



## **What Is a Mortgage Contingency?**

Most real estate contracts include contingency clauses. These are statements indicating the sale is conditional on something else happening. One of the most common contingencies is for a mortgage. The contract allows a limited amount of time for the buyers to be approved for a mortgage in order to buy the property. If the buyers aren't approved within the time frame, then the contract can be voided.

### **Components**

The wording of a mortgage contingency varies among contracts but generally includes a time frame, or deadline, by which the contingency must be met and thresholds for the mortgage terms. For instance, the contingency might give the buyer 20 days to obtain a mortgage commitment for a 30-year fixed rate loan at or below 5 percent with no points. The buyer has the option of terminating the contract if he can't get a loan within those parameters. There is no penalty for dropping out of the contract because a mortgage contingency can't be met.

### **Contingency Removal**

The manner in which a loan contingency is removed also varies among contracts. Some contracts are automatically canceled unless the buyer removes the loan contingency in writing by the deadline. In others, the contingency is automatically removed at the contingency deadline unless the buyer cancels the contract in writing before the deadline. Texas standard residential real estate contract specifies the buyer must remove the contingency or cancel the contract, in writing, before the end of the contingency period.

### **Mortgage Commitment or the Mortgage Itself?**

In the heyday of the real estate bubble, if you got what is called a "commitment letter" from a bank, in which the bank conditionally promises to make you a loan, you could rest assured you would get the loan. A commitment letter meant you could remove the loan contingency. But after the housing-induced recession hit, banks began taking their small-print conditions very seriously. One condition might be a deadline for the loan to fund. This is the date by which the sale must close, or finalize. A lot of details can delay the closing. In the past, if the deadline was not met, the bank would extend the loan--maybe



for a fee. Today, after the deadline passes, all bets are off. Maybe you'll get the loan; maybe you won't. In the meantime, if the buyers have removed the loan contingency

because they had the commitment letter but then lose the loan because the sale was delayed a day or two, they may find themselves in a contract they are obligated but unable to fulfill. Consequently, real estate contracts should be written to address this situation.

### **Mortgage Application Obligation**

In a seller's market, buyers sometimes rush to get into contract, whether they are seriously committed to purchasing the property or not. Buyers include contingencies in the contract so that if they find a property that more closely meets their needs they can cancel the initial contract and close on the preferred property. For this reason, some contracts, including Texas, contain a directive to buyers to "act diligently and in good faith to obtain the designated loan." If you sign a contract contingent on your obtaining a loan, you are obligated to try to get that loan.

### **Other Considerations**

The wording in a mortgage contingency is crucial. Failing to adhere to the strict instructions in the clause could result in a buyer being on the hook for a property even though he couldn't get a loan. One of the boilerplate conditions in a commitment letter is that the appraisal comes in at or above the price of the property. If the real estate contract does not have a separate appraisal contingency, then you probably don't want to remove the loan contingency until the appraisal is completed and approved by the lender. Commitment letters, like real estate contracts, vary.