Home Purchase Loan Program

Offers zero down payment guaranteed loans to service members, veterans, and surviving spouses

BACKGROUND AND PURPOSE

The U.S. Department of Veterans Affairs (VA) helps service members, veterans, and eligible surviving spouses become homeowners by providing a home loan guaranty benefit. VA loans are provided by private lenders, such as banks and mortgage companies.

Borrower eligibility for VA homeownership programs is determined by meeting minimum standards for length of service, which is confirmed by VA with a Certificate of Eligibility. Each veteran has a guaranty entitlement, which is a minimum of $36,000 and a maximum of 25 percent of the county loan limit. The guaranty is the amount VA will pay the lender in the event of a foreclosure. The guaranty effectively takes the loan-to-value (LTV) ratio down to 75 percent. The VA Home Purchase Loan program has made mortgage credit available to many veterans who otherwise would not be able to obtain a loan.

BORROWER CRITERIA

Loan limits: VA loan limits vary by county and are currently the same as those set by the Federal Housing Finance Agency (FHFA) for Fannie Mae and Freddie Mac (conforming loan limits). Although VA does not set a cap on how much a veteran can borrow to finance a home purchase, the department will only guarantee 25 percent of the VA loan limit. Therefore, lenders may require veterans to make a down payment on loan amounts that exceed the limits.

Income limits: This program has no income limits.

Credit: VA does not require a minimum credit score for a VA loan, but lenders may set their own requirements.

First-time homebuyers: First-time users of their VA eligibility get a lower funding fee. Generally, all veterans using the VA Home Purchase Loan guaranty pay a funding fee. The funding fee is a percentage of the

PROGRAM NAME	Home Purchase Loan Program
AGENCY	U.S. Department of Veterans Affairs
EXPIRATION DATE	Not Applicable
APPLICATIONS	http://benefits.va.gov/warms/pam26_7.asp
WEB LINK	http://www.benefits.va.gov/homeloans/index.asp
CONTACT INFORMATION	Lenders interested in participating should contact their local VA office, which can be found at http://www.benefits.va.gov/HOMELOANS/contact_rlc_email.asp
APPLICATION PERIOD	Continuous
GEOGRAPHIC SCOPE	National

loan amount that varies based on the type of loan, military category, first-time loan user status, and existence of a down payment. Veterans do not have to pay the fee if they are a:

- veteran receiving VA compensation for a service-connected disability, or
- veteran who would be entitled to receive compensation for a service-connected disability if the veteran did not receive retirement or active duty pay, or
- Surviving spouse of a veteran who died in service or from a service-connected disability.

Occupancy and ownership of other properties: A borrower[5] may only use VA financing for one property at a time, called "entitlement." The borrower must plan to occupy the property as a residence.

Special populations: To obtain a VA loan, the borrower must be a service member or veteran with a Certificate of Eligibility signifying that he or she meets the service requirements. During wartime, 90 days of active service is the minimum amount of service to be eligible; during peacetime, the requirement is 181 days. Military spouses are also eligible under certain criteria when the service member is unable to be the borrower. Officers of certain nonmilitary government agencies and people who served in World War II in certain non-U.S. armed services capacities may also be eligible.

Special assistance for persons with disabilities: The VA provides Housing Grants for Disabled Veterans to service members and veterans with certain permanent and total service-connected disabilities to help purchase or construct an adapted home, or modify an existing home to allow them to live more independently. For example, the Specially Adapted Housing Grant is designed to facilitate independent, barrier-free living for veterans with severely impaired mobility. Another example is the Specially Adapted Housing Assistive Technology Grant, which is designed to adapt the home of a veteran with no mobility-related disabilities.

Tribal Land Loans: Note that VA loans on tribal land are underwritten directly by VA. By statute, before VA may make a loan to any Native American veteran, the veteran's tribal or other sovereign governing body must enter into a Memorandum of Understanding (MOU) with VA. Native American veterans who are eligible for VA home loan benefits and whose sovereign governments have signed an MOU, may then apply directly to VA for a 30-year fixed-rate loan to purchase, build, or

[5] Note that spouses can co-sign on the loan and be included on the deed. In the event that a spouse does not want to co-sign on the loan, the veteran borrower and the non-borrower spouse must sign either the mortgage note or the mortgage deed. VA clarified this in Circular 26-16-01, https://www.benefits.va.gov/HOMELOANS/documents/circulars/26_16_1.pdf

POTENTIAL BENEFITS

VA loans offer competitive pricing and terms.

Community banks, as supervised institutions, receive automatic authority to originate and close loans with the VA guarantee, making VA loans a relatively easy type of mortgage to begin offering.

The VA Home Purchase Loan Program may allow community banks to expand their customer base among veterans in their communities.

Loans originated through VA may receive favorable consideration under the CRA, depending on the geography or income of the participating borrowers.

POTENTIAL CHALLENGES

Despite the ease of becoming a VA-authorized lender, community banks may need to acquire or develop new expertise and infrastructure in order to participate.

Lenders retain some risk since they are responsible for any loss over 25 percent.

improve a home located on federal trust land. They may also refinance a direct loan already made under this program to lower their interest rate.

Property type: The property type may be a house, a condominium unit in a VA-approved project, or a manufactured home and/or lot. If the manufactured home is not placed on a permanent foundation, VA will guarantee 40 percent of the loan amount or the veteran's available entitlement, up to a maximum of $20,000. Up to four residential units and one business unit (which cannot be more than 25 percent of the square footage of the home) is allowed. VA financing may also function as construction financing to build a home, simultaneously purchase and improve a home, or make energy efficiency improvements of up to $6,000.

LOAN CRITERIA

Loan limits: Each veteran has a guaranty entitlement, which is a minimum of $36,000 and a maximum of 25 percent of the county loan limit. The guaranty effectively takes the LTV ratio down to 75 percent. VA has set its loan limits to be the same as the loan limits for Fannie Mae and Freddie Mac single-unit loans. Borrowers may combine their entitlement with a down payment to purchase a property that is over the county loan limit, but such loans would be more limited in their secondary market options.

Loan-to-value limits: A loan-to-value (LTV) ratio of up to 100 percent is allowed. Closing costs may not be financed into the loan. However, it is possible to finance the funding fee and up to $6,000 in energy-efficiency improvements into the loan, in which case the LTV may go over 100 percent. From the lender's perspective, the veteran's entitlement effectively reduces the LTV ratio to 75 percent or less.

Adjustable-rate mortgages: Lenders may make adjustable-rate mortgages with VA guarantees. For traditional ARMs with annual interest rate adjustments or hybrid ARMs with an initial fixed-rate period of under five years, annual interest rate adjustments are limited to plus or minus 1 percentage point, with a maximum of 5 percentage points over the life of the loan. These loans must be underwritten at 1 percentage point above the initial rate. If the initial contract interest rate of a hybrid ARM remains fixed for five years or more, the initial adjustment is limited to a maximum increase or decrease of 2 percentage points, and the interest rate increase over the life of the loan is limited to 6 percentage points.

Down payment sources: Down payments are not required. A discounted funding fee is provided with down payments of 5 percent or more (discounted to 1.5 percent) and 10 percent or more (discounted to 1.25 percent). Lenders may require a down payment if necessary to meet secondary market requirements (such as those imposed by Ginnie Mae); generally, the VA guarantee plus down payment must be at least 25 percent of the loan amount.

Homeownership counseling: Homeownership counseling is not required.

Mortgage insurance: Mortgage insurance is not required.

Debt-to-income ratio: The maximum debt-to-income ratio allowed is 41 percent. However, applicants whose DTI exceed 41 percent can be granted an exception if the borrower qualifies based on residual income. If student loan repayments are scheduled to begin within 12 months of the date of VA loan closing, lenders should consider the anticipated monthly obligation in the loan analysis. If the borrower is able to provide evidence that the debt may be deferred for a period outside that timeframe, the debt need not be considered in the analysis.

Residual income: The VA wants to make sure that veterans have enough money for regular household and family needs after making their housing payment, so they measure a prospective borrower's residual income as well as debt-to-income ratio. Residual income is the amount of net income remaining (after deduction of debts and obligations and monthly shelter expenses) to cover family living expenses such as food, health care, clothing, and gasoline. Residual income does not automatically trigger acceptance or rejection of a loan, but it is considered in conjunction with other credit factors. If the borrower's DTI is more than 41 percent, he or she must exceed the regional residual income requirement by at least 20 percent. Lenders may reduce the residual income requirement by 5 percent for active-duty service members. The residual income threshold varies depending on family size and geographic region. See the VA's underwriting guide, Chapter 4, "Credit Underwriting," for the latest residual income limits.

Temporary interest rate buy downs: Interest rate and points are negotiated between the lender and borrower; temporary interest rate buy downs are allowed.

Refinance: Cash-out refinance is allowed. No cash-out refinance is allowed through the VA's Interest Rate Reduction Refinance Loan program.

Seller concessions: VA limits seller concessions to 4 percent of the loan. Examples are payment of prepaid closing costs, VA funding fee, payoff of credit balances or judgments for the veteran, and funds for temporary buy downs. Payment of discount points is not subject to the 4 percent limit.

Funding fee: Generally, all veterans using the VA Home Loan Guaranty benefit must pay a funding fee. The funding fee is a percentage of the loan amount that varies from 1.25 percent to 3.3 percent 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 or paid in cash at closing. Veterans with a service-connected disability are exempt from the funding fee.

Lender fees: The VA limits the fees lenders can charge borrowers. The veteran can pay a maximum of reasonable and customary amounts for typical closing costs designated by VA, plus a 1 percent flat charge by the lender, plus reasonable discount points. The seller, lender, or any other party may pay any of these fees on behalf of the borrower; however, the VA does not allow excessive seller concessions that place veterans in loans they would not otherwise qualify for because this increases the risk of default.

Appraisals: Prospective borrowers must use an appraiser assigned by VA.

Loss mitigation: VA has favorable terms for veterans who lose their homes to foreclosure, short sale, or deed-in-lieu of foreclosure. In the event of foreclosure, some of the veteran's entitlement will likely stay tied to the foreclosed property. Under most circumstances, borrowers may be able to use the remainder of their entitlement to qualify for a new mortgage. Waiting periods after foreclosure are shorter with VA than with conventional financing.

Potential Benefits

- VA loans offer competitive pricing and terms.
- Community banks, as supervised institutions, receive automatic authority to originate and close loans with the VA guarantee, making VA loans a relatively easy type of mortgage to begin offering.
- The VA Home Purchase Loan Program may allow community banks to expand their customer base among veterans in their communities.
- Loans originated through VA may receive favorable consideration under the CRA, depending on the geography or income of the participating borrowers.

Potential Challenges

- Despite the ease of becoming a VA-authorized lender, community banks may need to acquire or develop new expertise and infrastructure in order to participate.
- Lenders retain some risk since they are responsible for any loss over 25 percent.

RESOURCES

Direct access to the following web links can be found at https://www.fdic.gov/mortgagelending.

Lender resources
https://www.benefits.va.gov/homeloans/lenders.asp

Complete list of allowed fees and charges
https://benefits.va.gov/WARMS/docs/admin26/handbook/ChapterLendersHanbookChapter8.pdf

County-level loan limits
http://www.benefits.va.gov/homeloans/purchaseco_loan_limits.asp

FHFA loan limits
https://www.fhfa.gov/DataTools/Downloads/Pages/Conforming-Loan-Limits.aspx