7 ways to sink your home loan application

By Peter G. Miller

There is no shortage of tips to get a mortgage, but there are also ways to lose one. That may come as a shock after so much preparation and paperwork, but borrowers with solid credit and strong incomes can miss a good mortgage deal because of a surprise snag they could have avoided.

Actions and decisions that seem minor or logical during the mortgage application process can have surprising consequences, such as delaying the loan and losing a locked interest rate or even rejection of a mortgage application altogether.

Here are seven traps to avoid whether financing or refinancing a residence:

CHANGING JOBS

The Qualified Mortgage Rules released in early 2014 say lenders have an obligation to verify your ability to repay the loan. This means lenders must check both your income and the source of your income. If you change jobs in the middle of the loan process, the lender will have to get fresh information from the new employer, a task that can delay processing. If you've locked a mortgage rate and the loan does not close by the lock expiration date, it can mean the loss of a low interest rate.

Another reason changing jobs is a problem is that lenders like to see employment and income consistency. Taking a new teaching position after a 10-year career in teaching means you're in the same field, but going from teaching to transmission repair or from a salary to commissions as a real estate agent is a leap that may not point to the employment and income consistency that lenders want to see. The issue is not the new job or the choice you have made, but rather the lack of an employment history in the new field.

The bottom line: It is advisable to keep your job until after the loan closes.

MAKING A BIG PURCHASE

Lenders will check your credit initially when you apply for a loan. They will also sometimes re-check your credit prior to loan closing. The last thing they want to see is a big purchase on credit, so don't buy a car, truck, piano, refrigerator, etc. In fact, don't make any big purchases at all. When you apply for a loan, lenders must assure that you meet certain standards. Those standards – things such as the loan-to-value ratio (LTV), down payment amount and source, and your debt-to-income ratio (DTI) – are carefully measured. By making a big purchase, borrowers can cause the numbers to change. That means the numbers need to be run again, and if they exceed guideline maximums, the loan must be restructured and could potentially be declined.

The bottom line: Live like a hermit until the loan is closed.

MAKING LARGE DEPOSITS

It might seem counterintuitive, but big deposits in savings or checking accounts can create additional scrutiny from lenders. Lenders want to know that borrowers have the ability and discipline to save, especially for a down payment. While documented gifts may be welcome, the sudden appearance of large deposits can set off an alarm with loan underwriters, the people who check borrower applications against mortgage guidelines. Is the deposit a loan from a family member or friend, whereby a repayment is expected? If so, what are the terms of repayment? The monthly payment would have to be included as a liability and counted against the borrower's income. This could cause the debt-to-income ratio to exceed guidelines.

The bottom line: If you receive a big deposit immediately preceding and/or during the application period – a bonus, for example – tell the lender and document the source.

NOT DISCLOSING/REPORTING DEBT

By looking at your loan file documentation such as bank statements or paycheck stubs, the underwriter will check for unreported debts not included in your credit report. Lenders want to know about every debt because they must assure that your finances meet loan standards.

The bottom line: Disclose and report all of your debt.

OPENING NEW LINES OF CREDIT

A large study in 2013 by Equifax showed that "the vast majority of mortgage borrowers are forthcoming about their debts during the initial mortgage application; however, the problem occurs during the 'quiet period' between the original credit file pull and the loan closing. Almost one-fifth of all mortgage borrowers, including those with solid credit scores and debt-to-income (DTI) ratios, apply for at least one new trade line during this period."

Borrowers sometimes incur additional debt without thinking it will have an impact on their mortgage application. Imagine there is a sale on new cell phones and you can get 20 percent off if you buy them with the store's credit card, so you open an account and get your new phones with no money due for the next three months. By opening the account, you have created another line of credit. That credit line, and what you borrow, can change your application numbers and jeopardize your application.

The bottom line: Don't open any new credit lines until the loan closes.

MISSING ONE OR MORE DEBT PAYMENTS

If you miss a payment during the loan application process – particularly a mortgage payment – and the lender re-checks your credit report, it could result in a much lower credit score and could derail your loan application.

A related concern is an incorrect late or missed payment showing up on your credit report. In this case, you will have to contact the credit-reporting agency to show that the item is incorrect or out of date. Documentation will be required and speed is important because if you have locked your loan rate you don't want a credit dispute to slow the application past the lock deadline.

The bottom line: Pay every bill immediately when it comes due during the application process, because paying early assures accounts are properly credited. And keep careful records.

CLOSING CREDIT CARD ACCOUNTS

This is another counterintuitive problem. If you close a credit card account, isn't that a positive financial event? Seems reasonable, but in practice if you close an account your credit score might decline and a lower credit score can result in a higher mortgage rate. Lenders are very interested in credit. They like to see that you have credit and that by and large you do not use much of it.

Imagine you have three credit cards: Card A has a $5,000 limit and you have borrowed $1,000. Card B has a $7,000 limit and you have $3,000 outstanding. Card C has a $6,000 limit and you have a $0 balance. In total, you have $18,000 in available credit and $4,000 outstanding balances, so 22 percent of your available credit is in use. If you close Card C, the numbers look like this: You have $12,000 in available credit and $4,000 in outstanding balances, so 33 percent of your available credit has been used. That is a big difference. By closing one account, it appears that your credit usage has increased quickly and substantially.

The bottom line: Leave credit accounts alone until the mortgage has closed.

So there you have it, seven ways to lose a loan application that can be avoided with a little prudence and planning.

If you have any questions, please give me a call:

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