Published Feb. 7, 2013, in the Denver Post and in five Jefferson County weekly newspapers

Fees on FHA-Insured Loans Are Rising, Hurting First-Time Buyers the Most

REAL ESTATE TODAY

By JIM SMITH, Realtor®

There is often confusion about the role of FHA (Federal Housing Administration, a division of HUD-Housing and Urban Development) in financing home purchases. FHA does not lend money; they insure a mortgage against the possible default of the borrower. When an FHA-insured loan goes into foreclosure, HUD reimburses the lender and takes ownership of the property, which then becomes a "HUD home" and is sold by HUD to a new buyer.

So, where does the money come from to satisfy the lender's claim? The money comes from the Mutual Mortgage Insurance Fund (MMIF). The MMIF is funded by two forms of the Mortgage Insurance Premium (MIP), one paid by the borrower at closing (the "Upfront MIP", currently 1.75% and financed into the loan), and the second on a continuing basis through the renewal MIP, which is divided by twelve and added to the borrower's monthly payment, just like homeowner's insurance and property taxes. Because of the huge losses suffered by the MMIF as a result of the flood of foreclosures in recent years, FHA has raised its MIP several times. At the beginning of the crisis, borrowers paid 1.0% in upfront MIP and paid 0.55% in renewal MIP. In the case of 15-year loans, the annual MIP was eliminated once the principal loan amount fell to 78% loan-to-value.

Since then, the upfront MIP has nearly doubled to 1.75%, and the renewal MIP has more than doubled to the present level of 1.25% Effective with FHA case numbers issued on or after June 3, 2013, the renewal MIP will rise to 1.35%. In addition, the MIP on 15-year loans will no longer be eliminated when the borrower achieves 22% equity. In other words, even when you owe 5% of what your home is worth, you will still be paying an annual insurance premium of over 1% of the remaining principal to protect FHA from you defaulting on your loan. It would be fair to call this a fee rather than an insurance premium, since there's virtually no risk to insure against!

These fees are becoming so significant now, that buyers should consider FHA loans a last resort. Essentially, the borrower is paying just under 2% of the loan amount at inception (financed with the loan so you don't noticed it as much), plus more than 1% of the remaining principal each year for the life of the loan.

When they can, home buyers should consider non-FHA options ("conventional" mortgages), many of which offer low down payments and lower MIP fees.

This Week's Featured New Listing

Friendly Hills Home With View of Foothills

Imagine home ownership in this desirable location just a short drive to Red Rocks, other parks and golf courses! This split-level home with 3 bedrooms and 2 baths has a finished basement with a bonus room suitable for an office or hobby room. The new interior paint is almost dry and brand new carpet is in the bedrooms and family room. Hardwood floors grace the kitchen and dining/living room area, and both baths are tiled. The deck is being stained in the backyard, which includes a dog run and storage shed. This comfortable home is located in a quiet neighborhood, yet convenient to C-470 and I-70. Be one of the first to check it out as it is being held open from noon to 3:00 this Saturday!

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