

Understanding Home Equity Products Interactive Training

WORKSHEETS

You can use the three worksheets in this section to help in the loan application process. They will help you qualify your customer and select a Home Equity product. You can go through these worksheets manually with your customer.

- **Calculating Potential Equity**
- **Calculating Cost Benefits**
- **Comparing Mortgage Options for Savings**

Calculation Terminology

Important terms used on the worksheets in this section include the following.

Potential Equity and Actual Equity - determines the amount available for borrowing. Potential equity is based on the initial estimate of the current market value. The underwriter calculates the actual equity after the appraisal is completed.

LTV and CLTV Ratios - determines the amount a customer can borrow. The LTV (loan to value) ratio is the percentage of the property value allowed for borrowing on a first mortgage. The CLTV (combined loan to value ratio) is a combination of the first and all junior mortgages against the appraised or purchased value of the property. The CLTV ratio is calculated by dividing the total of all liens (i.e. the first mortgage and all recorded subordinate financing) by the lower of appraised value or the purchase price (if purchased within the last 12 months) at the time the loan is closed. The Combined Loan to Value (CLTV) maximum is based on the applicant's current credit score, debt to income and total liens on the property. You can get the maximum CLTV percentage permitted from the product guidelines.

Blended (or Weighted Average) Rate - shows the potential cost benefits of combining a first and second mortgage. The blended rate, or weighted average rate, is the overall cost of financing a property, expressed as an interest rate. It includes the interest rate on the mortgage or mortgages on the property, as well as the cost of any supporting products, such as mortgage insurance. You can calculate the blended rate by first multiplying the interest rate of each mortgage or loan product (PMI) by its remaining balance, and then total that number. Next, add up the total of the mortgages on the property. Finally, divide the first total, which is the interest and other costs, by the second total, which is the indebtedness on the property. That quotient will be the blended rate.

CALCULATING POTENTIAL EQUITY

This calculation worksheet is used to establish how much potential equity a customer may have on the property. **Potential equity is based on the initial estimate of the current market value.** The underwriter will calculate the actual equity after the appraisal is completed.

Items to Consider

- What is the property type (Single Family Residence, Co-op, Condo, Manufactured Home)?
- Is it a Primary Residence or Secondary Home?
- Does the applicant have an existing mortgage?
- Is the customer applying for the No Income Verification program?

If the customer would like more than the CLTV stated, you may be able to calculate at a higher CLTV provided that the customer meets the qualifications.

Calculating Potential Equity

Use this worksheet to establish how much potential equity a customer may have on the property. Enter the information requested on each line that says "Enter" and then calculate the other items (the formulas refer to item line numbers).

1	Enter estimated market value	
2	Enter maximum allowable CLTV %	
3	Amount available for financing (= 1 * 2)	
4	Enter the first mortgage balance	
5	Potential equity available (= 3 - 4)	

Calculating Actual Equity

After the appraisal is complete, the Underwriter will determine the actual equity that the customer has, which will always differ from the potential equity calculated above. Actual equity is calculated using the following steps.

- 1)** The first mortgage balance and the home equity line/loan amount are added together.
- 2)** The sum from Step 1 is divided by the appraised value.
- 3)** The result from step 2 is multiplied by the appraised value.

CALCULATING COST BENEFITS

This worksheet helps to show the cost benefits of combining a first and second mortgage using several different options. Enter the information requested on each line that says "Enter" and then calculate the other items (the formulas refer to item line numbers). Use your financial calculator to calculate the monthly payment information. If your calculator computes a monthly interest rate, you can multiply by twelve to get the annual interest rate.

Total Monthly Payments

1	Enter computed first mortgage payment (principle and interest)	
2	Enter computed second mortgage payment (principle and interest)	
3	Total monthly payment (= 1 + 2)	

Blended Rate (first and second Option)

4	Enter computed high LTV first payment	
5	Enter monthly mortgage insurance payment (= 4 + 5)	
6	Total monthly payment	
7	Regular payment (= first & second mortgage from line 3)	
8	Difference high LTV with PMI vs. first/second mortgage (= 6 - 7)	

Blended Rate (high LTV first with PMI Option)

9	Enter first mortgage interest rate	
10	Enter mortgage insurance premium (expressed as %, on annual basis)	
11	Sum (= 9 + 10)	
12	Blended rate (average of two rates) (= 11 / 2 (the number 2))	

COMPARING MORTGAGE OPTIONS

Benefits of combining a first and second mortgage include increased buying power, higher loan amounts, lower monthly payments, reduced settlement costs, and tax deductions.

PMI Savings: For a down payment of less than 20%, Private Mortgage Insurance (PMI) is required and PMI charges apply. PMI costs vary depending on the LTV, required coverage level and payment method (i.e. monthly or annual). With a second mortgage, PMI is not required and this can mean a significant savings.

Tax Benefits: Calculated annual savings on the worksheet excludes any tax benefits your customer may receive. Generally, interest on home equity products is tax deductible for aggregate loan and line amounts up to \$100,000 regardless of the use of the proceeds. Product amounts over \$100,000 may not be tax deductible unless the proceeds are used to buy, build or substantially improve the home. Consult a tax advisor regarding a specific situation.

Comparing Mortgage Options for Savings

This worksheet compares a single mortgage option with the combined first and second mortgage to show the savings with a second mortgage. Enter or calculate values as appropriate. Enter data in the shaded green boxes. Blue boxes remain empty.

		First Mortgage Loan	1st & 2nd Mortgages in Access Period (interest only, first 9 years)	1st & 2nd Mortgages in Repayment Period (principle + interest, over 20 years)
1	Enter Purchase Price			
2	Enter Down Payment			
3	Enter Second Mortgage Amount	---		
4	Principle Loan Amount			
5	LTV		---	---
6	CLTV	---		
7	Enter First Mortgage Term (in months)			
8	Enter Second Mortgage Term (in months)	---		
9	Enter First Mortgage Interest Rate (as a decimal, ex. = .08)			
10	Enter Second Mortgage Interest Rate (as a decimal, ex. = .06)	---		
11	Enter First Mortgage Payment (use financial calculator)			
12	Enter PMI		---	---
13	Enter Second Mortgage Payment (use financial calculator)	---	interest only	principle + interest
14	Total Monthly Payment			
15	Monthly Savings	---		
16	Yearly Savings	---		

Note: Access period for Connecticut is 9 years & 10 months. Tennessee has a 10-year repayment period.

Example: Comparing Mortgage Options for Savings

Green boxes are figures you must calculate and enter. Blue boxes remain empty.

		First Mortgage Loan	1st & 2nd Mortgages in Access Period (interest only, first 9 years)	1st & 2nd Mortgages in Repayment Period (principle + interest, over 20 years)
1	Enter Purchase Price	\$200,000	\$200,000 (1A)	\$200,000 (1A)
2	Enter Down Payment	\$20,000	\$20,000 (2A)	\$20,000 (2A)
3	Enter Second Mortgage Amount	---	\$20,000	\$20,000 (3B)
4	Principle Loan Amount	\$180,000 (1A-2A)	\$160,000 (1B-2B-3B)	\$160,000 (4B)
5	LTV	90% (4A/1A)	---	---
6	CLTV	---	90% (4A/1A)	90% (4A/1A)
7	Enter First Mortgage Term (in months)	360 months	360 months (7A)	360 months (7A)
8	Second Mortgage Term (in months)	---	120 months	240 months
9	Enter First Mortgage Interest Rate (as a decimal)	8%	8% (9A)	8% (9A)
10	Enter Second Mortgage Interest Rate (as a decimal)	---	4%	6%
11	Enter First Mortgage Payment (use financial calculator)	\$1320.78	\$1174.03	\$1174.03 (11B)
12	Enter PMI (use financial calculator)	\$120.00	---	---
13	Enter Second Mortgage Payment (use financial calculator)	---	\$65.75 ((3Bx10B)/365)x30 interest only	\$143.92 principle and interest
14	TOTAL Monthly Payment	\$1440.78 (11A + 12A)	\$1239.78 (11B + 13B)	\$1317.32 (11C + 13C)
15	Monthly Savings	---	\$201.00 (14A-14B)	\$123.46 (14A - 14C)
16	Yearly Savings	---	\$2412.00 (15B x 12)	\$1481.52 (15C x 12)

Note: Access period for Connecticut is 9 years & 10 months. Tennessee has a 10-year repayment period.