10 things that can kill a home loan

The mortgage world has changed dramatically in a few short years.

At the peak of the real-estate bubble, mortgage professionals joked that you needed only to be able to fog a mirror to get a loan. These days, even borrowers with good incomes and good credit scores can get turned down.

Much of the change is driven by the higher standards of the companies that buy mortgage loans, including [Fannie Mae](http://www.bing.com/search?FORM=msmony&q=definition+fannie-mae), [Freddie Mac](http://www.bing.com/search?q=definition+freddie-mac&form=msmony) and various large banks.

Here's what you need to look out for if you're trying to land a mortgage, whether you're buying a home or refinancing:

**1. The house needs too much work.**

A lot of properties on the market these days are foreclosures owned by banks, and many aren't in great repair. (See "[Should you buy a foreclosure?](http://articles.moneycentral.msn.com/Banking/HomebuyingGuide/should-you-buy-a-foreclosure.aspx)") If a house is in really bad shape, it can be tough, if not impossible, to persuade another lender to give you the money to purchase it.

Broken windows, defective appliances, roof leaks and serious water damage can all cause a lender to bail, said Dick Lepre, a senior loan officer with RPM Mortgage.

"A lot of deals just fall apart" after appraisers examine the homes, Lepre said. "Some sellers have gotten shot down so many times because the buyers couldn't get a mortgage that some homes are put on the market as 'all cash.'" In essence, the sellers won't consider buyers who need mortgages to purchase their homes.

In the past, Lepre said, a lender might have been more willing to set aside some of the cash from a deal to pay for necessary repairs. Today, lenders are far more likely to simply refuse to do deals.

**Bottom line:** If it's a real fixer-upper, you may need to pay cash.

**2. The appraisal came up short.**

Occasionally during the bubble an appraiser would decide a home was worth less than the price a buyer and seller had agreed upon. But that was relatively rare. Critics accused appraisers of colluding with lenders to "hit the number" -- deliver the values needed for loans to be approved. Some appraisers acknowledged the pressure, saying banks would turn to their competitors if they didn't hit the number.

These days, the situation is drastically different. New rules hold appraisers to higher standards and sharply limit communication between appraisers and lenders. So the appraisal on the home you want to buy may fall short of the agreed-upon selling price.

Even if the first appraisal goes well, Lepre said, a second evaluation -- known as the review appraisal and now ordered by most investors that buy home loans -- may not.

**Bottom line:** You may be able to nudge an appraisal a bit by showing there are better "comparable sales" available than the ones the appraiser used. In general, though, appraisers are much harder to influence. You may need to reopen negotiations with the seller or come up with a bigger down payment to make a deal work -- or pay down your mortgage in order to refinance.

**3. You have too much debt.**

Lenders look at how much of your income will go toward housing expenses (mortgage, property taxes and insurance) as well as how much you spend on other debt payments.

The total amount of your income that can be eaten up by these expenses can vary by the lender and even by the day. Over a matter of months, one major mortgage buyer dropped the ceiling of total debt from 65% to 55% and then to 50% of gross income, said Matt Hackett, the underwriting manager for New York lender Equity Now. Some have lower limits.

The mortgage industry still isn't as conservative about debt as it probably should be, said Michael Moskowitz, Equity Now's founder and president. Moskowitz noted that people can still get approved for loans that don't leave them enough breathing room for other costs, such as [adequately maintaining the house](http://articles.moneycentral.msn.com/Banking/HomebuyingGuide/your-1st-home-save-for-repairs.aspx) or saving for other goals, including [retirement](http://articles.moneycentral.msn.com/Retirementandwills/Createaplan/Createaplan.aspx).

**Bottom line:** If your projected housing-and-debt ratio exceeds 40% of your income, you should think twice about buying a home -- not because you won't get approved (you might) but simply because you're carrying too much debt. At the very least, you should [pay off all credit cards and other toxic debt](http://articles.moneycentral.msn.com/SavingandDebt/ManageDebt/6-steps-to-dumping-toxic-debt.aspx). Such debt indicates you're already living beyond your means, a situation that's likely to worsen if you buy a home.

**4. You're self-employed and your income has declined.**

To get a mortgage, you typically need to submit the past two years' tax returns. If your 2008 income was lower than your 2007 income and you're a W-2 wage earner, lenders will simply use the lower figure to decide how big a mortgage you can get.

The industry is far more leery of declining income if you're self-employed, Moskowitz said. Some lenders will use the 2008 figure, but others won't make the loan at all because they're worried your income will drop further and you'll default.

**Bottom line:** If you're self-employed and your income has dropped, talk to your mortgage professional about how that might affect your loan.

**5. You recently started being paid on commission.**

Companies eager to cut costs have been switching some of their staffs from salaries or hourly wages to commissions. That can wreak havoc with your mortgage application because lenders typically won't count commission income unless you've been earning commissions for at least two years.

**Bottom line:** If your company switched you to commissions before the end of 2008, you may have to wait to get a loan or use a spouse's income to qualify.

**6. There's a problem with your tax returns.**

Lenders don't accept your copies of your tax returns as the final word about what you earned. These days they order transcripts of the returns you filed with the Internal Revenue Service and compare those with what you had submitted.

Your loan will get tossed if you exaggerated your income, of course. But other problems include:

* Unreimbursed employee expenses. This snares a surprising number of borrowers, Hackett said. Any amount taxpayers deduct for these expenses has to be deducted from the income that can be used to qualify them for a loan. "We've had some loans that blew up because of this," Hackett said. "One guy had $49,900 of income but he wrote off $12,100 in (unreimbursed) auto expenses." Subtracting that amount from his pay left him too little income to qualify for the loan he wanted.
* Second-home expenses. Even if you own the property free and clear, the taxes and insurance you pay on it will affect your debt ratio. Borrowers may not list the property on their initial application, especially if there's no mortgage involved, but the tax transcript will pick up any of the second-home costs they deducted.
* A too-small payment for estimated taxes. If you're self-employed and pay estimated taxes, you might try to conserve cash by making a smaller-than-usual tax payment. That could be a mistake, since a lender might decide the smaller payment is a sign your income is declining.
* No transcript. It can take up to five weeks for a transcript to be available after a return is filed, Hackett said. So if you got an extension to file your return and didn't do so until the Oct. 15 extended deadline, your transcript won't be available for several more weeks, which could endanger your deal.

**Bottom line:** Review your tax returns with your mortgage lender or broker when you apply to see whether there are any red flags.

**7. You can't get private mortgage insurance.**

Technically, you still can get approved for a loan equal to up to 97% of a home's appraised value. To do so, however, you'd need to get approved for private mortgage insurance. And PMI companies, severely burned by the real-estate flameout, are being pickier than ever before.

If you're the ideal borrower -- credit scores of 720 or above, with a debt load below 40% of your income and several months' worth of expenses in the bank -- you might get approved for private mortgage insurance that would allow you to borrow up to 95% of a home's purchase price in a flat or improving market, Hackett said.

In declining markets such as Florida, the best you could hope for is 90%, he said. And if anything is slightly wrong with your profile as a borrower, you probably will have to settle for less. If you can't come up with a bigger down payment, you likely will get funneled into a Federal Housing Administration loan, which allows [down payments as low as 3.5%](http://articles.moneycentral.msn.com/Banking/HomeFinancing/get-into-a-house-for-just-3-point-5-percent-down.aspx) but may have somewhat higher interest rates.

**Bottom line:** A bigger down payment gives you more options. Read "[The end of the 0% down payment](http://articles.moneycentral.msn.com/Banking/HomeFinancing/the-end-of-the-0-percent-down-payment.aspx)."

**8. The lender doesn't like your condo association's finances.**

Mortgage buyers are enforcing guidelines on condo and co-op purchases that used to be widely ignored, as well as imposing new restrictions.

Some that you might stumble into include:

* The 10% ownership rule. If anyone owns more than 10% of the units in a building, you probably won't be able to get a loan. Lenders are worried that if this big owner defaults, the remaining owners won't be able to pay for proper maintenance. Yet 10%-plus ownership stakes are pretty common, particularly where apartments were converted to condos or co-ops and the original owner hung on to units to rent.
* The fidelity bond. Associations are supposed to buy a bond to protect against theft by management company employees. Many skated along with small bonds, but now lenders want to see more coverage. "A lot of (associations) had $50,000, and now you might need $400,000," Hackett said. The actual cost of increasing the bond is usually just a few hundred dollars a year, but board members may not understand the importance of this requirement and resist coughing up the extra cash.
* Cash reserves. Condo associations should generally have cash reserves equal to 60% of the association fees they collect over the year, to make sure they have sufficient reserves to pay for needed maintenance and repairs, RPM Mortgage's Lepre said. Many associations fall short of this mark. As above, owners who aren't actively trying to sell their properties may not realize the importance of this requirement and may resist efforts to boost reserves.

**Bottom line:** If you're buying a condo, talk to your mortgage pro about the unique requirements for these loans and make sure the association meets them before applying for a loan.

**9. Your lender is dragging its heels.**

Like most other companies in this recession, lenders are often reluctant to hire workers, even if mortgage applications are piling up. If it takes too long to get your mortgage approved, however, you could wind up paying a higher interest rate (if your rate lock expires), or your purchase deal could fall through, particularly if the seller has another interested buyer.

Another issue: getting [subordination](http://www.bing.com/search?q=home+equity+subordination&go=&form=MSMONY) for second mortgages. If you're refinancing and have a home equity loan or line of credit on your property, you essentially need to get your home equity lender's permission to complete the deal.

**Bottom line:** Ask your lender how long it will likely take for your deal to get done. If the wait time is too long, consider switching to a company that can offer faster approval. In any case, monitor your loan and follow up frequently with your mortgage professional and any home equity lender to make sure it stays on track.

**10. You fail to stay on top of the paperwork.**

By now, you should have a pretty good feel for how very much scrutiny your loan application is going to get. Lenders demand a ton of paperwork, and you should be prepared to prove anything and everything, especially your income and the source of your down payment.

Any missing document or oversight can delay or even torpedo your loan, which is why you need to respond instantly to your loan officer's requests.

Right before one loan was set to be approved, for example, Lepre got a notice that page 5 of the loan application hadn't been initialed.

"Before, nobody would have called about something like that," Lepre said. "I try to prepare people that they are going to be asked for stupid things, right up to the end."

**Bottom line:** Put your mortgage professional's number on speed dial and respond promptly to any document request, no matter how silly you think it is. Without every "i" dotted and "t" crossed, the loan might not get done.