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Should a Home's Energy Cost Be a Factor in Approving Your Mortgage?

REAL ESTATE TODAY

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A blog post on grist.org caught my attention this week. It stated that the energy cost of the average American home is $2,340 per year, 23% higher than the average property tax burden and three times the average cost of homeowner's insurance.

Yet, this cost of ownership — unlike taxes & insurance — is not considered when lenders calculate whether you can afford a particular mortgage on a particular home.

The whole process of approving a loan involves figuring out whether you can afford your payments. Lenders look at your debt-to-income ratio, for example, to see whether your current debts, when added to the debt for the contemplated mortgage, would be sustainable for you.

The last few years' wave of foreclosures was, indeed, the result of people getting into mortgages which they could not afford, partly because of their other obligations. At the height of irresponsible loan approvals in 2005-2006, loans were approved little regard to debt ratios and without verifying buyers' income assertions.

Now the pendulum has swung the other direction, and lawmakers and regulators are looking to eliminate any loophole that might permit a "bad" mortgage to be written.

With energy costs being the single biggest cost of ownership for a home, I have to agree that it makes sense to consider the energy efficiency of a given house — or at least the easily documented cost of heating and cooling it — along with taxes, HOA dues and insurance, when determining whether the prospective buyer can afford to purchase the home and therefore can be reasonably expected to repay the loan.

Sen. Michael Bennet is expected to introduce a bill this fall placing this additional documentation burden on lenders, but I'm not convinced this is the best way to achieve the desired result. It could well result in putting more homes out of range for more would-be buyers, endangering the recovery.

I like an alternative approach suggested by one of my mortgage colleagues, Shelley Ervin. She suggests that a reduced interest rate or tax credit be offered on homes which are energy efficient and/or have solar installations which reduce energy costs. This could incentivize and reward current owners of homes for making such improvements to their home knowing that it would make their home more attractive to buyers in a competitive housing market.

A link for the mentioned grist.org post can be found at JimSmithColumns.com.