

Buying a Home

Source: U.S. Department of Housing and Urban Development.

Shopping for a Loan

Your choice of a lender and type of loan will influence not only your settlement costs, but also the monthly cost of your mortgage loan. There are many types of lenders and types of loans to choose from. Many banks, savings associations, mortgage companies, and credit unions provide home mortgage loans. You can often find a listing of some mortgage lenders in the yellow pages and a listing of rates in your local newspaper.

Mortgage Brokers

Some companies, known as "mortgage brokers" offer to find you a mortgage lender willing to make you a loan. A mortgage broker may operate as an independent business and may not be operating as your "agent" or representative. Your mortgage broker may be paid by the lender, by you as the borrower, or by both. You may wish to ask about the fees that the mortgage broker will receive for its services.

Government Programs

You may be eligible for a loan insured through the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs or similar programs operated by cities or states. These programs usually require a smaller downpayment. Ask lenders about these programs. You can get more information about these programs from the agencies that run them.

CLOs

Computer loan origination systems, or CLOs, are computer terminals sometimes available in real estate offices or other locations to help you sort through the various types of loans offered by different lenders. The CLO operator may charge a fee for the services the CLO offers. This fee may be paid by you or by the lender that you select.

Types of Loans

Loans can have a fixed interest rate or a variable interest rate. Fixed rate loans have the same principal and interest payments during the loan term. Variable rate loans can have any one of a number of "indexes" and "margins" which determine how and when the rate and payment amount change. If you apply for a variable rate loan, also known as an adjustable rate mortgage (ARM), you should receive a disclosure and booklet (as required by the Truth in Lending Act) that will further describe the ARM. Most loans can be repaid over a term of 30 years or less. Most loans have equal monthly payments. The amounts can change from time to time on an ARM depending on changes in the interest rate. Some loans have short terms and a large final payment called a "balloon." You should shop for the type of home mortgage loan terms that best suit your needs.

Interest Rate, "Points," & Other Fees

Often the price of a home mortgage loan is stated in terms of an interest rate, points, and other fees. A "point" is a fee that equals one percent of the loan amount. Points are usually paid to the lender, mortgage broker, or both, at the settlement or upon the completion of the escrow. Often, you can pay fewer points in exchange for a higher interest rate or more points for a lower rate. Ask your lender or mortgage broker about points and other fees. A document called the Truth in Lending Disclosure Statement will show you the "Annual Percentage Rate" (APR) and other payment information about the loan for which you have applied. The APR takes into account not only the interest rate, but also the points, mortgage broker fees, and certain other fees that you have to pay. Ask for the APR before you apply, to help you find the loan that is best for you. Also ask if your loan will have a charge or a fee for making payments before they are due ("prepayment penalty"). You may be able to negotiate the terms of the prepayment penalty.

Lender-Required Settlement Costs

Your lender may require you to obtain certain settlement services, such as a new survey, mortgage insurance, or title insurance. It may also order and charge you for other settlement-related services, such as the appraisal or credit report. A lender may also charge other fees, such as fees for loan processing, document preparation, underwriting, flood certification, or an application fee. You may wish to ask for an estimate of fees and settlement costs before choosing a lender. Some lenders offer "no cost" or "no point" loans but normally cover these fees by charging a higher interest rate.

Comparing Loan Costs

Comparing APRs may be an effective way to shop for a loan. However, you must compare similar loan products for the same loan amount. For example, compare two 30-year fixed rate loans for \$100,000. Loan A, with an APR of 8.35%, is less costly than Loan B, with an APR of 8.56%, over the loan term. Before you decide on a loan, you should also consider the up-front cash you will be required to pay for each of the two loans.

Another effective shopping technique is to compare identical loans with different up-front points and other fees. As an example, assume that you are offered two 30-year fixed rate loans for \$100,000, both at 8% and with equal monthly payments, but the up-front costs are different. Loan A is set at 2 points (\$2,000) and has lender-required costs of \$1,800, totalling \$3,800 in costs. Loan B is set at 2¹/₄ points (\$2,250) and has lender-required costs of \$1,200, totalling \$3,450 in costs. A comparison of the up-front costs shows Loan B requires \$350 less than Loan A. However, your individual situation (how long you plan to stay in your house) and your tax situation (points can usually be deducted for the tax year that you purchase a house) may affect your choice of loans.

Lock-Ins

"Locking in" your rate or points at the time of application or during the processing of your loan will keep the rate and/or points from changing until settlement or

closing of the escrow process. Ask your lender if there is a fee to lock-in the rate and whether the fee reduces the amount you have to pay for points. Find out how long the lock-in is effective, what happens if it expires, and whether the lock-in fee is refundable if your application is rejected.

Tax and Insurance Payments

Your monthly mortgage payment will be used to repay the money you borrowed plus interest. Part of your monthly payment may be deposited into an “escrow account” (also known as a “reserve” or “impound” account) so your lender or servicer can pay your real estate taxes, property insurance, mortgage insurance and/or flood insurance. Ask your lender or mortgage broker if you will be required to set up an escrow or impound account for taxes and insurance payments.

Transfer of Your Loan

While you may start the loan process with a lender or mortgage broker, you could find that after settlement another company may be collecting the payments on your loan. Collecting loan payments is often known as “servicing” the loan. Your lender or broker should disclose whether it expects to service your loan or to transfer the servicing to someone else.

Mortgage Insurance

Private mortgage insurance and government mortgage insurance protect the lender against default and enable the lender to make a loan which the lender considers a higher risk. Lenders often require mortgage insurance for loans where the downpayment is less than 20% of the sales price. You may be billed monthly, annually, by an initial lump sum, or through some combination of these practices for your mortgage insurance premium. Ask your lender if mortgage insurance is required and how much it will cost. Mortgage insurance should not be confused with mortgage life, credit life, or disability insurance, which are designed to pay off a mortgage in the event of a borrower's death or disability. You may also be offered “lender paid” mortgage insurance (LPMI). Under LPMI plans, the lender purchases the mortgage insurance and pays the premiums to the insurer. The lender will increase your interest rate to pay for the premiums—but LPMI may reduce your settlement costs. You cannot cancel LPMI or government mortgage insurance during the life of your loan. However, it may be possible to cancel private mortgage insurance at some point, such as when your loan balance is reduced to a certain amount. Before you commit to paying for mortgage insurance, find out the specific requirements for cancellation.

Flood Hazard Areas

Most lenders will not lend you money to buy a home in a flood hazard area unless you pay for flood insurance. Some government loan programs will not allow you to purchase a home that is located in a flood hazard area. Your lender may charge you a fee to check for flood hazards. You should be notified if flood insurance is required. If a change in flood insurance maps brings your home within a flood hazard area after your loan is made, your lender or servicer may require you to buy flood insurance at that time.