Lending Rules Changing for People Who Lost Their Homes in the Great Recession

September 9, 2013 - Over the past week, there have been some important lending announcements from Fannie Mae and the FHA concerning anyone who lost their home in a short sale or foreclosure in the last few years. These changes will make it easier for millions of people in this position to purchase another home. But these buyers may have to jump through a few hoops to prove that they qualify for the new standards. More importantly, even those who do qualify would be well served to do some self-examination before borrowing to make sure that home-ownership is really financially feasible over the long haul.

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Until last week, FHA rules stated that borrowers would have to wait three years after a foreclosure or two years after a bankruptcy filing before they could obtain a new mortgage again. The only two exceptions to the rule were foreclosure or bankruptcy filings due to the death of a spouse or a medical emergency. Anyone qualifying for one of these exceptions only had to wait one year to become eligible to borrow again.

Early last week, the FHA announced a new exception to the rules: Borrowers whose income unexpectedly dropped by at least 20% or who lost their jobs. The new exception does not cover borrower who voluntarily resigned from their positions or who were fired "for cause".

Later in the week, Fannie Mae announced a lending policy change for people who sold their homes using a short sale. A short sale occurs when the homeowner sells their property for less money than they owe on it. These sales require the lender's approval.

Although Fannie Mae technically allowed borrowers to qualify for a new mortgage in less than seven years after a short sale, many borrowers haven't been able to qualify. The reason is that the credit bureaus don't distinguish between a short sale and a foreclosure. This means that many homeowners who sold their properties via a short sale have credit records that report the transaction as a foreclosure. And in most circumstances, if you have a foreclosure on your credit record you will need to wait seven years before you can get a new mortgage.

The new rule, which is really more of a document fix, allows prospective borrowers to notify their loan officer if a foreclosure is erroneously shown on their credit report. Although the credit reporting agencies still don't have an ability to differentiate between a short sale and a foreclosure, Fannie Mae now allows loan officers to make this correction with an explanation at the time the loan application is submitted. Any borrower using the new fix will be required to put 20% down on their new home.

These new rules have the potential to impact millions of Americans who struggled with home ownership during the recession. Whether that impact is positive or not really depends on borrowers' individual circumstances.

Anyone who lost their home in a foreclosure or was forced to sell using a short sale should probably take stock of their current financial circumstances before attempting to purchase a new home. There is quite a bit of economic evidence at this point that some housing markets in the United States are overheated and could go through another drop in prices. And while the most recent unemployment numbers released last Friday appear to be good news at first glance, a closer look tells a little different story. The latest unemployment rate reported by the government is 7.5%. That appears to be a significant drop until you realize that the actual reason for the low number is largely because many people have simply stopped looking for work. These "discouraged workers" are still unemployed but the government doesn't include them in their numbers. When they are included along with underemployed workers, the actual unemployment rate jumps to 13.7%.

What this means is that although many consumers are currently feeling better about the economy, the underlying economic data indicate that the so-called "recovery" is anemic at best, and many not be sustainable over the long term. That should be of great concern to anyone considering taking on large debtsâ€¦ inclusive of a home mortgage.
byJim Malmberg
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