA home loan rates are typically very similar and generally have lower rates than comparable conventional loans.

- **Costs –** The place where FHA goes sideways is cost. FHA requires an upfront mortgage insurance premium that is added to the loan balance. This is typically thousands of dollars and is charged regardless of the size of the down payment, etc. In addition, they charge a monthly mortgage insurance premium that is pretty expensive and at this point in time is not something that can be removed without refinancing the entire loan. Therefore, even if you had a very low interest rate, your EFFECTIVE interest rate could be much higher when you factor in the cost of the monthly mortgage insurance. VA loans do not ever have monthly mortgage insurance premiums, therefore your effective interest rate is your actual interest rate and nothing more.

<u>The case against VA</u> –

There ARE certain circumstances where the VA loan is NOT the best fit for the consumer. In fact, with everyone I ever consult with, my advice is to avoid coming into the consultation or buying situation with a preconceived notion of what you are going to do. We have a lot of situations where a client comes in and says, "I would like to apply for an FHA loan." To which I reply, "Why, specifically, would you like to apply for an FHA loan?" The answers that we get range from misconceptions related to credit, the fact that a friend received an FHA loan, or even situations where they really don't know. The loan programs, along with your income, assets, and credit, are just tools in the toolbox. My advice is that you always define exactly what the job is before you start pulling tools from the toolbox. Start with specific goals, and an idea of where you stand financially and go from there.

There are two things about the VA loan that could make them bad choices for the veteran or service member. Both of them you already know. The first of the two being that the VA loan is not an unlimited benefit. So, if someone was to use their VA eligibility on a property, but had plans of buying again in the future, they may not have a sufficient amount left to do so.

From time to time we get active military men and women who ultimately have a goal of buying their dream home back where they are from, but don't want to waste their BAH while they are in San Diego (smart). In the planning process, when we uncover their goal to ultimately buy their dream home when they get out of the military, sometimes it makes sense to keep their entire VA home loan benefit intact by using a conventional loan on the smaller purchase now. Doing so ensures that their entire VA home loan benefit is available to them when they are ready to buy their dream property. Keep in mind, this also assumes that the client wants to keep their non-dream home as a rental, since you CAN sell the property and reinstate the entire VA home loan eligibility amount. Again, it's all about working to create a personalized plan.

That brings up the second point. Remember in Section 2-4 we went over the VA funding fee. As you will recall, if you do not have service-connected disability, a purple heart, or any of the other qualifiers - the most typical funding fees are 2.3% for first time use, and 3.6% for any subsequent use. Even though the fees are rolled into the loan balance, they still exist and need to be taken into account, as these amounts can be pretty significant. So, the other instance where we may recommend a conventional loan is when a client is dead set on putting at least 20% down, (which avoids mortgage insurance), qualifies at 45% DTI and would be charged a funding fee if he went VA. In this case we would make sure that any rate increase due to the conventional loan is offset by the fact that conventional loans do not include the funding fee.

SECTION II – ACTION

CHAPTER 3 – RUNNING YOUR NUMBERS

Up until this point we have been discussing aspects of different types of lending as a means to understand the benefits of the VA home loan. Also, you have learned some specific functions and characteristics of the VA loan. With that foundational education, it is time to actually get some work done and give you some information that you can use. The best way to really understand what the VA home loan can do for you is to – drumroll please - actually calculate what it can do for you.

It should be stated that this process is not a replacement for a really good VA lender who can help you not only plan, but also ultimately execute your plan. Once you are ready to make a move, this manual is designed to give you a very good working knowledge to make you dangerous but does not mean you should try to manage everything on your own. It takes years to be able to navigate the planning, structuring, and execution of a VA home loan. It would also be a much longer book if I went into all of the intricacies of how income is calculated, credit analyzed, assets sourced, etc. The point is to get you a good idea of what you can do, hopefully show you that homeownership is entirely within reach, and get you on that path. When you are ready for a personalized plan, head over to www.vahomeloanbook.com and drop us a note and we can get you taken care of.

I can say with all objectivity that when you do make that decision to take the next step, my team is the best in the business at understanding not only the VA loan, but also the veteran. Please let us know what we can do to help. Veteran homeownership is our passion, and we would love to add you to the ranks of those we've helped when you are ready to take that step.

For now, let's run through and give you some tools so that you really understand what you qualify for in theory with a VA loan, and that starts with an analysis of your credit and monthly debt. As you go through this chapter, you can follow along with the worksheet provided in **APPENDIX E – PRE-APPROVAL WORKSHEET.** You can also download and print the worksheet at www.vahomeloanbook.com.

Let's get going…

3-1. CREDIT

CREDIT SCORES

<u>Step 1:</u> The first step is to get an idea of what your credit score is. Ultimately you will need a lender to pull your credit report, and if you have my office do it for you, we can also help you analyze and maximize your score. But, just to give you an idea, below is a rundown of some typical credit score profiles. Check them out and you can get an idea of where you stand most likely.

> **<u>740+</u>**: No late payments, low balances in relation to credit limits, long history of paying on time, good mix of different types of credit.
> **<u>700 – 740</u>**: No late payments, relatively low balances in relation to credit limits, and a solid history of paying on time.
> **<u>660 – 700</u>:** Possibly some old late payments or collections in the past, higher balances, and other good accounts.
> **<u>620 – 660</u>:** Some active collections, recent late payments, higher balances on credit cards, not a lot of solid good credit to offset the bad.
> **<u>Below 620:</u>** No real good credit accounts, multiple late payments or collections, tax liens, etc. Maxed-out credit cards, etc.

As an alternative, you can pull a free credit report online, but understand that it is typical for those scores to report in some cases far higher than a true lender credit report because free credit reporting agencies are not lending you any money. The misconception is that the credit bureaus actually formulate the scores. That's untrue. The bureaus only hold the data that actual credit companies run through their algorithms to create the score. So, if you have a free credit report company that is not lending you anything, it makes sense that their algorithm would be more lenient than a lender who is looking at giving you several hundred thousands of dollars for a home.

That being said, remember that VA loans are not super FICO sensitive, so whether you have an 800 FICO score or a 620 FICO score, you should be just fine. Anything under 620 and you may have to do some credit repair before buying. Again, before you pay for a credit repair company let us take a look at it and we may be able to advise you of some pretty simple fixes that could go a long way.

MONTHLY DEBT

<u>Step 2:</u> Account for all of your monthly debt payments on your credit report. This includes car payments, credit card minimum payments, student loans, etc. This does NOT include utilities, or anything else that does not show up on your credit report.

Notes:

- Exclude mortgage payments for what is or will become a rental property. This will be addressed in "income".

- Co-signed loans can be excluded only if the past 12 months payments have been made from the other parties account. For example, if you cosign for your child, and your child has made the last 12 payments out of their own account, you do not have to include this amount.
- Any installment such as a car payment, etc., that has less than 10 months remaining on the term can be excluded.

Take some time to log your debt payments on the pre-approval worksheet

3-2. INCOME

QUALIFY YOUR INCOME

Step 1 – Determine whether or not your income is from an acceptable source.

Rules:

- You must have two years INDUSTRY history. You do not need two years in the same job.
- Your two years CAN include schooling that resulted in a degree that pertains to the industry that you now work in.
    - I.e.: Nursing school to nursing job.
- Military transitions are typically pretty easy to work with, and military experience can typically be used to help cover the two years even if the jobs are not exact.
- If you are self-employed (you get paid on a 1099, as opposed to a W2, or own a corporation) you need two years history in the industry, AND two years history in the business.

QUANTIFY YOUR INCOME

<u>Step 2</u> – Calculate your <u>gross monthly income</u> from all acceptable sources for all borrowers on the loan.

Types of Income and Calculations:

- *Salary* – Use 100% of Salary
- *Military Base pay* – 100% of current rate
- *Full Time Hourly* – Use 100% of Full Time Hourly Pay
- *Retirement* – Use 100% from Award Letter
- *Social Security* – Use 100% from Award Letter
- *Bonus* – Use a 24 Month Average*
    - 24 Month Average is (Year 1 + Year 2) /24 = income
- *Overtime* – Use a most recent 24 Month Average*
- *Commissions* – Use a most recent 24 Month Average*
- *Child Support* – Use 100% of amount from agreement
    - Must show 6 months receipt and at least 3 years left
- *Alimony* – Use 100% of amount from agreement
    - Must show 6 months receipt and at least 3 years left

*For income sources that typically use a 24-month average, if the income was LOWER in the most recent span of 12 months, you have to use only the most recent 12 months average. Easiest way to do this is to take your year to date paystub and your year-end paystubs that show the total annual amount and divide it by 24 using the last 24 months income amounts.

- *BAH* – Use 100% to 125% of BAH depending on tax bracket
- *BAS* – Use 100% to 125% of BAS depending on tax bracket
    - Since BAH and BAS are tax-free, the VA allows you to "gross up" the pay up to your tax rate.
    - Conservatively, leave it at 100%. Moderate – 115%. Maximum would be 125% of the value from the LES.
- *Business Income* – Use a two-year average of NET profit, adding back depreciation.
    - Year 1 Net Profit + Year 1 Deprecation = Year 1 total
    - Year 2 Net Profit + Year 2 Depreciation = Year 2 total
    - Year 1 total + Year 2 total = 2-year total
    - 2-year total divided by 24 months = <u>monthly income</u>
- *Corporate Income* – Same as Business Income

- *Real Estate Rentals* - To do real estate rentals from the tax return is difficult. This would require professional loan advice. If you are leaving your current residence and will be renting it out, that is a different story.

To calculate rental income on a home NOT on tax returns:

- Take 75% of the prospective monthly rent
- Subtract your TOTAL mortgage payment including taxes and insurance from that figure -
- If the remainder is POSITIVE, it is considered income and should be added to the overall gross income;
- If it is NEGATIVE it is considered debt and should be added to the overall debt figure.

So, part of the reason why I listed all of these income sources was to give you specifics that you can use. The other reason is to further illustrate that the actual PROCESS of attaining a home loan is really complex if you do it right. To keep things VERY simple, just take a guess at your GROSS monthly income and use that as your income number.

Add GROSS INCOME to your worksheet in APPENDIX E

3-3. MAX APPROVAL

Now that you have a good idea that your credit is OK, and you know your gross income and monthly debt payments, you can finalize the form and get a really good idea of the maximum amount that a bank would qualify you for.

<u>Step 1:</u> Take your TOTAL GROSS INCOME and multiply it by .6

<u>Step 2:</u> Subtract your TOTAL MONTHLY DEBT from the product of *Step 1*

<u>Step 3:</u> The remaining figure is your MAX HOUSE PAYMENT

<u>Step 4:</u> Divide the MAX HOUSE PAYMENT by 600

<u>Step 5:</u> Multiply that number by 100,000

<u>This is the maximum price you would qualify for based on this calculation.</u>

Confused? Ok, to drive this concept home, let me do a quick run through of how this looks with a fictional borrower with income of 6500 per month, and 950 worth of car, credit card and student loan payments... The “600” figure is used because, very generally speaking, you can expect to spend APPROXIMATELY 600 dollars per month for every 100,000 dollars you spend on a home using a VA loan with zero down. This obviously changes as rates change as well as geographically, so again, this should only be used to get a ballpark idea of how things work.

Here you go:

Step 1: Household Income of 6500 per month x 60% (.6) = 3900

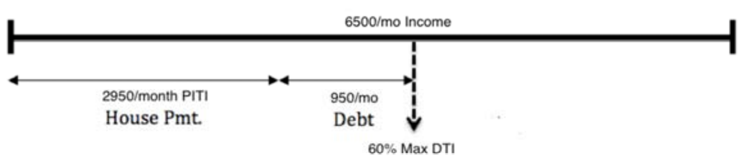
Step 2: 3900 minus Household Debt of 950/month = 2950

Step 3: Max House Payment of 2,950 per month.

Step 4: 2950 divided by 600 = 4.916

Step 5: 4.916 x 100,000 = An approximate 491,600-dollar max purchase price…

Here is how that example is shown on the line graph:



This is the calculation that will tell you the MAXIMUM that you would qualify for. It should not be implied that you would have to purchase a home of that size. There are many occasions where we have clients come in and qualify for much more than they want to spend on a monthly basis. This is why it is important to focus on this calculation to figure out your maximum, but then make sure you have a great understanding of how much you can comfortably spend each month from a personal finance standpoint.

To get a basic idea, not adjusted for interest rate adjustments, etc., you can use the 600 dollars for every 100,000 dollars borrowed figure. For example: 100K = 600 dollars per month; 200K = 1200 dollars per month, and so on. That amount takes into account a basic estimate for principal, interest, taxes, and insurance. Keep in mind; this is based on an estimated California tax rate of 1.25%. Other states would require an adjustment to this figure but give us a call and we can walk you through it if you are buying elsewhere.

Also remember that there is still the residual income requirement that is meant to make sure that you have money available to live on after paying for all expenses related to the home. Debt to income doesn't take into account any maintenance on the home, and it uses gross income to qualify. The residual income calculation removes pay deductions and subtracts all household expenses including estimated maintenance in order to make sure that the veteran has enough money remaining at the end of the month to take care his/her family. Residual income is pass/fail and will be checked when you get pre-approved for your actual purchase. Our worksheet would be a nightmare if we had to factor in residual income. In most cases if DTI calculations work, residual will be fine, but you'll want to verify with your lender before looking for homes.

3.4 – DOWN PAYMENT

If you have full eligibility available, H.R. 299 says that you will not be required to make a down payment. But, if you already have a VA loan out, a down payment may be required. This calculation is relatively easy but should be done by a licensed professional to ensure accurate calculation.

> For example: If I am buying a home in San Diego where the county loan limit is less than 800,000 dollars, and I want to buy a home that costs 800,000 dollars, I would have previously had to put a down payment. With the H.R. 299 law change, starting Jan 1, 2020 no down payment is required.
>
> If I already have a home in Virginia that used up a portion of my VA Eligibility, and I only had 400,000 dollars remaining as a max loan amount, I would need to put 100,000 dollars in down payment. $800,000 minus $400,000 is $400,000. 25% of which is my down payment – $50,000. (VA guarantees 25% up to my maximum, and I am responsible for the rest at 25%.)

So, as you consider the amount that you qualify for based on your debt and income, you can also consider the down payment that may be required for you to purchase your home. In the second section of the Pre-Approval Worksheet, you can calculate your potential down payment requirement.

a) If you have full eligibility, you are not required to make a down payment.

b) If you do NOT have full eligibility because you have another VA loan outstanding, you can calculate your remaining eligibility by following the steps below.

1) Figure out the county loan limit where you are buying your next home. The limits are updated annually and can be found by searching it on the internet, or the VA website.
2) Take 25% of the county loan limit. This is the figure that used to be the max guaranty for that county before H.R. 299.
3) Find the amount of eligibility you have already used on your certificate of eligibility. This should be listed pretty clearly under the "entitlement charged" section.
4) Subtract your "entitlement charged" from the figure that you got by taking 25% of the county limit. This is NOT your max loan amount, but the new VA max guarantee for your new purchase.
5) Since VA's guaranty to the bank is 25% of the loan, multiply the figure by 4 (or divide by 25% - same thing.) This will give you the new MAX purchase price with zero down payment using your VA loan.

Remember – you CAN buy a home at a higher price than this. But it will require a down payment equal to 25% of the DIFFERENCE between your maximum, and the sales price*

OK, I've got to say it again. This exercise was SOLELY to illustrate that you probably qualify for more than you think, with less hassle than you think. I want all military members and veterans to be homeowners and I want to give tactics. That being said, there are a lot of details related to the structure of a loan and verifying of information. So, if you get a good idea that you can most likely buy using this process, give me and my team a shout at www.vahomeloanbook.com and we will put some actual numbers on paper and get you set up and ready to go.

CHAPTER 4 – SAMPLE PRE-APPROVAL

The other day we had a client come through the door and I thought his family's situation would be a perfect scenario to use as a way to illustrate the loan pre-approval process. For anonymities sake, we will call him "Sgt. Jones".

Sgt. Jones is married and has two kids. He is a Sergeant with 6 years' time in Service, so per his LES, in 2017 (the time of the original publication of this book) he is making 2856 per month in base pay. He has 368 dollars in BAS and based on the Camp Pendleton zip code at his rank with dependents, he gets 2412 dollars BAH. He and his family are currently residing in base housing though, so that BAH is not currently collected.

On the debt side Sgt. Jones is doing pretty well. He and his wife just paid off her car, and his car payment is only 349 dollars per month. They have a Military Star Card and a Costco card, but the minimum payments are only about 110 dollars per month. No student loans, no other debts, and relatively good credit scores. The wife doesn't work, and her credit was slightly lower due to some old collection accounts, so strategically we are going to leave her off of the loan but put her on title. That way she is an owner of the property but does not negatively affect the interest rate at all. However, because this is a VA loan, we DO have to take into account all household debt, meaning if a couple is married, we have to account for the spouse's debt even if in this case she will not be on the loan.

So, here is the breakdown:

INCOME –
- 2856 Base Pay
- 2412 BAH
- 368 BAS
    - This totals 5636 per month in INCOME

DEBT –
- Car - $349/month
- Wife's STAR card – $59/mo
- Costco card – $51/mo
    - Total debt – $459/mo

With this information we can the max pre-approval calculation:

- Step 1 – Apply the debt to income max
    - $5636 Income x .6 (60% Max DTI) = $3382
        - This is the max available room for debt and house payment

- Step 2 – Subtract the debt
    - $3382 – $459 Debt = $2923
        - This is the max house payment including taxes, insurance, etc.

- Step 3 – Convert that into a purchase price
    - 2923 divided by 600 = 4.871
        - This means that the family would qualify for a home at zero down

payment of 487,000 dollars, approximately.

Since Sgt. Jones has never used his VA Home Loan Benefit, we weren't surprised to see that he had full VA eligibility when we pulled his Certificate of Eligibility online. Since that full VA eligibility is intact, and H.R. 299 removed the VA loan limits starting Jan 1, 2020, no down payment is needed. In addition, his agent was ultimately able to negotiate that the seller pay all closing costs, so this particular military family was able to get into a home for no down payment, and absolutely zero money out of pocket.

Here are some additional financial benefits that this military family now enjoys:

- Since BAH is 2412 per month, if this family were to stay in base housing, they would have lost out on about 87,000 dollars in tax-free income over the next 3 years at this duty station. BAH is one of the most powerful things financially because it allows tax-free income to be used to buy a tax-advantaged asset like a home. Buying a home allows them to stop wasting this income.

- Sgt. Jones should consult his tax preparer because he can anticipate some tax savings due to the purchase. Mortgage Interest and Property Taxes will now be one of his biggest tax deductions, adding up to thousands of dollars per year saved due to the purchase of his home.

- Appreciation in the area Sgt. Jones is buying at this time has been running at about 3 percent annually. If the Jones family home continues to accumulate equity in this way, he can expect an additional 15,000 dollars per year in net worth due to property appreciation. From losing 87,000 dollars over the next three years in lost BAH to adding net worth of 45,000 dollars if housing trends in his area hold up. A potential swing of 132,000 dollars over three years without saving another dime.

- That being said, even if the trends DON'T hold up, what is the worst that can happen? The vast majority of VA loans done out of our office are 30-year fixed loans. Because of this, the Jones Family can always rent the home out if Sgt. Jones deploys or moves duty stations. In addition, even if the property never appreciated a dollar, which is highly unlikely, he would still have a financial asset worth hundreds of thousands of dollars to leave to his kids, or for whatever other need that may arise.

This and other reasons are why some of the most successful veterans that I know attribute at least part of their financial success to the purchase of real estate using the VA loan. Some purchased multi-unit properties and rented the other units out. Others purchased a home in each duty station they landed at and built an impressive real estate portfolio while still enlisted. Some of my friends had a million dollars in real estate assets before they retired and now enjoy military retirement as well as passive rental income. This is why I am passionate about veteran homeownership. It's a game changer if you do it right.

Connect with us at www.vahomeloanbook.com and we can do for you what we did for Sgt. Jones. It all starts with a plan.

CHAPTER 5 – NEXT STEPS

5.1 – PRE-APPROVAL

Your next steps are simple. It could absolutely be too early for you to buy. It may make no sense at all to buy now. However, I have never met anyone in my life where it was too early to get educated and put a plan in place. I mentioned it once, and I will mention it again: At our office we do not see our job as "getting people loans", even if that is what our job ultimately leads us to do. Our job is to advise and educate military members and veterans on their options and help them put plans together so that when they ARE ready to buy, they are educated, fully engaged, and have 100% peace of mind through a great understanding of the process.

The first step in the home-buying process is NOT finding the home. If you find the home of your dreams and you want to move quickly, you'd better have a briefcase full of money, or a pre-approval. Getting a pre-approval done up-front is important for a number of reasons:

First, you don't know if you can buy unless you have sent all of your income and asset documents to be reviewed, have had your credit pulled and reviewed with you and have been pre-approved fully. I can't tell you how many clients think they are fine and find out that some credit card reported their payment late and their credit score dropped. We also run into a ton of veterans who now own businesses and make a lot of money in reality, but when their accountant gets ahold of it, they make far less on paper. Good for taxes, bad for qualifying. So, you have to know that you CAN qualify first.

> Second, logistically you want to have a fully vetted file so that when you DO get your offer accepted you could move quickly. Once you find a home, most sellers want to close in 30 days and that is not an issue, but you certainly don't want to be tracking down tax paperwork for the first 10 days of the process. Having your pre-approval up-front helps ensure a stress-free process.
>
> Last, sellers will not accept offers if a buyer is not first pre-approved. Furthermore, most good Realtors won't even show property to clients without a pre-approval. It's not that it's a waste of the Realtor's time to show property to a client who has not been pre-approved, but it could very well be a huge waste of your time if you spend days looking for property you can't purchase.

You definitely want to have a good Realtor working for you, and you definitely want to be pre-approved. If you are lat all interested in putting a plan together, or have any questions about the home loan process, make sure to connect with us at www.vahomeloanbook.com and we can get you taken care of. Whether that is just answering questions or getting you pre-approved and putting you in contact with a great Realtor who knows how to serve veterans and military families, we are here to help either way. When you are ready, it is just as important to work with a Real Estate Agent who understands VA home loans and veteran's issues as it is to work with a lender who understands VA home loans and veteran's issues.

5.2 – THE VA HOMEBUYING PROCESS BY THE NUMBERS

Once you are pre-approved, you are ready to look for houses with your Real Estate Agent and make offers. Here is a quick rundown of how the home buying process works. To explain every single document and process would be a waste of your time at this point, so this is very simple and by the numbers…

Searching for the Home:

1) You get Pre-Approved and educated on the loan process
2) You meet with your Realtor and give them specs on homes that you would like to see.
3) Your Realtor puts together a list of homes and drives you around to view them.
4) You decide which homes you like, and if everything lines up well, you can make an offer to purchase the home.
5) Your Realtor will help to advise you on how much to offer, and the terms of the purchase.
6) The offer is presented to the seller and reviewed. It can be accepted, denied, or they can send back a counteroffer.
7) When accepted, the terms are finalized, the offer is fully executed, and the file is said to be “In Escrow”.

Opened Escrow to Approval:

1) All parties are notified, and an escrow company is called upon to act as the neutral third party.
2) A "good faith deposit" – typically approximately 1% of the price of the home – is deposited into escrow as a show if seriousness by the buyer. This amount can vary.
3) The loan file is updated, disclosures are sent out, the appraisal is ordered, and the file is sent to the underwriting department to be approved.
4) The buyer typically requests a full home inspection with a licensed inspector. Any repairs necessary can be requested, or a credit in lieu of the repairs being done can be requested as well. This is different than an appraisal. Appraisers only look for major defects and establish value. Home Inspectors give a VERY detailed report of the state of the home.
5) Appraisal comes back and is sent to the buyer. The two things to pay attention to are the VALUE of the home, and any lender request that REPAIRS be done. The appraiser typically only requires repairs that pertain to potential health and safety issues. If the appraisal comes in low, you can renegotiate the price, pay the difference, or cancel the transaction.

6) The Loan is "CONDITIONALLY APPROVED" by the underwriter – which means it is approved with some clarification or documentation requested.
7) The Lender requests any conditions set by the underwriter. Once those items are satisfied, the loan is sent back to be FULLY APPROVED, or "CLEARED TO CLOSE".

Approval to Close:

1) Once loan is "clear to close" the lender will order the loan documents from the closing department of the bank
2) Loan documents are sent to escrow, and escrow prepares an estimated settlement statement that the lender can review with the buyers. The settlement statement itemizes all fees and gives an idea of how much cash (if any) is required to close.
3) Escrow will schedule the loan documents signing in their office, or via a mobile notary who specializes in loan document signings and will show up wherever you want to meet them.
4) Buyers sign the loan documents. In some states, this is the close of escrow. However, in states like California, escrow receives the documents back and sends them to the lender for funding.
5) The Lender receives the fully executed documents, finalizes any conditions and will "Fund" the loan. This means they send

escrow/title a check in the amount of the approved loan.

6) Once the funds are received from the bank and from the borrower, Title will release the file for recording at the County.
7) Once the file is recorded, the buyer is the legal owner of the property and can pick up their keys and move in.

5.3 – AFTER THE PURCHASE TRANSACTION

The VA IRRRL

As a VA homebuyer you have access to a pretty amazing asset even after you finalize your purchase. If you take advantage of a 30-year fixed rate, your payment can never increase. However, it can decrease if the interest rate market gets better through the process of refinancing. Refinancing is taking out a new loan, preferably with better terms, to pay off the old loan. With conventional lending, in order to refinance you would have to do a new appraisal and resubmit all income documentation and do an entirely new loan. However, with the VA loan, you have access to what is called the Interest Rate Reduction Refinance Loan, or IRRRL program.

An IRRRL refinance allows you to present very little documentation and benefit from a lower interest rate whenever it is available. It also does not require a new appraisal. The IRRRL loan can have closing costs associated with it, but it can be rolled into the balance of the loan, or paid by the lender at a slightly higher rate than would be available otherwise. We have had many clients who saw their rent increase over and over. Even in a situation where a purchase increased their monthly payment slightly at first, the security of a payment that doesn't increase but that can be reduced is a huge benefit. The best of which cases are those in which VA buyers are able to BENEFIT from the rising rents by renting their homes out once they move.

If you have a VA loan now and would like us to analyze it and make sure you are in the best possible position, or to see if an IRRRL would be beneficial, just reach out to us at www.vahomeloanbook.com and we can analyze your situation and get you some objective feedback.

The VA Cash-Out Refinance

The VA loan program also allows the most possible flexibility when it makes sense to access some of your equity to do home repairs, remodels, pay off debt, etc. Cash out refinances should be very well thought out, and it is important to make sure that all of the pros and cons are weighed. But if access to capital is important, and ideally you are able to reduce your interest rate at the same time as you are accessing the needed capital, the VA allows for the cash out refinance up to 90% of the value of your home. Again, understand that there are a lot of lenders who would sell you on this idea without looking at the consequences. If you do end up taking 90% of your equity out of your home, it could potentially put you at risk of not being able to sell if necessary. So again, work through all of your options before going this route.

ALL THAT BEING SAID – for now, let's get to work on GETTING you that equity. Let's face it, it wouldn't be a bad thing to have the option of accessing wealth if necessary, but it can't be accessed unless it is available, and there is no way you are going to build any long term wealth by renting or staying in base housing and losing out on your BAH each month. It may not be the time to buy, but it is ALWAYS the time to plan. GET STARTED ON YOUR PLAN TODAY! If we can play any part in your success, please don't hesitate to reach out and let us know how!

Thanks for reading. Hope it was useful.

Semper Fi!

Daniel Lehman, Author
Marine Corps Veteran

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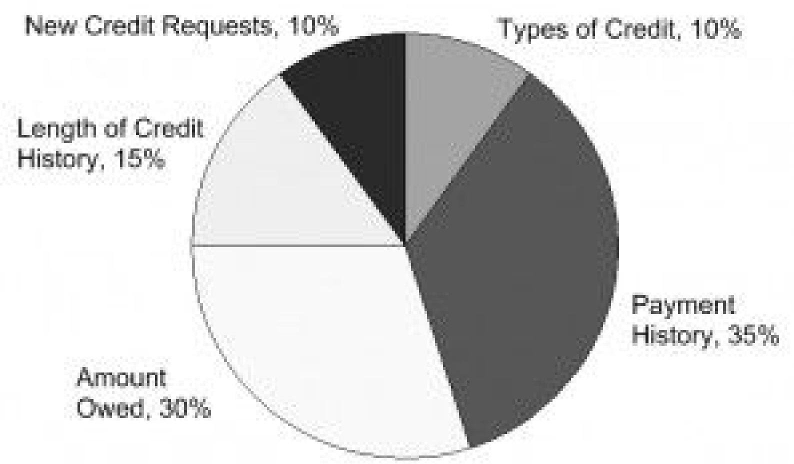
SECTION III – APPENDICES

APPENDIX A – CREDIT BEST PRACTICES



Make-Up of a Credit Score

- **Payment History – 35% of score**
  - Make sure that you have a system of paying bills on time. Credit is not considered late until it is 30 days late. If you do go late before it is reported, ask your creditor if they are able to change the reporting out of good faith if it is the first offense. The more recent the late, the more it will hurt your credit.
- **Amount Owed – 30% of score**
  - This should read: "Amount owed in relation to credit limit". The higher your balance is in relation to your limit, the lower your credit

will be. Keep your balances below 30% if at all possible. Use your cards, but pay them down each month.

- **Length of Credit History – 15% of score**
    - NEVER close credit accounts unless absolutely necessary. If you close a credit card, you not only remove an "ability to borrow" that helps with the "amount owed" ratio, but you also remove all of the positive credit history that exists. The longer you have a good account, the better your credit will be.
- **New Credit Requests – 10% of score**
    - This is also called "Inquiries". If you go around filling out credit card applications and taking out consumer credit in a short period of time, your score will be negatively affected. However, credit pulls for auto purchases and mortgages are slightly different, as they do not have the same negative affect. Have enough credit to get a good score, but do not take out multiple inquiries in a short period of time.
- **Types of Credit – 10% of score**
    - Make sure that you have a wide variety of credit types. A couple of credit cards used lightly, a car loan and a mortgage will have a much better score than someone with only one credit type being used.

If you need help with your credit or have questions, we can help… Connect with us at www.vahomeloanbook.com

APPENDIX B – INCOME

- **ALL INCOME**
    - Must have 2 years history in same industry
        - Self-employed borrowers must have 2 years self-employed
    - Must be "likely to continue"
    - All income used for qualifying us GROSS income (before tax)
    - Military borrowers must have 1 year left on contract or "intent to reenlist" with ability to reenlist documented from Command
- **INCOME TYPES AND CALCULATIONS**
    - **Earned Income**
        - Military Base Pay – 100% of current base pay
        - BAH/BAS – Up to 125% of BAH/BAS where purchase is located, due to tax-free income type.
        - Salary – 100% of current salary used
        - F/T Hourly – 100% of hourly used
        - Commission, Bonus, Overtime – Average over 12-24 mos
        - Allowances – OK if documented and will continue
    - **Self Employed Income**
        - Schedule C – Net Business income minus meals and entertainment, plus depreciation, averaged over 2 years.
        - S Corporation – K1 income minus meals and entertainment, minus any loans due in less than 1 year, plus

depreciation, plus any salary paid, averaged over 2 years.

- **Rental Real Estate Income**
  - If on tax returns, this is a specific calculation done by the lender that is basically net income minus expenses over a 24- month period.
  - If NOT on tax returns yet (current residence transferring to rental, or new purchase of a rental) the calculation is 75% of gross rental income amount minus the total mortgage payment.
- **Retirement Income/Disability**
  - 100% of documented retirement income OK.
  - Tax-free military disability can be up to 125% of value
- **Child Support/Alimony**
  - Can be used as long as it will continue for an additional 3 years past the closing date. Typically evidenced by divorce decree and/or children's birthdates.

- **NON-USABLE INCOME**
  - GI Bill Benefits – these are temporary and are not earned if you stop going to school
  - Any income paid "Under the Table"
  - Part time income without a 2-year average
  - Income from any borrower not appearing on the application

If you have specific questions about your income, let us know by reaching out at www.vahomeloanbook.com.

APPENDIX C – SAMPLE CERTIFICATE OF ELIGIBILITY

VA **Department of Veterans Affairs** — **CERTIFICATE OF ELIGIBILITY**

REFERENCE NUMBER 3537059 — FOR LOAN GUARANTY BENEFITS

IAME OF VETERAN [redacted]

SERVICE NUMBER
SOCIAL SECURITY NUMBER [redacted]

ENTITLEMENT CODE **04** BRANCH OF SERVICE **Marine Corps** FUNDING FEE **NON EXEMPT**

Prior Loans charged to entitlement

VA Loan Number	State	Loan Amount	Date of Loan	Entitlement Charged	Status

THIS VETERAN'S BASIC ENTITLEMENT IS $36,000*
TOTAL ENTITLEMENT CHARGED TO PREVIOUS VA LOANS IS $0*

he veteran is eligible for the benefits of Chapter 37, Title 38, U.S. Code, subject to any condition(s) cited below. Basic entitlement or veterans who have not previously used home loan benefits is $36,000. Additional entitlement is available for most loans in xcess of $144,000. In such cases, the entitlement amount is 25% of the VA loan limit for the county where the property is located. /A county loan limits are adjusted annually, and the current limits are available at www.benefits.va.gov/homeloans.

INCLUDES –

- Name of Veteran
- Social Security Number
- Branch
- Whether or not exempt from VA Funding Fee (Service-Connected Disability, Purple Heart, Etc…)
- Previous VA loans
- Current VA loans if applicable
- Current entitlement charged
- Current VA disability amount (if applicable)

APPENDIX D – CURRENT VA FUNDING FEE TABLES

CURRENT FUNDING FEE WORKSHEET			
Loan Type	% Down Payment	First Time Use	Subsequent Use
Purchase	0 - 4.99%	2.30%	3.60%
Purchase	5% - 9.99%	1.65%	1.65%
Purchase	10% or more	1.40%	1.40%
Cash Out Refinance	N/A	2.30%	3.60%
IRRRL Refinance	N/A	0.50%	0.50%
10%+ Service Connected***	Any	0.00%	0.00%

***REMEMBER – Service-Connected disability, Purple Heart Recipient, and a few other circumstances WAIVES the funding fee forever. This is a potential savings of tens of thousands of dollars over several purchase transactions.

Also – if you APPLY for Service-Connected Disability before you close your loan and disclose it on your application, you can have the funding fee refunded once your VA disability claim is awarded.

APPENDIX E – PRE-APPROVAL WORKSHEET

	Gross Monthly Income	Monthly Debt
Borrower 1:	$______________	$______________
	+	+
Borrower 2:	$______________	$______________
	=	=
TOTALS:	**$ ____________ (A)**	**$____________(B)**

MAX PAYMENT:

$____________ VA = 60% Max DTI

**X $**__________/mo ____(B)$__________ /mo (A)$________/mo

(Gross Income (A) x 60%) – Monthly Debt (B) = Max House Payment (X)

Max House Payment $________________/mo

MAX PRICE:

Every 100K on a VA Loan with zero down payment using CA property taxes, estimated insurance equal to approximately 600 dollars per month PITI.

Approximate Max Purchase Price = Max House Payment (X) divided by 600

The outcome is how much home you can afford in 100,000's…

Approximate Max Home Price = $______________________

For illustration purposes only

SECTON IV – USEFUL TERMS AND DEFINITIONS

A

Adjustable-Rate Mortgage (ARM)

These are mortgages where the interest rates can fluctuate based on what's happening in the greater economic landscape. Most ARMs allow for an annual rate change based on the one-year Treasury bill index.

Appraisal

Mortgage appraisals help determine the fair market value of a property by comparing it to nearby homes that have sold recently. The VA Appraisal also aims to help ensure veterans are purchasing homes that are safe, structurally sound and sanitary. To that end, VA appraisers also look at a broad range of property condition guidelines, known as the Minimum Property Requirements. Lenders can also have their own property condition guidelines. The VA appraisal is not as in-depth as a home inspection and should not be considered a substitute for one. A Home Inspection is also recommended, as it can provide a more thorough look at a property’s structural integrity and major systems.

Annual Percentage Rate (APR)

This rate reflects the total cost of borrowing money, including the interest rate and other costs built into the loan amount. The interest rate and the APR are typically different, and veterans should look at both when comparing VA lenders. Two loans can have similar interest rates, but the one with a higher APR will cost more. Buyers should also understand that lenders can calculate this figure differently, so it's always best to look at actual fees and rate together when considering a loan.

Automated Underwriting System (AUS)

Mortgage lenders often use a computer system to help immediately assess a borrower's suitability for a home loan. These automated underwriting systems evaluate a borrower's credit, finances and more. Getting approval from one of these systems can help veterans move through the loan process faster and with more flexible requirements.

B

Basic Allowance for Housing (BAH)

BAH is a monthly allowance to help qualified active duty service members cover housing expenses. Mortgage lenders can count BAH as effective income toward qualifying for a mortgage. Housing allowances can help defray or entirely cover monthly mortgage payments.

Buyer's Agent

This is the real estate agent who represents the homebuyer.

C

Cash-Out Refinance

This refinance loan allows qualified veterans to refinance and take out cash from the equity in their home. Borrowers can typically look to refinance up to 90 percent of their home's value. Underwriting guidelines for a VA Cash Out Refinance can vary by lender and the borrower's individual circumstances.

Certificate of Eligibility

This is a formal VA document that says whether a prospective borrower is eligible for a VA home loan. You do not need to have your COE in hand to start the loan process. In fact, lenders can often get it for you once you've kick-started your homebuying journey. But borrowers will need a COE before they can close on their loan and it’s recommended to have one at pre-approval so that eligibility can be verified.

Clear to Close

This stage of the loan process means that most major loan conditions have been satisfied and the borrower is ready to close on the home purchase. Buyers will typically still have conditions on the loan that need to be satisfied after getting their clear to close, but these are typically more basic and procedural. Borrowers should continue to maintain healthy financial habits and avoid taking on new debt after receiving a clear to close.

Closing Costs

These are costs and fees associated with obtaining a home loan to purchase real estate.

Comparable Sales

They're better known as "comps." These are recently sold properties that are similar in size, location and other key facets to a home being purchased. Appraisers will evaluate the fair market value of a property using recent comparable home sales.

Compensating Factors

These are strengths on a loan application that can help offset lender concerns about a borrower's credit or financial weaknesses. Low debt, great credit history and liquidity are all examples. Compensating factors must go above and beyond what would be considered a normal program requirement if they are necessary to qualify.

Conditional Approval

There are multiple stages of the underwriting process and getting a conditional approval on your file is a common initial outcome. This typically means underwriters don't see immediate red flags, but they will need additional documents or information before being able to green light the loan file for closing. Those requests for additional information are known as conditions. A good lender should be able to foresee potential conditions and pre-emptively provide what is needed.

Conforming Loan Limit

Fannie Mae and Freddie Mac can only purchase or guarantee mortgages below what's known as the conforming loan limit. This limit can change every year and is higher in more expensive housing markets. Fannie and Freddie do not purchase or guarantee VA loans, and starting in 2020, VA loan limits are far higher than conventional loan limits if the veteran has full eligibility.

Construction-to-Permanent Refinance Loan

This allows qualified borrowers to refinance a construction loan into a VA loan. Guidelines and requirements for this type of loan can vary by lender and other factors.

Conventional Loan

These loans feature no government guarantees but adhere to the standards and requirements of government-sponsored enterprises Fannie Mae and Freddie Mac. There's an array of conventional loan products out there, all requiring different down payments, credit scores, mortgage insurance and more.

Credit Score

These reflect a consumer's ability and willingness to repay debt. Credit scores are affected by a variety of factors, including current debt load, past payment history and more. There are dozens and dozens of credit scoring formulas, some of which are unique to the credit bureau and the type of credit being issued.

VA does not require a minimum credit score, but lenders typically will – generally 580 at minimum.

Closing Disclosure

This five-page form shows buyers the final details of their home purchase, including costs and fees. Buyers should receive the Closing Disclosure at least three business days before their loan closing. You can compare it to the Loan Estimate you received earlier in the mortgage process to see how costs and fees might have changed. Talk with your loan officer if you have any questions about your Closing Disclosure.

D

DD-214

This Defense Department document is also known as the Certificate of Release or Discharge from Active Duty. The DD-214 typically allows Regular Military veterans to verify their service history for benefits and helps qualified borrowers obtain their Certificate of Eligibility. Reservists and National Guard members don't have a single discharge certificate like the DD-214. They'll often need to provide their latest annual retirement points summary along with evidence of their honorable service to establish eligibility for VA loan benefits.

Debt-to-Income Ratio (DTI)

This is a ratio of your major monthly debt payments to your gross monthly income. Lenders look at debt-to-income ratio as a way to help assess your purchasing power and what you can afford. There are two types of DTI ratio calculations in mortgage lending, a front-end ratio that looks at the new mortgage payment in relation to gross monthly income; and a back-end ratio that considers all major monthly debts, including the new payment. VA lending considers only the back-end ratio.

Caps on DTI ratio can vary by lender and other factors. VA buyers whose DTI ratio exceeds 41 percent need to meet a higher threshold for residual income.

Discount Points

Borrowers pay these to essentially buy a lower interest rate. A point is equal to 1 percent of the loan amount. Lenders might quote interest rates with and without points, so be sure to double check rates AND points when comparing offers from multiple lenders. Paying points has to make sense and online lenders tend to quote low rates and hide points in the small print.

E

Earnest Money

This good-faith deposit is typically made as a buyer gets under contract and shows sellers that they're serious about completing the purchase. There's no set amount for an earnest money deposit, and real estate agents are a good guide for what's common in a given market and price range. These funds are held by a neutral third party and can be applied towards a down payment and/or closing costs. The purchase contract will stipulate how the earnest money can be forfeited or refunded. VA buyers have an additional protection known as the VA Amendatory Clause, which allows buyers to keep their earnest money if they walk away from a deal because of a low appraisal.

Entitlement

The VA uses the word to mean the amount of money it will guarantee on a given loan. VA Loan Entitlement helps buyers determine how much of a down payment will be necessary, if any. There are two layers of entitlement: A basic level and a secondary or second tier that varies depending on the current VA loan limits.

Entitlement isn't clearly reflected or explained on the Certificate of Eligibility, and a trusted lender can help you assess your entitlement situation and what might be possible.

F

FICO Score

FICO stands for Fair Isaac Corp., a California-based company that created the first-ever credit score. FICO scores continue to be the most common among mortgage lenders and run from 300 to 850. There are dozens upon dozens of different scoring models, and they vary in part by the type of credit you're seeking.

That's one reason why the informational scores consumers might see from credit monitoring services are often different than the mortgage credit scores lenders see when they pull your credit. Policies and guidelines can vary based the lender, the loan size and other factors.

Fixed-Rate Mortgage

Your interest rate cannot fluctuate on a fixed-rate mortgage. Borrowers with this type of loan will have the same principal and interest payments for the life of the loan. The most common fixed-rate terms are 15 years and 30 years, but there are other options available depending on the lender and their offerings.

Float

Once VA buyers get under contract, they need to decide whether to lock their interest rate in place or float, meaning they will wait to see if VA mortgage rates go down as their loan closing nears. Prospective buyers can't typically lock their rate until they're under contract to purchase a home. Your loan officer can help you evaluate the pros and cons of locking. Every buyer's situation is different, and some have more tolerance for risk than others.

Foreclosure

This basically means the lender takes back the home because you failed to keep up with mortgage payments. Some states require foreclosures to go through the court system, while others do not. There are multiple forms and offshoots of foreclosure, including a deed-in-lieu of foreclosure and a short sale. There are restrictions on foreclosures against active duty service members through the Servicemembers Civil Relief Act (SCRA). Foreclosure can hurt your credit score, and you'll typically need to be two years removed from a previous foreclosure to secure a new VA loan.

Funding Fee

The VA Funding Fee is charged by the Department of Veterans Affairs to help keep the VA loan program running for future generations of military homebuyers. This is the only closing cost on a VA purchase that can be financed on top of the loan. The fee varies based on a borrower's service history and down payment, but it's typically 2.30 percent for most first-time buyers. Borrowers who receive compensation for a service-connected disability are exempt from paying this fee. This fee goes directly to the VA, not to mortgage lenders.

G

Government-Sponsored Enterprises (GSEs)

These are federal financial services corporations, with Fannie Mae and Freddie Mac being the most familiar. Fannie Mae securitizes mortgages in the “secondary mortgage market”. Freddie Mac purchases, pools and sells mortgages to investors. Fannie and Freddie don't purchase VA mortgages. But VA loan limits can be tied to the conforming loan limit, which is a cap above which Fannie and Freddie cannot purchase mortgages. These limits can change annually, and they're higher in more expensive parts of the country. “Ginnie Mae” (GNMA) is a GSE that purchases government loans like FHA and VA on the secondary mortgage market.

Guaranty

This is essentially a form of insurance that the VA provides to lenders. The VA loan program promises to repay lenders a portion of the loan if a borrower defaults. The VA guaranty helps give lenders the confidence to make $0 down loans along with a host of other important benefits.

H

Homeowners Insurance

Lenders require borrowers to secure a homeowner’s insurance policy to cover their home in the case of fire or damage. You might also hear this called "hazard insurance." You'll typically need to pay your first year's homeowners insurance premium at closing. Buyers will usually pay a portion of their annual premiums each month as part of their overall mortgage payment with the lender or servicer escrowing the funds and paying the bill on your behalf. Buyers can shop around for homeowner’s insurance.

Hybrid Adjustable-Rate Mortgage (ARM)

This combines elements of both fixed- and adjustable-rate mortgages, which is why it's called a "hybrid." A hybrid ARM will start with a fixed interest rate for a set number of years, often three or five, before reverting to an adjustable-rate loan for the remainder of the term. This is typically used more strategically when it is probable that the loan will be paid in full or refinanced prior to the start of the adjustment periods. ARM's are generally not used for first time buyers, or buyers who are not very comfortable with lending concepts.

I

Inspection

Buying a home can feature multiple types of inspections. Home Inspections are the most common. These aren't required for a VA loan, but they're your best chance to identify any issues with a home before you sign on the dotted line. The VA appraisal includes a broad look at a property conditions, but it is not a substitute for a home inspection. For homebuyers with an inspection contingency in their purchase contract, the home inspection acts as an important negotiating tool in the event a home needs repair. Some properties may need additional inspections, including ones for drinking water supplies, septic systems, pests and more.

Interest Rate

This is the cost of borrowing money. The interest rate on your loan is expressed as a percentage, and rates can vary widely depending on market conditions, the size of the loan, credit score and more. The VA does not set an interest rate. You might also hear this referred to as the "note rate," which helps differentiate it from the loan's Annual Percentage Rate (APR).

VA loans continue to have the lowest average fixed interest rate on the market.

Interest Rate Reduction Refinance Loan (IRRRL)

This is also known as a VA Streamline Refinance. This is a refinance with reduced costs and documentation requirements designed to get veterans into a lower-rate mortgage or out of an adjustable-rate loan. The IRRRL is open only to veterans who currently have VA loans. Borrowers cannot take cash out with an IRRRL. Some lenders may not need an appraisal or even require a minimum credit score requirement. Guidelines and policies can vary. Unlike other VA loans, this requires only prior occupancy, meaning the veteran doesn't need to intend to occupy the home that's being refinanced.

J

Jumbo Loan

Generally, these are loans above what's known as the conforming loan limit. Jumbo VA Loans typically feature tighter requirements than a traditional VA loan, but they still offer some tremendous benefits compared to conventional jumbo loans. Some jumbo VA loans can be had without a down payment, while others will require one -- every buyer's situation is different. But even buyers who need to put money down often need smaller down payments for jumbo VA loans compared to their conventional counterparts and Jumbo VA loans still generally have lower rates and require no monthly mortgage insurance.

L

Lender Appraisal Processing Program (LAPP)
This computer system allows authorized lenders to directly order and process VA appraisals, which are conducted by independent VA-approved appraisers.

Leave and Earnings Statement
This is basically the Verification of Employment document for active duty service members.

Listing Agent
This is the real estate agent representing a home seller.

Loan Estimate
Within three business days of receiving a complete loan application, lenders are required to send you this three-page form that contains key initial information

about your new loan, including the interest rate, your monthly mortgage payment, and costs and fees required to close. Borrowers can compare this to the Closing Disclosure they receive as they near their loan closing. Unlike the Closing Disclosure, the Loan Estimate features estimated costs.

Loan Officer

An individual who is licensed by the Nationwide Mortgage Licensing System (NMLS) and can legally "originate" a loan. Licensing is relatively easy, so it is important that you find a good Loan Officer, since they are responsible for navigating the loan process. For VA loans, it is really important to find a loan officer who specializes in working with Veterans and Military Families, as VA loans have special features which should be discussed.

Loan Processor

This person pulls together outstanding documents and information once a borrower has signed a purchase contact. Their job is to piece together loan applications for an underwriter.

M

Manual Underwriting

Lenders will typically input a prospective borrower's information into an automated underwriting system that can generate an immediate green light, indicating there are no major red flags and the veteran can

proceed to the next step. In some cases, loan files do not meet this initial underwriting approval, at which point they might be subject to what's known as manual underwriting.
Manual underwrites usually mean tougher lending requirements and a closer look from underwriters earlier in the process. But they're also not uncommon, and plenty of borrowers who encounter manual underwriting go on to close on their loan.

Minimum Property Requirements
These are broad health and safety conditions that a property must meet to satisfy the VA. Independent VA appraisers will assess the property in light of the minimum property requirements during their time at the home. Any repair issues noted by the appraiser will often need to be addressed before the loan can close. Home sellers and even VA buyers can pay for repairs to keep the loan moving forward. Generally, the VA wants veterans purchasing homes that are move-in ready, but an appraisal that turns up MPR issues does not mean your purchase is automatically in jeopardy. Repairs are often negotiated with sellers, but every situation is different.

Multiple Listing Service (MLS)
Real estate databases and software that allow agents and brokers to look at transactions, post home listings and access a suite of other property information and tools. There are dozens of MLS databases spread across the country. Home sellers typically need to

work through a real estate agent to get their home posted to an MLS.

N

Negative Compensating Factor

Compensating factors are strengths on a loan application that can help borrowers secure a loan. Negative compensating factors can do the opposite. Bankruptcies, foreclosures, late payments can all be considered negative compensating factors.

Note Rate

This is another term for your interest rate, which is different from your Annual Percentage Rate (APR), which includes additional costs related to your transaction. The note rate reflects the cost of borrowing money from the mortgage lender.

Notice of Value (NOV)

This is the final determination of a property's fair market value based on the VA appraisal. The appraised value of the home comes from an independent appraiser's comparison of the home to recent comparable home sales. If the home's appraised value comes in below the purchase price, buyers will need to renegotiate with the seller or walk away from the deal. Renegotiation is common, but veterans who walk away will get their earnest money back because of what's known as the VA Amendatory

Clause, which protects buyers in the event of a low appraisal.

O

Origination Fee

Some lenders charge up to 1 percent of the loan amount to cover in-house costs and services, such as originating, processing and underwriting the loan. A 1 percent fee on a $250,000 loan is $2,500. Lenders also have the option to skip the flat fee and charge an array of fees to cover overhead, so long as their total cost doesn't exceed 1 percent of the loan amount. VA buyers can ask sellers to pay all of their loan-related closing costs (including the origination fee) and up to 4 percent in concessions, which can cover things like prepaid taxes and insurance and much more. The Lehman Group does not charge origination fees.

P

Permanent Buydown

Veterans can pay money upfront to essentially purchase a lower interest rate for the life of the loan. You'll pay in the form of what are called points, where 1 point is equal to 1 percent of the loan amount. The VA allows veterans to pay reasonable points to buy down their rate, typically not to exceed 2 points.

PITI

The acronym stands for Principal, Interest, Taxes and Insurance. These are the four pillars of a veteran's monthly mortgage payment. The Principal and Interest portions of your payment will not change on a fixed-rate loan. Lenders also collect for Taxes and Insurance – holding the funds in an "impound account" (also called an escrow account) to be paid when tax/insurance bills come due.

Power of Attorney

A surrogate with power of attorney can sign contracts and other documents on behalf of an absent service member. Many lenders require a unique power of attorney document. Talk with lenders about their guidelines given your specific situation. This helps when a servicemember deploys and the spouse is interested in purchasing a home while the servicemember is not available to sign loan documents.

Preapproval

This is a more serious step than prequalification and involves a lender verifying key information about your debts and income. VA loan pre-approval gives you a clear sense of your buying power, and it shows real estate agents and home sellers you're a strong and serious homebuying candidate. Getting preapproved doesn't obligate you to any particular lender or to purchasing a home, and it is not a guarantee of financing. But it is the first big milestone of the VA purchasing process. Most good lenders will do an educational rundown of qualifications at the time of pre-approval.

Prequalification

This introductory step is often mostly just a conversation with a loan specialist about your service history, your employment and finances, and your homebuying goals that ends with a look at your mortgage credit scores. VA loan pre-qualification doesn't usually involve much verification of information beyond your credit score, and so it holds little weight with home sellers and real estate agents, who are looking for buyers with loan preapproval. It is a good idea to move on to full pre-approval when you are serious about purchasing a home. Most sellers and good real estate agents will require full pre-approval to consider offers in a way that is taken seriously.

Private Mortgage Insurance (PMI)

On most conventional mortgages, borrowers who can't put down 20 percent of the loan amount are required to pay this form of insurance. PMI protects lenders against borrowers who default and also helps borrowers who can't muster a large down payment. PMI typically ends once the homeowner's loan-to-value ratio reaches about 80 percent.

There is no PMI on a VA loan, which can boost your buying power and save veterans tens of thousands over the life of the loan.

Q

Qualified

Different from "entitlement"- which veterans earn through service, a borrower is qualified by verifying credit, income and assets are sufficient to acquire a loan to finance a home.

R

Rate Lock

A binding commitment that locks a borrower to a specific interest rate. Borrowers can typically lock their interest rate as soon as they sign a purchase agreement and up to five days before the loan closing. Rate locks are good for specific blocks of time. The most common lock periods are for 15 days, 30 days, 45 days and 60 days. Longer locks cost more so it is important to work with a lender who can advise according to your plan.

Realtor

A real estate agent who is a member of the National Association of Realtors.

Refinance

A loan that replaces an existing mortgage to finance at a lower interest rate and/or take out cash. The most common reason for refinancing is to take advantage of interest rates lower than when the loan was originally made. The VA has two primary refinance options. One is the Interest Rate Reduction Refinance Loan (IRRRL), which is available only to current VA loan holders. Veterans can use this to refinance into a lower-rate mortgage or out of an adjustable-rate loan. The other is the VA Cash Out Refinance. This allows qualified homeowners to refinance and extract cash from their equity, regardless of whether their current loan is backed by the VA.

Reserves

Some borrowers might need a set amount of cash reserves in the bank to close on their VA loan. Reserves are often expressed in terms of a certain number of months' worth of mortgage payments. Cash reserves aren't a common requirement for VA loans, but they can also be a compensating factor that strengthens your loan file.

Residual Income

This is a lending standard unique to VA loans. Residual income is the amount of money a borrower has left over each month after covering all their major monthly debts and obligations. The VA wants to see veterans have a minimum amount residual income, which can vary depending on the size of your family and where in the country you're buying.

RESPA

This stands for Real Estate Settlement and Procedures Act, a 1974 law that increased transparency and disclosures involving the home-buying process. The loan application paperwork is sometimes lumped together as RESPA documents or RESPA packets. Lenders have three days to send you the paperwork once they've pulled your credit.

S

Seller Concessions

The VA allows sellers to pay all of a buyer's loan-related closing costs and up to 4 percent in what are known as seller concessions. Concessions can cover a wide range of expenses and fees, including paying the portion of a buyer's property taxes and homeowner’s insurance due at closing; paying off a buyer's collections and judgments; and more. Home sellers are not required to anything on behalf of a VA buyer, but every purchase and negotiation is different.

Staff Appraisal Reviewer (SAR)

A lender's staff appraisal reviewer, or SAR, examines a property's independent VA appraisal and issues the final Notice of Value.

Second-Tier Entitlement

Eligible veterans have two layers of VA loan entitlement, which reflects the government's guaranty on the loan. Veterans have a basic entitlement, and a second tier of entitlement that helps boost their zero-down buying power. The amount of this second layer of entitlement can vary depending on where in the country you're buying and your previous history with the VA loan program. Second-tier entitlement is how veterans can have multiple VA loans at the same time or purchase again after losing one to default.

Secondary Mortgage Market

Lenders sell mortgages, often packaged into mortgage-backed securities, in this marketplace. Private investors and government-sponsored enterprises like Fannie Mae and Freddie Mac buy loans in the secondary market.

Short Sale

On the selling side, this is an alternative to straightforward foreclosure. This is when the bank agrees to let you sell your home for less than it's worth. A short sale will negatively affect your credit score. Veterans who lose a home to short sale will lose whatever VA loan entitlement they utilized on the property, but they might have little trouble purchasing again using second-tier entitlement. On the buying side, it is when you purchase a home from someone who is selling for less than is owed. Although it can be a bit of a longer process – due to the seller’s lender requiring approval, the loan process is very similar for the buyer. VA loans can be used to purchase short sales, foreclosures, and any other distressed properties as long as they meet minimum property standards.

Special Adapted Housing (SAH)

The VA has a few specialized housing grant programs for veterans with disabilities. These grants help qualified veterans to purchase or build an adapted home or to make modifications to an existing home. The two primary programs are the Specially Adapted Housing (SAH) grant and the Special Housing Adaptation (SHA) grant, and maximum funding for these can change every year.

Streamline

A VA Streamline is another name for the Interest Rate Reduction Refinance Loan (IRRRL). The nickname comes because these are designed as a swift, low-paperwork way to get qualified veterans into lower-cost loans or out of adjustable-rate mortgages.

Subprime

This essentially means borrowers or loans below an accepted credit standard, typically around 620. Subprime borrowers carry greater risks and now have trouble securing financing. VA loans are not considered Subprime loans.

T

Title Insurance

This form of insurance protects borrowers, sellers and lenders against previous ownership claims on a property and other possible issues related to the property's chain of ownership. There are two types of title insurance, one for lenders and the other for buyers. Lenders will require a lender's policy, and buyers typically obtain their own, too. Title insurance must be paid at closing. In many markets, the buyer's policy is paid for by the seller of the home.

U

Underwriter

These trained experts review a borrower's loan file and give an ultimate thumbs-up or down. They act as the lender's gatekeeper. Prospective buyers should expect to have some basic requests from underwriters once they're under contract, but a good lender is like a good attorney if the underwriter is the equivalent of the judge. It's incredibly uncommon for loans to just sail through without conditions, but they should be manageable in most cases with proper planning. Generally, the faster you respond to questions and requests for additional information, the faster you move toward closing day.

Uniform Residential Loan Application

This is the five-page loan application for almost all home mortgages.

V

Verification of Employment

This is an important document that lenders send to a veteran's employer(s). The VOE, as it's known, helps lenders verify employment, tenure, salary and any bonuses or raises.

Z

Zero Money Down

A type of loan where the borrower isn't required to pay a down payment. The VA Loan is one of the two remaining major loan programs that offer the advantage of no money down. Conventional Loans typically require at least a 5 percent down payment, with FHA loans requiring a minimum 3.5 percent. Despite the zero-down benefit, VA loans have had the lowest foreclosure rate on the market for most of the last decade. That's a testament to the program's sound underwriting guidelines and its commitment to helping veterans purchase and keep their homes.