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New Worries for Buyers Seeking Mortgages

By MARC SANTORA

AT last, the hunt was over.

After months of having her hopes dashed as swiftly as they were raised, viewing nearly 40 apartments and cycling through three different brokers, Deborah Herman finally found the perfect New York City home.

The moment she stepped into the two-bedroom apartment at 59th Street and First Avenue, with its oversized windows and sweeping views of the Queensboro Bridge, she just knew.

“We made an offer, and we got it,” she said.

That was in August. But it was only in February, nearly six months later, that she finally closed on the $1.15 million apartment.

In the intervening months, as she battled through a computer glitch and reams of documentation, Ms. Herman underwent a crash course in the complexities of navigating the mortgage market — which itself continues to undergo profound change.

The dread of not finding a lender after the market collapsed in 2009 has been replaced by uncertainty, confusion and frustration. According to brokers and lenders, the list of demands that stand between finding a place to buy and signing on the dotted line simply never stops morphing.

Changes proposed by the Obama administration to limit the role of the federal government in the mortgage market could further alter the rules of the road, for borrowers and lenders alike.

In New York City, there is particular concern about the federal government’s lowering the limit on the loans it will buy through the Federal National Mortgage Association, known as Fannie Mae, and the other housing finance giant, Freddie Mac.

Lower-income buyers could also be affected as the federal government seeks to limit the size of loans eligible to be bought by the Federal Housing Administration and Department of Veterans Affairs.

And let's not forget the federal government's proposal to eliminate the mortgage interest tax deduction for high-income earners; the changes in the way brokers will be compensated because of new regulations; and the fact that banks — despite recent profits — are still leery of lending. Taken together, all these elements create a situation that can paralyze potential buyers.

"Confusion and uncertainty can have the same impact as fear, unfortunately," said David S. Marinoff, a mortgage broker and managing director of the Guard Hill Financial Corporation.

Jonathan J. Miller, the president of the appraisal firm Miller Samuel and a market analyst for Prudential Douglas Elliman, said that even though affordability was at an all-time high, the usual equation involving interest rates, housing prices and personal income was almost irrelevant, if shoppers were unable to get mortgages to buy properties now tantalizingly within reach.

Private banks have swung too far in overcorrecting for the excesses of the credit boom from 2003 to 2008, he said, and are actively looking for ways not to lend.

"Housing does not truly recover until lending does," Mr. Miller said. "It is currently dysfunctional."

At the moment, the federal government, through Fannie and Freddie, is supporting about 90 percent of new mortgage loans, because banks are reluctant to make loans without government guarantees.

Currently, Fannie will buy loans of up to $729,750.

In September that limit will fall to $625,500 if no action is taken by Congress. Considering that the average Manhattan apartment in the last quarter of 2010 sold for $845,000, according to Mr. Miller, the change could affect a wide swath of the market.

For instance, even if a buyer put 20 percent down — which would be $169,000 for the $845,000 home — the total loan needed, $676,000, would still be above the new limit. The buyer would have to come up with $50,500 more to avoid paying the likely higher interest rates that a lender would charge on a "jumbo" mortgage, assuming that the buyer could qualify for a loan at all.

Yet many politicians have been calling for the federal government to lessen the role it plays in the mortgage market, even if the first steps prove painful. There are also plans, several years down the road, for ending Fannie Mae and Freddie Mac altogether.

Before the credit crisis in 2008, the limit on loans that Fannie would buy was $417,000. But when private lending all but disappeared and the government seized control of Fannie, the agency raised the limit of loans it would buy to $729,750 in more expensive cities like New York, Boston and San Francisco.

Banks simply weren't lending at that time, Mr. Marinoff said.

Real estate brokers and private mortgage lenders say that although 2010 was not as bleak as 2009, tighter credit has affected nearly every sector of the market in New York City.

For lower-income families, mainly outside Manhattan, the collapse in subprime lending to borrowers with a problematic credit history or low incomes has led to a boom in the number of loans backed by the F.H.A. and Veterans Affairs.

In 2005, fewer than 1 percent of all the loans issued in the city were backed by these agencies. In 2009, 16 percent of loans in the city were made possible by these federal programs, according to a recent report by the Furman Center for Real Estate and Urban Policy at New York University.

But another change being proposed by the Obama administration — shrinking the size of loans eligible to be bought by the F.H.A. and V.A. — could mean that less affluent buyers would need to come up with larger down payments as well. The government also said it would raise fees on F.H.A. borrowers for the third straight year.

The reasons for all the proposed changes are well chronicled, since it was easy credit and lax oversight that led to the bubble to begin with. And there has been bipartisan agreement that the role of the government needs to be scaled back.

Sarah Gerecke, the executive director of the Furman Center, says changes that bolster the confidence of borrowers and lenders will be a positive step.

But others worry about the effect that all the changes will have on a still-fragile market.

Borrowers and developers in New York City will also be facing new hurdles resulting from two regulations that Fannie put in place starting March 1. In the first, if a buyer wants to get a federally backed loan for an apartment in a new condominium conversion, Fannie is requiring that the property be inspected to determine how much cash the condo board needs to keep in reserve for capital improvements.

Especially for older buildings, the rule could require that developers keep more than 20 percent of their annual budget in reserve — much more than the current norm of 10 percent for condos.

One result, according to Orest Tomaselli, the chief executive of National Condo Advisors, an independent advisory group, could be higher maintenance fees.

Co-ops are not covered under the new regulation.

The other new regulation declared that Fannie Mae would not issue loans to people buying into converted condominium buildings in which more than 30 percent of the units remained rent-stabilized, unless the project had been previously approved.

These changes, taken together with lower limits on the loans Fannie will issue, could severely affect what is still a halting recovery, Mr. Tomaselli said.

Beyond the new rules and regulations, even those who qualify for a loan can be flummoxed by the process of getting from preapproval to closing.

Ms. Herman, who bought the apartment overlooking the Queensboro Bridge, said she had been armed with $440,000 in cash in the bank and tax returns from the previous three years showing an annual income of $700,000 to $1.1 million.

Weeks turned to months as Ms. Herman, who owns a linen supply company, awaited final approval on the loan. And every 30 days she was required to update all the financial information she had turned over to the bank.

Then, at some point during her wait, a glitch surfaced in the electronic transfer of her mortgage payment for her Florida home, making it seem as if she had missed a payment.

Her credit score fell to 670 from 740, and the deal almost collapsed. Only after another flurry of letters, a phone call from her lender in Florida to the prospective lender in New York, and another three-week delay, did the matter get resolved.

She had always planned to put 20 percent down, but as the deal drew closer, she was told by the New York lender that the only way she would get the seven-year adjustable-rate mortgage at 3.5 percent was to put 38 percent down, bringing the amount below the $729,750 ceiling for a federally guaranteed loan.

“Fortunately,” she said, “I had the money.”