WHAT IS AN **FHA LOAN?**

Everything
ABOUT MORTGAGE

DEFINITION
REQUIREMENTS
& LIMITS

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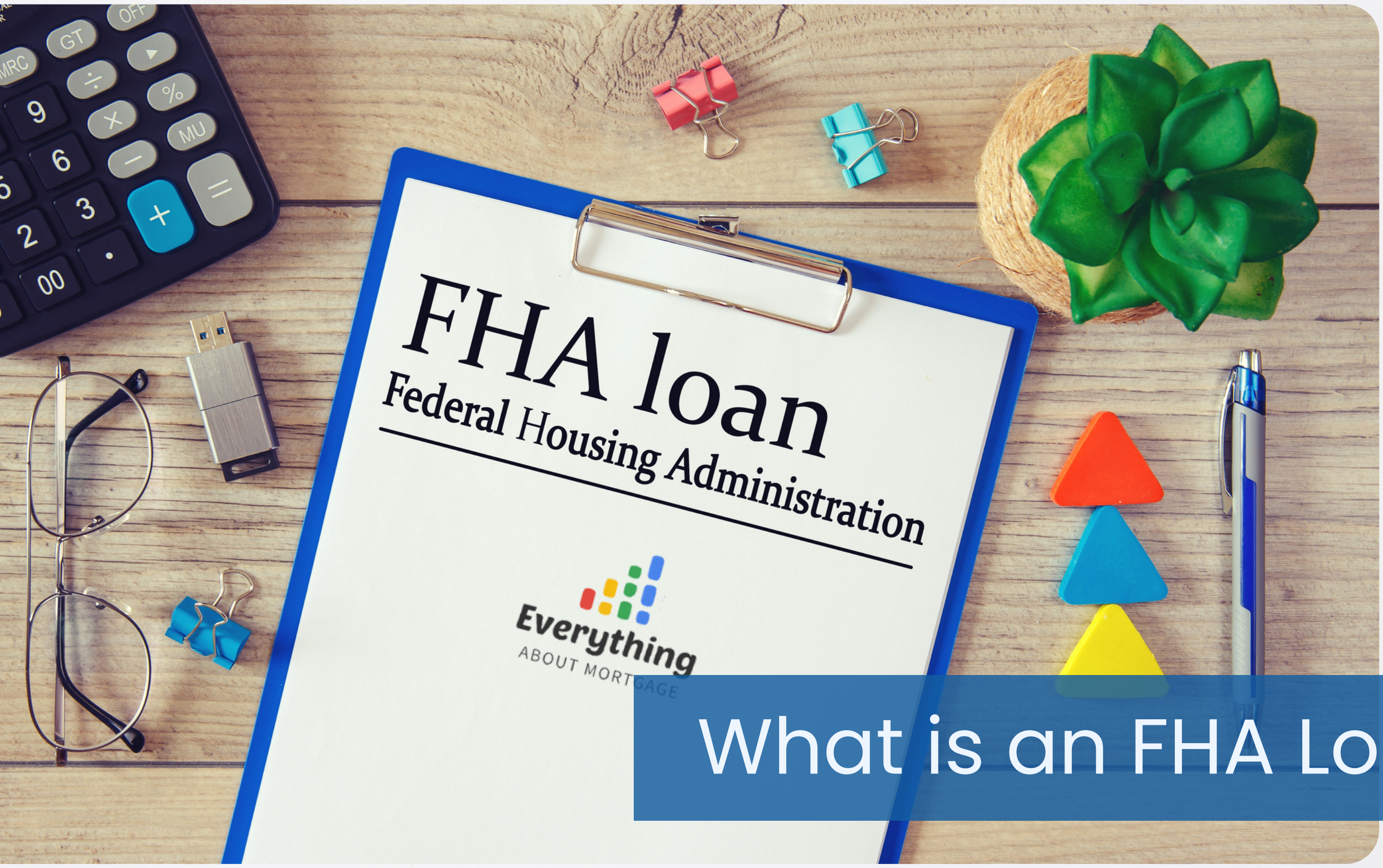


What is an FHA Loan?

An **FHA loan** is a type of mortgage insured by the *Federal Housing Administration* (FHA), which is overseen by the *U.S. Department of Housing and Urban Development* (HUD). While the government insures these loans, they're actually underwritten and funded by third-party mortgage lenders approved by the FHA. You'll find many big banks and other types of lenders offer them.

FHA loans have a low minimum credit score and down payment requirement, which makes them especially popular with first-time homebuyers. You can get an FHA loan with a credit score as low as 580 if you have 3.5 percent of the home's purchase price to put down, or as low as 500 with 10 percent down. These flexible underwriting standards are designed to help more borrowers become homeowners.

You can't buy just any home with an FHA loan, however. Based on your credit and finances, the lender determines how much mortgage you'd qualify for, within the FHA loan limits for your area. You can't use this type of loan to buy an investment property or vacation home, either.

How do FHA Loans Work?

FHA loans work like most other mortgages, with either a fixed or adjustable interest rate and a loan term for a set number of years. FHA loans come with two term options: 15 years or 30.

You'll also pay closing costs for an FHA loan, such as appraisal and origination fees. The FHA allows home sellers, a home builder or mortgage lender to cover up to 6 percent of these costs.

In order to insure these loans against default — that is, if you were to stop repaying your loan — the FHA requires borrowers with a down payment below 20 percent to pay *mortgage insurance premiums*, or MIP. These go into the *Mutual Mortgage Insurance Fund* (MMIF) that covers loss claims. Although you'll be paying the premiums as the borrower, FHA mortgage insurance protects the lender.

FHA Loan Requirements

Along with mortgage insurance premiums, here's an overview of the requirements for an FHA loan:

Credit Score Minimum	580 with 3.5% down; 500 with 10% down
Debt-To-Income (DTI) Ratio Maximum	43% (up to 50% in some cases)
Down Payment Minimum	3.5% with a credit score of at least 580; 10% with a credit score of 500-579
Mortgage Insurance Premiums	1.75% upfront premium; 0.15%-0.75% annual premiums
Occupancy	Primary residences only; 1-4 units

FHA Loan Limits

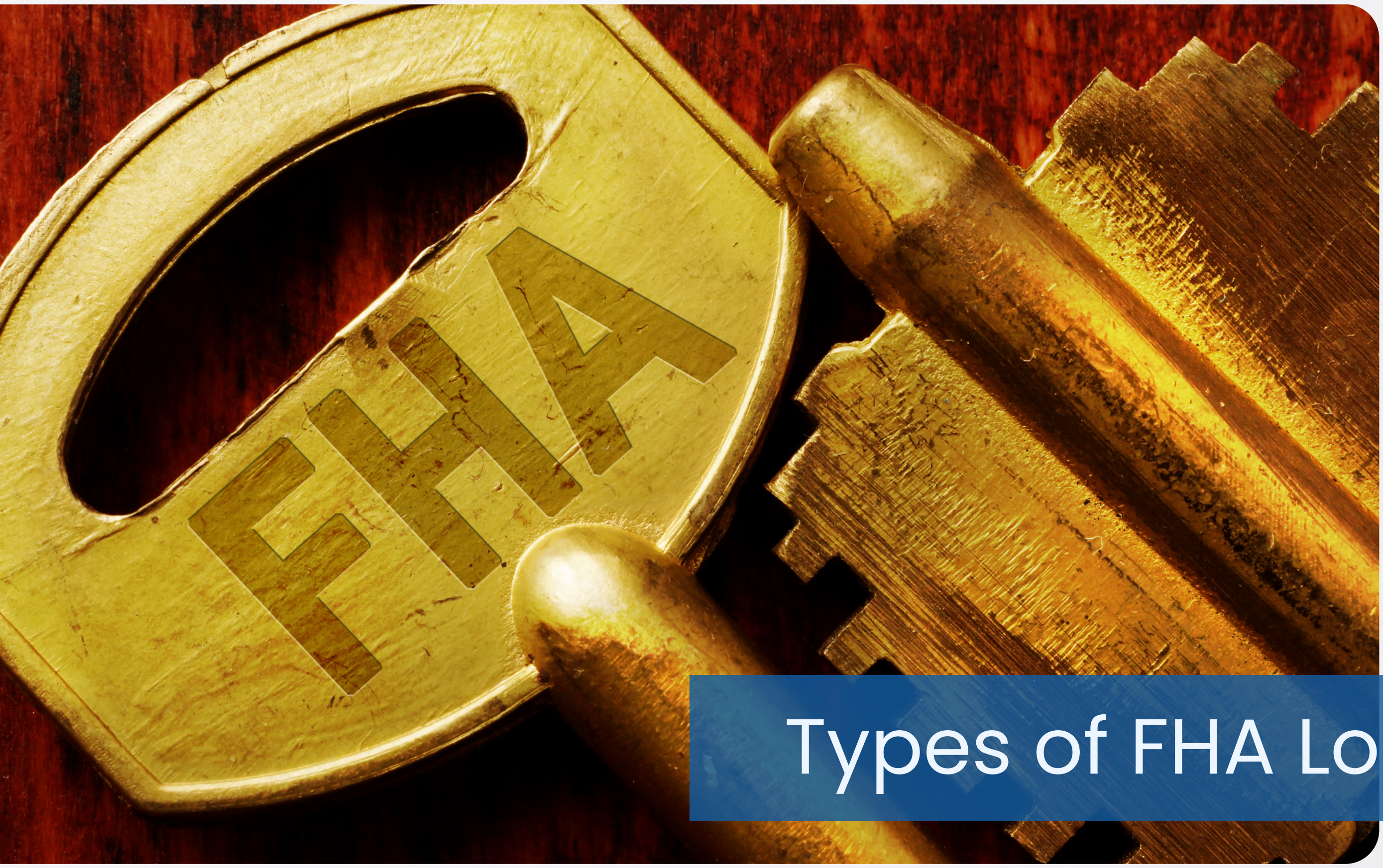
Each year, the FHA sets limits on the maximum amount they will lend depending on the property type and the area. For 2024, the floor limit for a one-unit residence is $498,257, adjusting upward in higher-cost areas. For the most expensive areas, the limit is $1,149,825.

FHA Mortgage Insurance Premiums

FHA loan borrowers who put less than 20 percent down on their home purchase are responsible for paying two mortgage insurance premiums:

- **Upfront MIP** – 1.75 percent of the amount you're borrowing, paid at closing or financed with the rest of the loan
- **Annual MIP** – Ranges from 0.15 to 0.75 percent of the amount you're borrowing, typically paid monthly with your mortgage payment; for most borrowers, it'll be 0.55 percent

The annual premium rates are based on the length of your loan term (15 years or 30), the size of your down payment and the amount you're borrowing. The down payment piece is key: If you put at least 10 percent down, you can stop paying FHA insurance premiums after 11 years. If you put less than 10 percent down, you'll pay these premiums for the duration of the loan term.



Types of FHA Loans

If you're thinking of getting an FHA loan, it's good to know there are several types, which include:

- **Basic Home Mortgage Loan (203b)**: The 203b loan is the FHA's main home loan program. These loans come with fixed and adjustable-rate options, as well as a choice between 15- and 30-year terms.

- **Rehabilitation Mortgage (203k)**: Borrowers buying a fixer-upper can use an FHA 203k loan to cover repairs and upgrades to their home. This type of FHA construction loan comes in Standard and Limited options, which differ based on how much money you need to spend on upgrades.

- **Disaster Victims Mortgage (203h)**: If you've lost your home due to a major disaster and need to rebuild or buy a new home, an FHA 203h loan may help you do that. There's no down payment required, but you have to have been affected by a Presidentially designated disaster.

- **Home equity conversion mortgage (HECM)**: The HECM is a reverse mortgage insured by the government that allows those over the age of 62 to tap the equity in their home. This equity acts as a source of income. However, when the borrower dies or moves out of the home, the mortgage must be paid back.

- **Energy efficient mortgages (EEMs)**: This is a mortgage designed for the purchase of an energy-efficient home, or to upgrade a home to make it more energy efficient.

- **Graduated payment mortgage (245a)**: A graduated payment mortgage is unusual and rare. These mortgages come with payments that start small and increase over time, making them an option for those who expect to make more money in the future.

How to get an FHA Loan

1. **Confirm your eligibility**: The requirements for an FHA loan include having a minimum 580 credit score (500 if you have at least 10 percent to put down); proof of consistent employment and income; and a debt-to-income (DTI) ratio of no more than 43 percent.
2. **Get familiar with loan limits**: There are limits to how much you can borrow with an FHA loan, depending on the type of property you're buying and where you live. In many areas, the limit for a single-family home is $498,257 in 2024. Multi-unit properties and areas with a higher cost of living have higher limits.
3. **Know your budget**: Consider your income, expenses and savings, and use Bankrate's affordability calculator to estimate your budget.
4. **Compare lenders**: Whether you ultimately go with your bank or another lender, shop around for rates. You can find out if a lender offers FHA loans through its website or customer service department, or by using HUD's lender lookup tool. Note that lenders set their own rates, origination fees and underwriting standards, so long as it meets FHA minimum requirements. That's why it's important to compare offers.
5. **Compile your documents and apply for your loan**: Before you apply for an FHA loan, gather two years of tax returns; two recent pay stubs; your driver's license or other official identification; and full statements of your assets (checking account, savings account, 401(k) and any other places you hold money).

PROS and CONS of FHA Loans

Pros of FHA Mortgages

- **You can have a lower credit score**: A credit score of 620 is the minimum for most conforming conventional mortgages. But for an FHA loan, you can get a loan with a score of 580 and 3.5 percent down, or as low as 500 with 10 percent down.
- **You can make a low down payment**: With a credit score of at least 580, you can make a down payment on a home of as little as 3.5 percent.
- **You can own a home sooner**: Since FHA loans are easier to qualify for, you might be able to get into a home and start building equity sooner, acquiring an important asset that increases your overall net worth.

Cons of FHA Mortgages

- **You won't be able to avoid mortgage insurance**: Everyone pays upfront mortgage insurance premiums with an FHA loan. For annual MIP, if you put down less than 10 percent, you'll pay it for the life of the loan. If you put down at least 10 percent, you'll pay annual MIP for 11 years, or until you refinance or sell.
- **You'll have to meet property requirements**: FHA mortgages are not allowed to exceed certain amounts, which vary based on location. You have to live in the property, too: FHA loans aren't designed for second homes or investment properties.
- **You could pay more**: When you compare mortgage rates between FHA and conventional loans, you might notice lower FHA loan interest rates but higher annual percentage rates, or APRs. The APR represents the total cost of borrowing, including fees and points.

FHA Loans vs. Conventional Loans

Unlike FHA loans, conventional loans are not insured by the government. Here's a side-by-side comparison of the two:

	Conventional Loan	FHA Loan
Credit Score Minimum	620	580 (500 with 10% or more down)
Down Payment Minimum	3% for fixed-rate loans; 5% for adjustable-rate loans	3.5% with a credit score of at least 580; 10% with a score as low as 500
Loan Term	8- to 30-year terms	15- or 30-year terms
Mortgage Insurance	*Private mortgage insurance* (PMI) if putting less than 20% down; temporary	Everyone pays mortgage insurance premiums (MIP). If you put less than 10% down, you'll pay an annual MIP for the life of the loan. If you put down more than 10%, you'll pay an annual MIP for 11 years.

FHA Loan FAQs

Is an FHA Loan right for you?

An FHA loan can help you get into a home even with poor credit and limited savings for a down payment. For that reason alone, it's worth considering. FHA loans are costlier, though, thanks to the mortgage insurance premiums. If you have a stronger credit score — at least 620 — you could qualify for a conventional mortgage even if you can't put 20 percent down. On a conventional loan, you won't have to pay mortgage insurance for the entire loan term — you can cancel PMI when you accumulate 20 percent equity in your home.

How do FHA Loans compare to other loan types?

Compared to conventional loans, FHA loans offer a more generous credit score threshold but similarly come with a mortgage insurance requirement if you put less than 20 percent down. Compared to VA loans and USDA loans, FHA loans are open to anyone who qualifies. VA loans are only for active-duty military, veterans and surviving spouses, while USDA loans are only for homebuyers in certain rural areas.

Who qualifies for an FHA Loan?

Beyond those listed above, FHA loans have other specific requirements. These include:

- The property must be your primary residence
- You must occupy the home within 60 days of closing
- The property must pass an FHA inspection and meet FHA standards
- The property must be appraised by an FHA appraiser

How do I get rid of FHA Mortgage Insurance?

Everyone who gets an FHA loan pays mortgage insurance. You can get rid of FHA mortgage insurance after 11 years of payments if you put down 10 percent or more. If you put down less than 10 percent, you'll pay mortgage insurance until you pay off the loan, sell the home or refinance to a conventional mortgage.

Let’s Chat.

I’m sure you have questions and thoughts about the real estate process.

I’d love to talk with you about what you’ve read here and help you on the path to selling your house. My contact information is below, and I look forward to working with you.

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