Glossary & Terms

ACRONYMS

AMI: Area median income

ARM: Adjustable-rate mortgage

AUS: Automated underwriting system

BEA: Bank Enterprise Awards (U.S. Department of the Treasury)

BIA: Bureau of Indian Affairs

CAM: Customer Account Manager (Fannie Mae)

CDFI: Community Development Financial Institution

CDFI Fund: Community Development Financial Institutions Fund (U.S. Department of the Treasury)

CMF: Capital Magnet Fund (U.S. Department of the Treasury)

CRA: Community Reinvestment Act

DTI: Debt-to-income ratio

DU: Desktop Underwriter® (Fannie Mae)

FDIC: Federal Deposit Insurance Corporation

FHA: Federal Housing Administration

FHFA: Federal Housing Finance Agency

FHLBanks: Federal Home Loan Banks

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

HARP: Home Affordable Refinance Program

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

LLPA: Loan-level price adjustment

LTV: Loan to value

MBS: Mortgage-backed security

MOU: Memorandum of understanding

OCC: Office of the Comptroller of the Currency (U.S. Department of the Treasury)

PFIs: Participating Financial Institutions (FHLBanks)

PMI: Private mortgage insurance

REO: Real estate owned

UFMIP: Upfront mortgage insurance premium

USDA: U.S. Department of Agriculture

VA: U.S. Department of Veterans Affairs

TERMS

Adjustable-rate mortgage (ARM): A mortgage loan with an interest rate on the note that is periodically adjusted based on an index that reflects the cost to the lender of borrowing on the credit markets. Most ARMs permitted in programs covered in this Guide are hybrid ARMs that have an initial fixed-rate period; the periodic adjustments begin at the end of the fixed period. ARMs may have restrictions, or cap rates, on the amount of the first, periodic, and lifetime total changes in the interest rate.

Aggregator: An entity that purchases mortgages from loan originators and typically securitizes them into mortgage-backed securities that are then sold to the secondary mortgage market.

Appraisal: A valuation of real estate by an authorized person who observes, analyzes, and reports the physical and economic characteristics of the property. The estimate is limited to readily observable conditions; the observations on which it is based are not as comprehensive as a licensed home inspection.

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

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

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

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

Base loan-to-value ratio: The loan-to-value (LTV) ratio calculated using the mortgage amount excluding the financed mortgage insurance premium. (This is in contrast to the gross LTV ratio, which includes the mortgage amount and financed mortgage insurance premium.) Fannie Mae and Freddie Mac use the base LTV ratio to determine the mortgage insurance coverage amount.

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

Buy-down funds: Funds offered by the seller of the property, typically a builder or developer, to the buyer to lower the interest rate in the early years of the loan.

Cash-out refinance: A refinance transaction in which the new mortgage amount is greater than the existing mortgage plus loan settlement costs. The borrower receives a cash payment for the difference between the two mortgage amounts minus any settlement costs not paid out of pocket. (See also Limited cash-out refinance.)

CDFI Fund distressed community: The CDFI Fund defines distressed communities based on geographic and economic criteria. At least 30 percent of the eligible residents must have incomes less than the national poverty level, and the unemployment rate must be at least 1.5 times greater than the national average. The area must have a population of at least 4,000 if within a Metropolitan Statistical Area (MSA). If not in an MSA, it must have a population of at least 1,000. Alternatively, the area must be located entirely within an Indian Reservation.

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

Chattel loan: Chattel refers to moveable property. Manufactured homes titled as personal property are financed through loans on personal property known as chattel loans. The lender holds a lien against the manufactured home only, the land is not encumbered.

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

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

Community land trust (CLT): A nonprofit housing development organization that acquires parcels of land (with or without housing on the parcel) and holds them in perpetuity primarily under long-term ground leases to provide permanently affordable housing opportunities for low- and moderate-income families and communities. At the time of purchase, the owner of a CLT property agrees to sell the home at a resale-restricted and affordable price to another lower-income homebuyer in the future. The nonprofit board is governed by CLT residents, community residents, and public representatives.

Conforming loan: A conventional mortgage loan that has an original loan amount not exceeding the government-sponsored enterprise (GSE) conforming loan limit at the time a GSE purchased or securitized the mortgage. The GSEs are restricted by law to purchasing mortgages with origination balances below a specific amount, known as the conforming loan limit. In addition to size limits, the conforming loan must meet the GSE's underwriting and documentation standards.

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

Correspondent lender: A lending institution that originates and funds loans in its own name and then sells them to another lender or investor. The underwriting function in a correspondence relationship can be carried out by the correspondent or the investor. As a correspondent lender, the originating lender is acting as an extension of the investor. For example, correspondent lenders work with approved seller/servicers to originate government-sponsored enterprise loan products.

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

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

Discount points: Prepaid interest that borrowers can pay at loan origination to lower the amount of interest they have to pay in the future. Each discount point costs 1 percent of total loan amount and lowers the interest rate by 1/8 to 1/4 percentage point. Lenders benefit by receiving cash up front instead of waiting for it in future interest payments.

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

Equity investment: Investment capital is used to buy or hold shares of a company. In the case of a nonprofit entity, "unrestricted net assets" on the balance sheet are the equivalent of equity. The major feature of equity — in contrast to debt — is that there is no obligation on the part of the firm to repay the investment or use it for specific purposes or, usually, to pay interest on it.

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

Extended buy down: The lender offers the borrower an initial interest rate that is lower than the note rate by up to 3 percentage points. The interest rate is then increased by no more than 1 percentage point annually for more than two but no more than three years. This gives the borrower lower initial payments and the stability of predictable payment increases.

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

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

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

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

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

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

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

Guaranteed Underwriting System (GUS): The automated underwriting system used by the U.S. Department of Agriculture (USDA). It is optional at the time of this writing, but USDA expects to continue development and eventually make it required. Otherwise, loans for USDA programs are underwritten manually.

Homeownership Center (HOC): The U.S. Department of Housing and Urban Development (HUD) centralizes many of the mortgage-insuring processes into four HOCs that each supports a specific geographic area. Each HOC insures single-family Federal Housing Administration (FHA) mortgages, assures FHA mortgage quality, and oversees the selling of HUD homes for the states in its jurisdiction. The four HOCs are in Atlanta, Philadelphia, Denver, and Santa Ana.

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

Hybrid adjustable-rate mortgages: A mortgage that blends characteristics of fixed- and adjustable-rate mortgages. The mortgage has an initial fixed interest rate. At the end of the fixed-rate period (the "reset date"), the interest rate adjusts based on an index plus a margin. These mortgages are often advertised as 3/1 or 5/1 ARMs: the first number indicates how long the fixed-rate period is and the second number indicates the frequency with which the rate may subsequently be adjusted. For example, a 3/1 ARM has a three-year, fixed-rate period after which its rate may be adjusted annually.

Interest Rate Reduction Refinancing Loan (IRRRL): A loan made to refinance an existing U.S. Department of Veterans Affairs (VA) loan. Refinancing to a lower interest rate means the borrower's monthly payment will decrease. The borrower can also choose to refinance an adjustable-rate mortgage to a fixed-rate loan.

Investing lender: A financial institution, including a charitable or nonprofit organization or pension fund, that is approved by the Federal Housing Administration (FHA) to purchase, hold, or sell FHA-insured mortgages. This mortgagee type may only service FHA-insured mortgages if it receives prior approval to do so on a case-by-case basis, and cannot originate or fund FHA loans.

Land-lease community: Residential land-lease permits a tenant to use a piece of land owned by the landlord in exchange for rent. Land leases are almost exclusively used for manufactured home communities," with the exception of land leases known as ground rents that are used for site-built properties in certain states.

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

LIBOR: Short for London Interbank Offered Rate. A benchmark interest rate that banks use to charge each other for short-term loans. Based on five currencies — the U.S. dollar, Euro, pound sterling, Japanese yen, and Swiss franc — it serves seven different maturities: overnight, one week, and 1, 2, 3, 6, and 12 months. LIBOR is scheduled to be phased out by 2021.

Limited buy down: The lender offers the borrower an initial interest rate that is no more than 2 percentage points below the note rate and is increased by no more than 1 percentage point annually for no more than two years. This option is a good fit for borrowers who have the capacity for higher earnings within a few years of obtaining a mortgage. It gives the borrower lower initial payments and the stability of predictable payment increases. Fannie Mae and Freddie Mac specify when this practice is acceptable, and it varies by program. (See also Extended buy-down.)

Limited cash-out refinance: A refinance transaction in which the mortgage amount generally is limited to the sum of the unpaid principal balance of the existing first mortgage, closing costs (including prepaid items), points, and the amount required to satisfy any mortgage liens if the documented proceeds of the subordinate financing were solely used to acquire the property if the borrower chooses to satisfy them, and other funds for the borrower's use as long as the amount does not exceed the lesser of $2,000 or 2 percent of the principal amount of the new mortgage. This definition applies to Fannie Mae mortgage programs. (See also Cash-out refinance.)

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

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

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

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

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

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

Mortgage broker: A company that matches borrowers and lenders and charges a commission for the service. A mortgage broker typically takes the borrower's application and sometimes processes the loan. Unlike a mortgage lender, a mortgage broker does not use its own funds to close the loan.

Mortgage insurance: An insurance policy paid for by the borrower to cover the government insurer's (FHA, VA or USDA) cost of insuring the loan against losses. In the event of foreclosure, the insurer pays a set amount to the lender to cover some or all of the outstanding loan balance. Mortgage insurance should be distinguished from hazard insurance, which a homeowner purchases to cover losses from, for example, fire or theft.

Mortgage insurance premium (MIP): The term used for mortgage insurance payments on a Federal Housing Administration loan. On an FHA 203(b) loan, borrowers are assessed an upfront mortgage insurance premium (UFMIP) that is typically included in the loan amount as well as an annual MIP that is paid out in monthly installments throughout the life of the loan.

Mutual Mortgage Insurance Fund (MMIF): Federal Housing Administration (FHA) approved lenders are protected by the Mutual Mortgage Insurance Fund in the event a borrower defaults. The MMIF is financed through the premiums paid by mortgage borrowers for FHA mortgage insurance.

Non-supervised lender: This term is used in the context of the FHA program to refer to a lending institution — but not an insured depository — that has as its principal activity the lending or investing of funds in mortgages, consumer installment notes, or similar advances of credit, or the purchasing of consumer installment contracts. Such lenders can be approved as Federal Housing Administration (FHA) lenders to originate, underwrite, close, endorse, service, purchase, hold, or sell FHA-insured mortgages.

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

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

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

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

Sponsor: For the Federal Housing Administration, a sponsor or sponsored third-party originator relationship is one in which a lender (acting as the sponsor) permits another entity to originate mortgages on the lender's behalf. The sponsor may then buy the loan upon closing. Sponsors must have direct endorsement authority.

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

Supervised lender: For the Federal Housing Administration (FHA), a financial institution that is a member of the Federal Reserve System or whose accounts are insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration. A supervised lender may originate, underwrite, close, endorse, service, purchase, hold, or sell FHA-insured mortgages.

Temporary interest rate buy down: A mortgage option to lower the interest rate of the loan from the note rate by a decreasing amount for a defined period. A typical buy down, written as a 3-2-1, would reduce the interest rate by 3 percent in the first year, 2 percent in the second year, and 1 percent in the third year. (See also Extended buy down.)

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