

THE BASICS OF EVERY LOAN

To insure a smooth transaction, we begin by taking a 3 step loan origination process.

Step 1: Education and discovering the best options available for you.

Step 2: Strategizing and building a game plan according to your goals.

Step 3: Set expectations, executing the action plan.

We start with Step 1: Education.

When a Mortgage Loan is underwritten, there are four primary qualifications that are being measured. They are...

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| 1. Income / Employment History | <i>Typically seeking 2 years steady history</i> |
| 2. Assets: | <i>Typically seeking 3 to 6 months of reserves (PITI)</i> |
| 3. Debt / Credit History (FICO score): | <i>Ideally 680 score and above</i> |
| 4. Equity position and / or down payment: | <i>Ideally a 20% or greater equity position</i> |

In an ideal world, all underwriters are seeking to "hit a homerun!" In other words, they would like to see **all** borrower(s) meet **all** of these pre-requisites. In doing so, it is easy for the bank to approve the loan because there is a high level of confidence that the loan will not be defaulted on. As we all know, this is not always the case. In fact, many borrowers fall short in one category or another. The important thing to remember is not to give up! There are other alternatives to consider for those who have a difficult time meeting all of the "ideal criteria." In fact, there are new and innovative loan programs being released almost daily. These programs are being tailored specifically to meet the needs of an ever changing and diverse borrowing community. A qualified Mortgage Professional should be able to quickly assess your situation, navigate through the options available to choose from, and make a recommendation that makes sense based on your specific qualifications. For more information or if you would like to have your own situation reviewed, call our office today and ask to speak with one of our Professional Loan Consultants.

UNDERSTANDING WHAT REALLY IMPACTS THE RATES

Is a Fed rate cut really good news for mortgage rates? The facts may be surprising. The Fed can only control the Discount Rate and the Fed Funds Rate. This is very different from mortgage rates. A mortgage rate can be in effect for 30-years, a rate that is set by the Fed can change from one day to another.

Another common mistake is in thinking that 30-year Treasury bonds or 10-year Treasury notes are directly pegged to mortgage rates. Those are government securities that are backed by the full faith and credit of the U.S. government and have no direct effect on mortgage rates.

So what are mortgage rates based on? As it turns out the answer is mortgage-backed bonds known as Mortgage Backed Securities (MBS). Bonds issued by Fannie Mae and Freddie Mac (MBS) and the trading performance of those bonds will determine the direction of mortgage rates. Finding the catalyst that causes mortgage bonds to move will give you the keys to finding out what makes mortgage rates rise or fall

SHOULD I LOCK OR FLOAT

Occasionally the question arises about what is meant in the Mortgage Industry by "the risks of locking" or "the risks of floating" Before clarifying, we need to have a fundamental understanding of how financial instruments such as mortgage bonds, corporate bonds, treasury bonds, commodities, futures, options, and stocks trade in a free market.

The Personality of Mortgage Bonds

First, there are a tremendous number of possible factors or variables involved in why any particular bond or stock trades the way it does. Some of these variables include fundamental analysis or evaluation, economic news, financial news, trader psychology, technical analysis and technical indicators to name a few. Another point to consider is each individual entity traded, such as a particular stock or bond, can exhibit its own "market personality" by trading in response to or because of a combination of some of the variables just mentioned. There is even an interesting theory called "The Personality of Markets Theory" developed by Ed Downs of Nirvana Systems that states individual securities exhibit individual personalities and if you can pinpoint a security's personality, and apply the right trading system for that personality, you can predict its next move and make money.

So, what causes these different personalities to develop? Price moves occur because of what people do and, human nature says people tend to be rather predictable. Furthermore, the same people make up a large portion of the market. So, the traders who liked a mortgage bond or stock last week and are selling it this week, will probably like it again next week. Again, human nature says that once you've traded a security and either made a good move, or missed a move, you will look for another opportunity to try again. Also, different types of people are attracted to different types of securities.

Technical analysis is the art of measuring these repeating patterns of human behavior in order to predict future behavior and the resulting price action. By looking at the past behavior of the market, traders have observed certain patterns and created trading systems based on those patterns. You can use these systems to predict what will happen next in the market or in a particular security. The problem is that there have been hundreds of trading systems developed; all of which work well as long as the market is exhibiting the personality for which the system was designed.

The trading system we've been successfully using with mortgage bonds is the Japanese Candlestick method of trading. Japanese Candlesticks capture the psychology and personality of the mortgage bond market. Candlesticks have also been remarkably accurate for us in signaling reversals in direction and predicting moves in mortgage bond prices.

The personality of the mortgage bond market can change from time to time. It can occasionally be volatile but most often it is either trending or in a trading range. While trending or within a trading range, we look for resistance and support levels to help define the risks of locking or floating at a given point in time. There are a number of ways to determine resistance (where selling pressure occurs) and support (where buying pressure occurs) levels for different periods of time. Usually, resistance and support levels can be charted on a short-term (1-16 days), medium-term (17-32 days), or long-term (33-64 days) daily basis. Previous intra-day highs and lows within these time intervals can serve as resistance and support levels. Moving averages can also serve as resistance and support levels. For short-term levels, 10-day increments can be used. For example the 10, 20, 25, 30, 40, and 50-day moving averages are typically used to help define possible resistance and support levels. Another effective method for determining resistance and support levels is through the use of Fibonacci Retracement.

At Lenox Financial, we make use of all of these methods to help us identify resistance and support levels. We keep a close watch on these levels as the bond price approaches them because it is at these levels where reversals in direction most often occur. In addition, our Market Analysis includes making use of the Japanese Candlestick system of trading because we feel this best captures the personality of the mortgage bond market. Within this system, we identify resistance and support levels for you using several different methods and watch for signs of price reversal or change in the direction of trend. Based on these resistance and support levels, we then calculate the "risks" associated with either locking or floating at the current price level. The technical analysis of mortgage bonds provides you with another tool to assist with making timely and effective decisions to "lock" or "float" loans. We feel this analysis gives us a decisive edge over our competitors by allowing us to pass along this expertise to our clients.

Understanding Different Loan Products

Conventional vs. ARMs

Conventional Mortgage: Any mortgage that is not insured or guaranteed by the federal government. The following is a list of commonly seen conventional mortgage programs:

- 30 year fixed
- 20 year fixed
- 15 year fixed
- 10 year fixed

Adjustable Rate Mortgage (ARM): A mortgage that permits the lender to adjust its interest rate periodically on the basis of changes in a specific index. Depending on the mortgage program, there may or may not be a "fixed rate" period. The following is a list of commonly seen ARM programs:

- 10/1 ARM
- 7/1 ARM
- 5/1 ARM
- 3/1 ARM
- 1/1 ARM
- 6 month ARM
- 1 month ARM
- Home Equity Line of Credit (HELOC)

Amortized payments vs. Interest Only

Amortized payment schedule: The loan payment consists of a portion which will be applied to pay the accruing interest on a loan, with the remainder being applied to the principal. Over time, the interest portion decreases as the loan balance decreases, and the amount applied to principal increases so that the loan is paid off (amortized) in the specified time. An amortization schedule is a table which shows how much of each payment will be applied toward principal and how much toward interest over the life of the loan. It also shows the gradual decrease of the loan balance until it reaches zero.

Interest Only payment option: This is when the mortgage consists of an "interest only" payment option for a specified period of time. Depending on the mortgage program, the option time period can vary. In comparison to an amortization schedule where a portion of every payment is applied towards paying back the principle balance of the loan, an interest only payment is computed as a simple interest payment

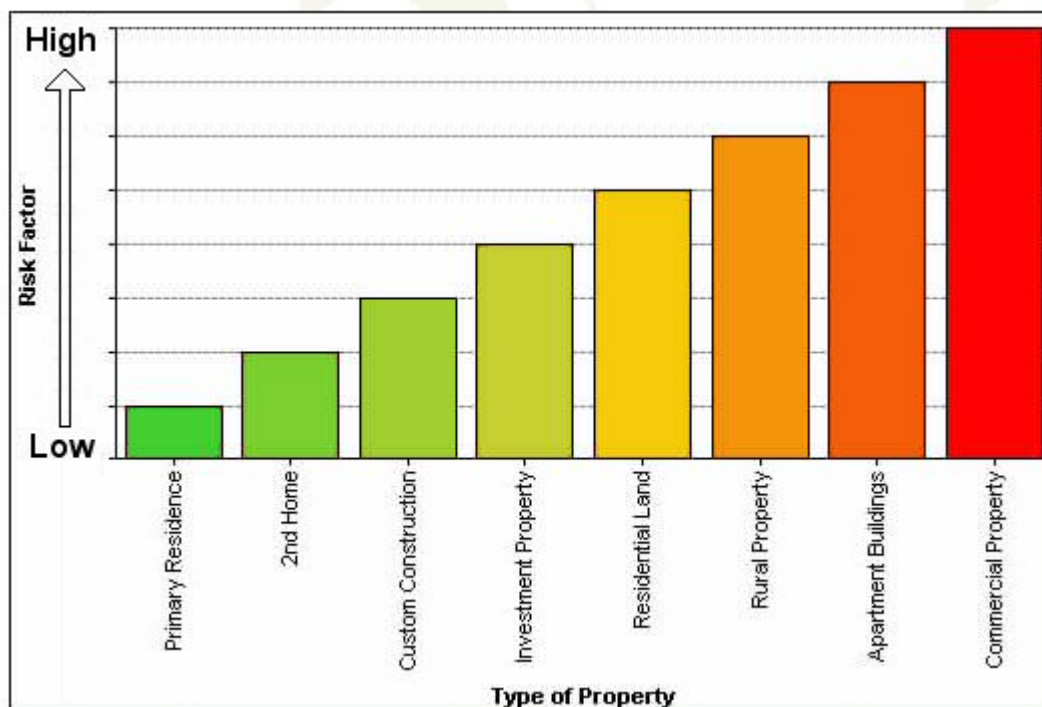
calculation, resulting in minimum payment equal to the "interest only" portion. For example, if a person were to borrow \$100,000 at 6 % interest, the following is how the minimum monthly mortgage payment would be calculated:

$$\$100,000 \times .06 = \$6,000 \text{ (minimum interest owed per year)}$$

$$\$6,000 \text{ divided by 12 months per year} = \text{\$500 Interest Only payment due per month}$$

Understanding different types of properties

Before a lender makes a commitment to loan money, they will want to be clear on the exact type of property that is being collateralized. This is because there are different levels of risk associated with different types of properties (see the chart below).



The tax benefits of home ownership

In tax lingo, your principal residence is the place where you legally reside. It's typically the place where you spend most of your time, but several other factors are also relevant in determining your principal residence. Many of the tax benefits associated with home ownership apply mainly to your principal residence--different rules apply to second homes and investment properties. Here's what you need to know to make owning a home really pay off at tax time.

Deducting Mortgage Interest

One of the most important tax advantages of home ownership is the deduction of mortgage interest. If you itemize deductions on Schedule A of your federal income tax return, you can generally deduct the qualified residence interest that you pay on certain home mortgages taken on your principal residence. (This also applies to second homes.) That is, you may be able to deduct the interest you've paid on a mortgage to buy, build, or improve your home, provided that the loan is secured by your home. Such a mortgage is known as acquisition indebtedness by the IRS. Your ability to deduct interest depends on several factors.

Up to \$1 million of acquisition mortgage debt (\$500,000 if you're married and file separately) qualifies for interest deduction. (Different rules apply if you incurred the debt before October 14, 1987.) If your mortgage loan exceeds \$1 million, some of the interest that you pay on the loan will not be deductible.

Although this deduction also applies to certain home equity loans secured by your home, the rules are different. Home equity debt involves a loan secured by your main or second home that exceeds the outstanding mortgages on the property. Home equity debt is limited to the lesser of:

- The fair market value of the home minus the total acquisition debt on that home, or
- \$100,000 (or \$50,000 if your filing status is married filing separately) for main and second homes combined

The interest that you pay on a qualifying home equity loan is generally deductible regardless of how you use the loan proceeds. For more information, see IRS Publication 936.

Tax treatment of real estate taxes

Along with mortgage interest, you can generally deduct the real estate taxes that you've paid on your property in the year that they're paid to the taxing authority. Only the legal property owner can deduct the real estate taxes. In some cases, prepaid real estate taxes can be deducted in the year of the prepayment. Taxes placed in escrow but not yet paid to the taxing authority, however, generally aren't deductible.

Tax treatment of home improvements and repairs

Home improvements and repairs are generally nondeductible. Improvements, though, can increase the tax basis of your home (which in turn can lower your tax bite when you sell your home). Improvements add value to your home, prolong its life, or adapt it to a new use. For example, the installation of a deck, a built-in swimming pool, or a second bathroom would be considered an improvement. In contrast, a repair simply keeps your home in good operating condition. Regular repairs and maintenance (e.g., repainting your house and fixing your gutters) are not considered improvements and are not included in the tax basis of your home. However, if repairs are performed as part of an extensive remodeling of your home, the entire job may be considered an improvement.

Deducting points and closing costs

Buying a home is confusing enough without wondering how to handle the settlement charges at tax time. When you take out a loan to buy a home, or when you refinance an existing loan on your home, you'll probably be charged closing costs. These usually include points, as well as attorney's fees, recording fees, title search fees, appraisal fees, and loan or document preparation and processing fees. You'll need to

know whether you can deduct these fees (in part or in full) on your federal income tax return, or whether they're simply added to the cost basis of your home.

Before we get to that, let's define one term. Points are costs that your lender charges when you take a loan secured by your home. One point equals 1 percent of the loan amount borrowed. As a home buyer, you can deduct points in the year that you buy your home if you itemize your deductions. However, you must meet certain requirements. You can even deduct points that the seller pays for you. More information about these requirements is available in IRS Publication 936.

Refinanced loans are treated differently. The points that you pay on a refinanced loan generally must be amortized over the life of the loan. In other words, you can deduct a certain portion of the points each year. There's one exception: If part of the loan is used to make improvements to your principal residence, you can generally deduct that portion of the points in the year that the points are paid.

And what about other closing costs? Generally, you cannot deduct these costs on your tax return. Instead, you must adjust your tax basis (the cost, plus or minus certain factors) in your home. For example, if you're buying a home, you'd increase your basis with certain closing costs. If you're selling a home, you'd decrease your amount realized from the sale (i.e., your sale price). For more information, see IRS Publication 530.

Exclusion of capital gain when your house is sold

Now let's see what happens when you sell your home. If you sell your principal residence at a loss, you generally can't deduct the loss on your tax return. If you sell your principal residence at a gain, however, you may be able to exclude from taxation all or part of the capital gain.

Generally speaking, capital gain (or loss) on the sale of your principal residence equals the sale price minus your adjusted basis in the property. Your adjusted basis is the cost of the property (i.e., what you paid for it initially), plus amounts paid for capital improvements, less any depreciation and casualty losses claimed for tax purposes.

If you meet the requirements, you can exclude from federal income tax up to \$250,000 (\$500,000 if you're married and file a joint return) of any capital gain that results from the sale of your principal residence, regardless of your age. In general, an individual, or either spouse in a married couple, can use this exclusion only once every two years. To qualify for the exclusion, you must have owned and used the home as your principal residence for a total of two out of the five years before the sale.

For example, you and your spouse bought your home in 1981 for \$200,000. You've lived in it ever since and file joint federal income tax returns. You sold the house yesterday for \$350,000. Your entire \$150,000 gain (\$350,000 - \$200,000) is excludable. That means that you don't have to report your home sale on your income tax return.

What if you fail to meet the two-out-of-five-years rule? Or what if you used the capital gain exclusion within the past two years with respect to a different principal residence? You may still be able to exclude part of your gain if your home sale was due to a change in place of employment, health reasons, or certain other unforeseen circumstances. In such a case, exclusion of the gain may be prorated.

Additionally, special rules may apply in the following cases:

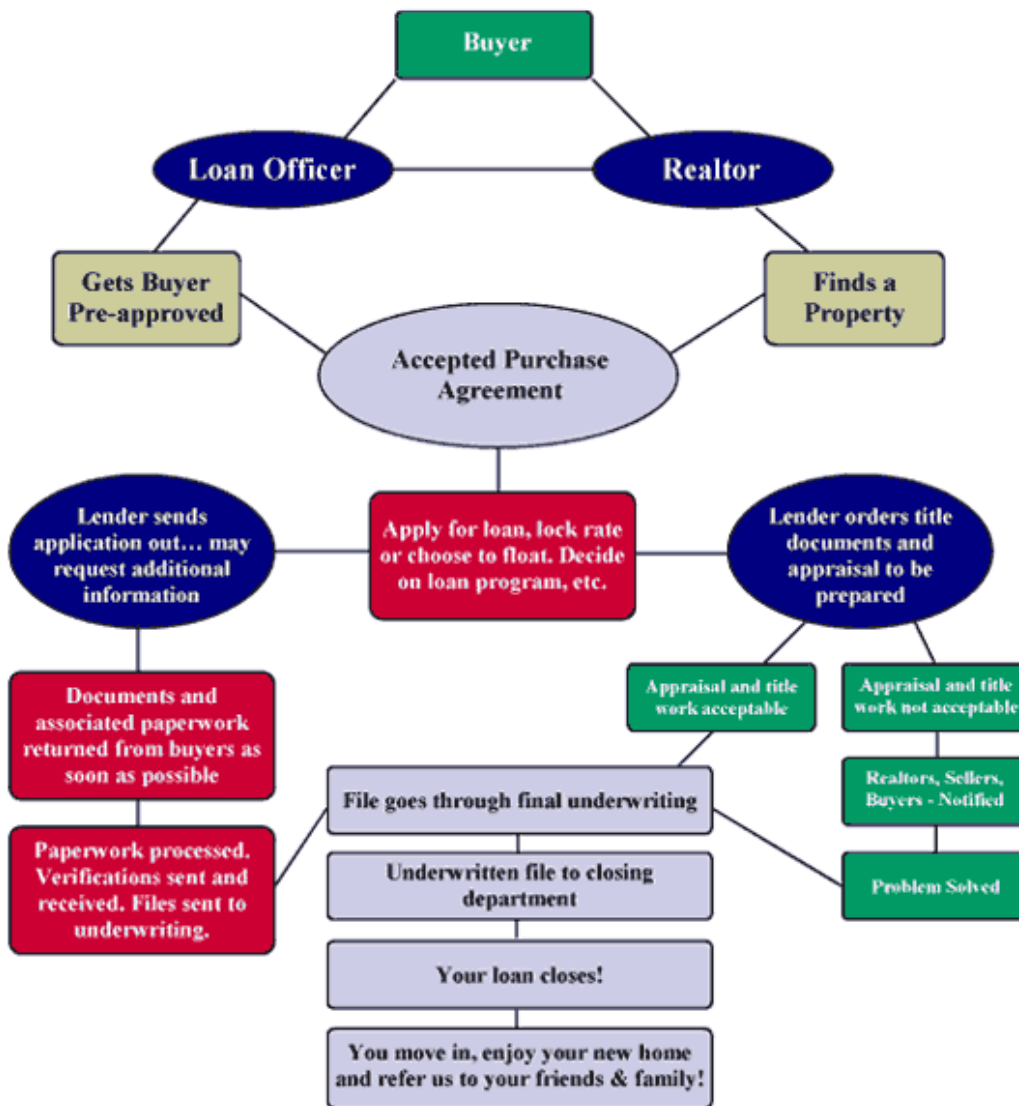
- If your principal residence contained a home office or was otherwise used partially for business purposes
- If you sell vacant land adjacent to your principal residence
- If your principal residence is owned by a trust
- If you rented part of your principal residence to tenants

- If you owned your principal residence jointly with an unmarried taxpayer

Note: Members of the uniformed services and foreign service personnel may elect to suspend the running of the 2-out-of-5-year requirement during any period of qualified official extended duty up to a maximum of 10 years.

This information is intended for informational purposes only and should not be construed as tax planning advice. As always, you should consult a qualified tax professional for details and specific advice.

Loan Process Overview



We begin Step #3 with rolling up our sleeves and executing the plan.

Day	What You Do	What We Do
1 <i>Monday</i>	Apply for a loan by phone or online @ our website.	Pull your credit; develop loan options; prepare loan disclosures and set an appointment to discuss with you; inform you what documents you need to supply us with.
2 <i>Tuesday</i>	Call me; complete your application, loan disclosures and send in NEEDS LIST ITEMS	Explain your loan disclosures, verify all items received and your next steps etc.
3-5 <i>Wed-Fri</i>	Relax and know you're in good hands.	Order the preliminary title report and appraisal; follow-up with processing/underwriting for formal loan approval
6-9 <i>Mon-Thur</i>	Call me if you have any further questions about the process etc.	Prepare your loan application and SUBMIT TO PROCESSING/UNDERWRITING FOR FINAL LOAN APPROVAL.
10 <i>Friday</i>	Begin to gather required and anticipate conditions/ supporting documentation	EXPECT APPROVAL ; notify you of required conditions you can meet; gather any other internal conditions needed.
11-13 <i>Mon-Wed</i>	Gather and respond with any conditions; then trust we are taking care of processing your loan.	Follow-up with underwriting, review and submit appraisal, title report and any conditions received to the underwriter. Request Estimated (HUD -1)
14-16 <i>Thur-Mon</i>	Check your email for any further items needed re-faxing etc.	Submit final conditions to underwriter for their review and clearance; ORDER LOAN DOCUMENTS and REVIEW FINAL SETTLEMENT STATEMENT w/ YOU (HUD -1)
17-19 <i>Tuesday-Thursday</i>	Make arrangements to be available to sign loan documents once they are available (24-48 hrs from now) possibly today!	Follow-up with the closing department to release documents into title; coordinate a signing with you and escrow
20 <i>Friday</i>	RELAX & ENJOY THE WEEKEND! ☺	Docs arrive in Title/Escrow; they contact you to set a signing appointment and prepare the documents for your signing date.
23-24 <i>Mon-Tues</i>	SIGN YOUR LOAN DOCUMENTS with co- (usually at your home or at title company)	Gather and submit to underwriter any Prior to Funding conditions (PTF's)
25 <i>Wednesday</i>	If short to close or a purchase, you would wire cash from the verified source or deliver cashier's check made payable to escrow in the amount from BOX 303 of final HUD-1	Title returns signed loan docs to US the lender for final review and to prepare for funding.
26-26 <i>Thur-Fri</i>		Closing department reviews signed loan documents and remaining funding conditions
30 <i>Monday</i>	RELAX...☺	YOUR LOAN FUNDS!!
31	Smile! The process is complete!	LOAN RECORDS ; Funds are wired/disbursed

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