

Pre-Qualifying Debt Ratio - Case Study

Joseph and Patricia Parker intend to refinance their two home mortgages by combining them into one 15-year fixed rate loan at 7%. Their current first mortgage is a 30-year loan at 8% with 24 years left to pay. The P&I is \$1,100.65 and the outstanding balance is \$140,737.94. The second mortgage was for 10 years at 9.5% with eight years left to pay. The P&I payment is \$517.59 and the outstanding balance is \$34,712.24.

Included in the new housing payment will be property taxes of \$125.00/month and \$30.00/month for homeowners insurance. Because they are borrowing more than 80% LTV, they will also have a \$65.00/month premium for private mortgage insurance.

In addition to the new mortgage, they have three years left on a car loan at \$425.00/month. They have four outstanding credit cards with minimum payments of \$175.00, \$100.00, \$90.00 and \$65.00/month. Patricia has a student loan with five years left, costing \$125.00/month. They also have a finance company loan for five years with a \$110.00 monthly payment.

The total closing costs and pre-paid finance charges will total \$4,549.82 and the Parkers want to include them in the new loan.

Joe works as a line foreman at a local manufacturing plant. He regularly works 40 hours a week and earns \$19.50/hour. He also receives non-taxable military disability pay of \$1,850.00/month. Patricia is working as an office manager of a large medical practice and earns a salary of \$50,000.00/year.

The Parkers recently had the house appraised at \$200,000.00.

The Parker's projected new P&I payment is \$1,617.89.

Case Study Exercise

Complete the debt ratio worksheet and answer the following questions.

1)	What is the Parker's new loan amount?	\$ 180,000.00
2)	What is the LTV of the new loan?	90 %
3)	How much will their PITI payment be?	\$ 1,837.89
4)	What will the Parker's front-end" debt ratio be?	19 %
5)	What will the Parker's "back-end" debt ratio be?	30 %
6)	How much would it cost the Parkers if they chose to pay one discount point to buy the rate down?	One Point = \$ 1,800.00
7)	Bonus Question: If the Parkers were purchasing a home with the same terms and loan amount of \$180,000 and they were closing on April 18th, how much pre-paid interest would they be required to bring to the closing table?	\$ 448.76

Debt Ratio Worksheet

Borrower(s): Joseph and Patricia Parker

Home value or sales price	Loan Amount	LTV	Term	Interest Rate
\$200,000	\$180,000	90%	15 years	7%

Income	Housing Payments	Other Debt Payments
Borrower Base \$3,380.00	Principal Interest \$1,617.89	Auto Loan 1 \$425.00
Borrower Other \$	RE Taxes \$125.00	Auto Loan 2
Co-borrower Base \$4,166.66	Hazard Insurance \$30.00	Auto Loan 3
Co-borrower Other \$	Mortgage Insurance \$65.00	Installment Loan 1 \$125.00
Other Income \$	PITI \$	Installment Loan 2 \$110.00
	HO Dues, etc. \$	Installment Loan 3
		Installment Loan 4
		Revolving Loan 1 \$175.00
		Revolving Loan 2 \$100.00
		Revolving Loan 3 \$90.00
		Revolving Loan 4 \$65.00
		Other
		Other
		Other
		Other
Total Gross Income	Total Housing Payment	
\$ 9,859.16	\$ 1,837.89	
Disability Income Grossed Up	Total payments excluding installment loans with less than 10 months left to pay	
\$1,850 X 1.25 =	\$ 1,090.00/mo	
	Total monthly debt payments	Sub-Total
\$ 2,312.50	\$ 2,927.89/mo	\$1,090.00

Debt Ratios

$\frac{\text{Total Monthly Housing Payment}}{\text{Total Gross Income}} =$	\$ 1,837.89	Front- or Top-End Ratio
	\$ 9,859.16	19 %
$\frac{\text{Total Monthly Debt Payment}}{\text{Total Gross Income}} =$	\$ 2,927.89	Back- or Bottom-End Ratio
	\$ 9,859.16	30 %