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## **Self-Employed Workers Face Mortgage Hurdles**

When self-employed workers apply for a mortgage, the biggest challenge is demonstrating they meet the lender's income requirements.



ILLUSTRATION: CHRIS GASH

By

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Being your own boss allows for innovation and independence. But the self-employed also face difficulties when applying for a mortgage.

The biggest hurdle, experts say, is demonstrating they meet the lender's income requirements. Self-employed workers don't receive a W-2 form, the document that shows annual wages and withholding amounts. Instead, lenders need to rely on tax returns to verify a self-employed applicant's income. That's a challenge for lenders, because on one hand, self-employed applicants need to show enough income to qualify for a mortgage. On the other hand, they want to lower their taxable income by taking deductions and write-offs that they're legally entitled to.

"That's sometimes where self-employed people struggle, because they may not be showing enough income to qualify for the mortgage even though all the other characteristics of their credit profile look OK," says Scott Witherspoon, chief credit officer of Affinity Federal Credit Union, a lender in Basking Ridge, N.J.

Self-employed business owners often take tax write-offs, such as depreciation of office equipment. The amount is deducted from their business income, even though it's a noncash transaction. Personal expenses, such as car leases or travel and entertainment costs, are frequently covered by the business as well, so the net income reported on the tax return may not accurately reflect the true earnings of the business.

"You want to show as much income as possible to the lender so they know you can afford the mortgage, but pulling all these personal expenses out doesn't reflect the operations of the business," says Stephen G. Rosen, a certified public accountant in Boca Raton, Fla. "You need to help the lender understand that the business is making more money than you're showing."

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—CPA Stephen G. Rosen

Mr. Rosen says he often writes letters on behalf of his clients to help lenders better understand their business operations. He also provides profit-and-loss statements in which he removes personal expenses. That helps to reconcile the difference between the reported income on the tax return and the actual income the borrower claims on the mortgage application.

Another challenge for a self-employed mortgage applicant is the complexity of the tax returns they provide to the lender. "You have to figure out what kind of entity they own, what type of business they're in and how the income is flowing from the business return to the personal tax return," says Matt Hackett, operations manager for Equity Now, a direct mortgage lender in New York.

Mr. Hackett says Equity Now has approved jumbo loans that other lenders rejected. "We meet people all the time who were denied by another lender that could not understand or calculate self-employment income," he says. "We are experts at determining the cash flow of a business to help self-employed borrowers qualify for a mortgage."

A recent example: The applicant's business had a net operating loss that was being carried forward to offset present income. The business had actually been profitable for two years, but was still showing the paper loss on its returns. Equity Now added the loss back into the applicant's business income and was able to approve the loan.

*Here are a few things to consider if you're self-employed and plan to apply for a jumbo mortgage.*

**Find a good accountant.**

Not only can an accountant help explain your business and its cash flow to a potential lender, but he or she can provide invaluable advice on structuring that loan to benefit both the business and personal tax situations.

**Seek business-savvy underwriters.**

Make sure your lender has sufficient expertise to analyze your tax returns, both business and personal. Staff underwriters should be able to understand a Schedule C and all other schedules annexed to the tax return. "You need a lender who can actually go through those forms in detail and know which expenses to add back in order to properly qualify and maximize the amount of mortgage that person could qualify for," says Mr. Witherspoon.

**Consider a mortgage broker.**

Rather than applying to a direct lender, consider a mortgage broker, who works with many different lenders and can try to find the best program to fit your situation. "Self-employed applicants are not cookie-cutter loans," says Mat Ishbia, president and chief executive officer of United Wholesale Mortgage in Troy, Mich. An independent mortgage broker can also look for a portfolio lender, which will have more flexibility on underwriting than a lender planning to sell the jumbo to an investor.