BECOMING A SUCCESSFUL HOMEOWNER

PMI

PMI

Expanding Homeownership Opportunities…

PMI is proud of our efforts to assist homebuyers through an array of innovative programs and initiatives. We've become the MI leader in the emerging markets business segment because we recognize the enormous potential of this business – one of the fastest-growing markets ever.

PMI believes strongly in the importance of supporting first-time homebuyers. Through professional counseling homebuyers can understand the obligations and benefits of homeownership. We've provided such assistance for more than 45,000 new homeowners in the last six years. PMI also sponsors post purchase counseling for homebuyers facing financial challenges.

Throughout the 21st century, we'll continue to make affordable housing our top priority. PMI is in the homeownership business. We're committed to making the 'American Dream' attainable for as many families as possible in the United States and elsewhere around the world.

L. Stephen Smith

L. STEPHEN SMITH
Chairman and CEO
THE PMI GROUP, INC.

CREDIT RELEASE AGREEMENT

In an effort to assist you in the event of financial difficulty, PMI Mortgage Insurance Co. has contracted with the National Foundation for Consumer Credit ("NFCC") and its member agencies. NFCC is a non-profit organization with a national membership of non-profit agencies to provide you with free credit and financial counseling.

If you are delinquent on your loan payment, your lender, servicing agent and/or agent designee may wish to release information about the condition and/or status of your home loan to NFCC for the sole purpose of providing you with the opportunity to obtain free financial counseling services. If NFCC, your lender, servicing agent and /or agent designee determines that you might benefit from more specific face-to-face counseling, you may be referred to a member agent of NFCC. You may refuse to give your authorization to release your information to NFCC. If you refuse to permit your information to be released, you may not be able to take advantage of NFCC's free counseling services. **All information provided to NFCC remains confidential and will not be released to any other party except as expressly permitted by law.**

Release Authorization/Opt-Out

☐ I give my lender, servicing agent and/or agent designee permission to disclose credit information pertaining to the past due status and/or any other information pertinent to my inability to pay my loan, to NFCC or a local agent of NFCC.

☐ I do not consent to the disclosure of my personal credit information or loan payment history to NFCC or any other agency

Dated this _______________ day of _______________, 20______.

____

BORROWER SOCIAL SECURITY NUMBER

____

SIGNATURE

Please fill out this form and remove it from the guide. Return this form to you're loan representative (broker, lender, processor, or underwriter)

TABLE OF CONTENTS

Introduction

The purpose of this guide is to help you succeed in making your dream of homeownership a long-term reality. As you know, dreams don't just happen – they require work, planning, and *(occasionally)* sacrifice. Use this guide to chart the steps you need to take and to prepare for the challenges ahead.

Once you have completed this guide and Worksheets 1 to 3 plus 8 to 10, you will be scheduled for a telephone conversation with a Consumer Credit Counseling Services (CCCS) housing counselor. The counselor will review the material with you and can answer any remaining questions you may have. By the end of the session, you should be able to:

- List at least three advantages of owning vs. renting your home and three challenges you will face as a homeowner – challenges you did not worry about as a tenant;
- Describe three factors that determine how large a mortgage you can afford;
- List and define the four parts of your mortgage payment and where/when to make the payment;
- Detail two ways you can improve your credit profile;
- Explain the purpose of the closing or settlement process and at least one step you can take to prepare for it;
- If an emergency arises and you find you cannot make your mortgage payment on time, describe what steps to take and when.

Again, we want you to succeed. It is possible to achieve your dream of becoming a successful homeowner!

Chapter I

Homeownership:
The Impossible Dream?

Maybe you have been thinking about buying your own home for a long time. Or maybe a friend recently encouraged you to take this step. Perhaps you come from several generations of renters and are the first family member to consider homeownership. Before you take that final step, let's review the pros and cons one last time:

Renting—On the Plus Side

There are pluses to renting an apartment or house. For example:

- Renting an apartment typically requires less upfront cash than a buying a home.
- You do not have to worry about ongoing maintenance problems. If the toilet begins to leak, you simply contact the apartment maintenance crew.
- If you need to move, giving notice to a landlord is much easier and less time-consuming than selling a house or condo.
- During those months when money is a little tight *(like around the holidays)*, your landlord may be willing to accept a partial rent payment or even give you a few days to catch up on what you owe.

Renting—On the Minus Side

Of course, there are also negative aspects to renting:

- Your rent, depending on the terms of your lease, could increase each year.
- You may not be able to persuade the landlord to paint the walls your favorite color—dark purple.
- Your rent provides shelter for you and your family but no potential for building equity. *(Equity represents the portion of your property you own debt-free and is an important factor in creating personal wealth.)*

And you could probably add several other pros and cons to these lists.

Homeownership—On the Plus Side

What about homeownership? On the plus side:

- Homeowners may deduct their interest and property tax payments from their federal income tax.
- As you pay down the amount you owe your lender, your equity in the property increases. If the value of your property increases *(or appreciates)*, your equity also increases.
- You may customize your property and its décor, as you see fit.
- You own something tangible that you can leave to your heirs.

Homeownership—On the Minus Side

But let's not forget the cons to homeownership:

- Buying a home requires significant upfront cash. These upfront expenses typically include:
  - In most cases, your lender will require that you make a **down payment**, rather than lending 100% of the sales price of your house. The theory is that you will be less likely to stop making mortgage payments if you have invested your own cash in the property. *(We will discuss down payments in more detail in Chapter II.)*
  - Before ownership is legally transferred to you, there will be a formal closing or settlement. This process involves expenses for the lender, closing agents, and others—expenses you will pay. You will also be required to prepay certain monthly costs. The total **closing costs** you will owe may range from 3% to 10% of the sales price depending on the terms of your mortgage. Remember that these closing costs are in addition to the down payment. *(We will discuss closing costs in more detail in Chapter III.)*
- Your overall housing expenses will most likely increase. For example, heating and air-conditioning a two-story townhouse is probably more expensive than heating and air-conditioning a single-level 2-bedroom apartment. You will also face maintenance/upkeep costs and property taxes *(and homeowner association fees if you are moving into a community that requires these).*
- Your increased maintenance responsibilities mean less free time. You may have to cut back on weekend softball games to mow the lawn or clean out the gutters.
- It will typically take longer to sell a home than it will to give your landlord notice.
- Your property may depreciate *(or decrease)* in value through no fault of yours. For example, if there is a regional downturn in the economy and many people lose their jobs, they may be forced to put their houses on the market. Many houses with few buyers will result in lower prices.
- If an emergency arises and/or you have not been wise in your spending/saving habits, you risk the ultimate danger of losing your home to foreclosure. Despite the myth, most lenders do not like foreclosing on homes because they will typically lose money in the process themselves. But the risk is real—you could lose your home and all of the money, time, and love you have invested in it. *(We will review steps to take if an emergency occurs and how to work with your lender.)*

So, are you really ready for homeownership? Review the following checklist to confirm where you stand:

Are You Ready for Homeownership Checklist

QUESTION	YES	NO
1. Do you have a steady job and income? *(Remember that you will no longer be dealing with a 'flexible' landlord.)*		
2. Do you plan on remaining in the same area for a few years? *(Remember that it's typically much easier to give notice to a landlord than it is to sell a home.)*		
3. Do you have enough set aside for your down payment and closing costs?		
4. Have you worked out how much more you can afford to spend each month on total housing costs—including higher utilities, for example?		
5. Do you currently have savings set aside for an emergency? *(It is recommended you have three months of mortgage payments in your bank account in case an unforeseen event occurs.)*		
6. Do you live within your means, avoiding credit card debt? *(Again, if you are not living within a spending/savings plan, you risk the ultimate danger of losing your home if an unforeseen event occurs.)*		
7. Do you now live within a budget plan—carefully considering major purposes and paying more than the monthly minimum required on your credit cards?		

How many "Yes's" did you check off? If they outnumber the "No's," you're in good shape. But carefully re-examine each "No" to make sure it's not a deal-breaker. Even if you are not quite ready to become a homeowner today, there's always tomorrow.

SUMMARY OF KEY POINTS

As we've seen above, there are both positive and negative aspects to renting and to homeownership. Do the pluses of homeownership outweigh the pluses of renting for you? Are you comfortable with the challenges and responsibilities of being a homeowner? The decision is yours to make. Don't let anyone push you into taking a step you're not yet ready for.

If you are ready, the transition from renter to homeowner is possible—with preparation and planning. In the following chapters, we will review your next steps.

Chapter II

Homeownership: *Buying a Home Means Borrowing Money*

Unless you are independently wealthy, you will probably need to borrow some money in order to buy your home. How much can you afford to borrow? In this chapter, we first review the factors lenders consider in making this calculation and then we will look at the additional factors you need to consider.

Lender Calculation—How Much Can You Afford to Borrow?

1. Income and Employment

Not surprisingly, lenders are interested in your income—its amount and stability. Typically, homeowners with a stable source of income will be more likely to repay the money borrowed. Lenders prefer two years of employment in the same job or industry. Self-employment must be thoroughly documented with tax returns and profit and loss statements.

> An old rule of thumb is that you can afford a sales price that is 2.5 times your gross *(before payroll deductions)* annual income. However, this calculation may underestimate your buying power if the interest rates charged by lenders are relatively low.

2. Other debts (for example, car and student loans, credit cards, etc.)

Lenders are concerned about the overall amount of debt you typically carry. There are two basic types of debt lenders consider—**installment** and **revolving**.

- With an installment loan, you have borrowed a set amount and are paying back the loan in equal monthly installments. Examples of installment loans are car loans and student loans.
- Credit cards are example of revolving debts—the amount you borrow and the amount you pay may change from month to month.

Remember that your income will have to cover your mortgage payment as well as your car loan, student loan, credit card payments, etc.

Traditionally, lenders have employed a pair of ratios to calculate how large your monthly mortgage payment should be. The first ratio is the housing expense ratio and covers only your monthly mortgage payment divided by your gross monthly income. *(Your gross monthly income is the amount you make before taxes and other deductions are taken out of your paycheck.)* The housing expense ratio used depends on the mortgage product; it may range from 28% *(the most conservative calculation)* to 33% or even higher.

Let's say that Angie makes $4,000 a month. She has applied for a mortgage product with a housing expense ratio of 33%. So her total monthly mortgage payment should be no higher than

$4,000	*(Gross Monthly Income)*
x .33	*(Total Housing Expense Ratio*
$1,320	*to cover her mortgage payment)*

This mortgage payment of $1,320 must include all four components or the total **PITI**:

- **P stands for Principal** or the amount of the loan you borrowed.
- **I stands for Interest.** Lenders charge you interest on the money you are borrowing.
- **T stands for Taxes.** Each month, your lender typically collects approximately 1/12 of the annual property taxes you owe, then makes the payment on your behalf when the tax bill is due. These monthly payments are placed in an escrow account from which the property tax payment is drawn. Lenders assume this responsibility to ensure that your property taxes are paid as required.
- **I (the final I) stands for Insurance.** Each month, your lender typically collects approximately 1/12 of the annual homeowner's *(or hazard)* insurance premium you owe, then makes the premium payment on your behalf. As noted above, these monthly payments are placed in an escrow account from which the insurance premium payments are drawn. Again, lenders assume this responsibility to ensure that your home remains insured.

The second ratio is the total debt ratio which takes into consideration student and car loans, credit card debt, and so on.

In Angie's case, the total allowable debt ratio for the mortgage product she is interested in is 41%. In other words, her PITI plus her normal monthly debts should not exceed 41% of her gross monthly income.

$4,000	*(Gross Monthly Income)*
x .41	*(Total Debt Ratio*
$1,640	*to cover PITI plus other debt payments)*

As more and more lenders adopt automated or computerized underwriting systems, ratio calculations are less strictly applied. Angie may, in fact, be approved for a mortgage payment higher than $1,320 depending on her credit profile and the amount of her down payment, among other factors.

3. Downpayment

As we mentioned above, lenders do not typically lend 100% of the sales price of the home you would like to buy. You are required to make a cash down payment, on the theory that you will be less likely to walk away from a property in which your own money is invested. Different mortgage products *(that we discuss below)* have different down payment requirements. The good news is that the tradition of a 20% down payment requirement is obsolete. Today you can find mortgage products that require as little as a 1% or 2% down payment.

The flip side of the down payment percentage is the loan-to-value *(or LTV)* ratio. For example, let's say that Angie is interested in a house with a sales price of $100,000 and is making a down payment of $5,000:

$100,000	*(Sales Price)*
-5,000	*(Down Payment)*
$ 95,000	*(Loan Amount)*

She would need to borrow $95,000 and her loan-to-value ratio or LTV would be:

$95,000 *(Loan Amount)* divided by $100,000 *(Sales Price)* = 95% = LTV

If Angie were making a down payment of only $2,000, her loan-to-value ratio or LTV would be:

$100,000	*(Sales Price)*
-2,000	*(Down Payment)*
$ 98,000	*(Loan Amount)*
$98,000	*(Loan Amount)* divided by $100,000 *(Sales Price)* = 98% = LTV

So, the lower the down payment, the more you need to borrow and the higher your LTV.

4. **Cash available after closing**

Lenders will examine how much cash you have on hand to pay for closing costs as well as your down payment. Remember that, at closing, you will be paying for expenses incurred by the lender, closing agents, and others related to the closing and settlement process plus certain prepaid monthly costs. The total **closing costs** you will owe may range from 3% to 10% of the sales price depending on the terms of your mortgage. The lender does not want you to walk away from the closing with no cash remaining in your pockets.

What if you don't have quite enough available funds for closing? Acceptable sources of cash include:

- A gift from a family member
- A grant or unsecured loan from a nonprofit or government agency *(a housing counselor could help you locate such a grant or unsecured loan)*
- A contribution from the seller or other interested party *(the builder, for example)*
- Sale of an asset

5. **Type of mortgage product**

Mortgage products can be broadly divided into two groups—products that are insured or guaranteed by the government and those that are insured or guaranteed by private mortgage insurance companies.

This mortgage insurance *(whether provided by a government agency or by a private company)* reimburses the lender or investor for losses if they foreclose on your loan. However, you *(the borrower)* pay the mortgage insurance premium.

Government Loans

Government loans include:

- VA loans are guaranteed by the Veterans Administration and available to eligible veterans. These loans require no down payment; the maximum loan amount is $203,000. For further information, access the Veterans Administration web site at www.va.gov or ask your lender.
- FHA *(Federal Housing Authority)* loans are administered by the U.S. Department of Housing and Urban Development (HUD). The down payment requirement is 3% to 5% and the maximum loan amount varies by region. For more information, access HUD's web site at www.hud.gov or ask your lender.
- RHS *(Rural Housing Service)* loans are administered by the U.S. Department of Agriculture and require very low or no down payment. To be eligible, you must meet income guidelines and purchase a home in a rural area. Your lender can confirm the eligibility guidelines for you.

Conventional Loans

If a loan is not insured or guaranteed by a government agency, it is considered to be a conventional loan. If you make less than a 20% down payment, you will probably be required to pay a mortgage insurance premium to a private mortgage insurance company. The advantage of private mortgage insurance is that you need less upfront cash to buy your home. You no longer have to wait until you have saved 20% of the sales price, as was true historically. You can now purchase a home with a minimal down payment of only 1 or 2%.

Under the Homeowners Protection Act of 1998, borrowers with a good payment record who have paid off 20% of the original loan amount may request that their premium be canceled. For some mortgages, the premium will be automatically canceled on the date the borrower has paid off 22% of the original loan amount. *(Automatic cancellation now occurs on FHA loans as well when they reach the 22% mark.)* Be sure to ask your lender about the cancellation policy of the mortgage product you apply for.

Interest Only Loan (IO)

Interest only loans can be fixed/fixed rate or ARM and feature an initial period where the borrower is paying interest, but no principal, resulting in a monthly mortgage payment that is below a normally amortizing loan. Interest only (IO) loans represent an increased risk due to:

- Lack of equity build-up in the early years of the loan.
- Payments when they become fully amortizing will be higher than those of a standard amortizing loan and may result in payment shock to the borrower.

Balloon Payment Mortgages

Balloon payment loans have periodic, level installments of principal and interest that do not fully amortize the loan over the loan term. The balance of the mortgage is due in lump sum at the end of the term.

Option Payment Mortgage

The Option Payment Mortgage can be a fixed-rate or adjustable rate loan. This loan offers a choice of monthly minimum payment options which may include a minimum payment *(which is generally less than fully amortizing)*, an interest only payment, a fully amortizing payment, and a 15 year amortized payment.

Negative Amortization – Potential and Scheduled

Negative amortization occurs when the payment rate is less than the interest rate and; therefore, the payment is not sufficient to pay the interest due on the loan and the shortfall is added to the total principal outstanding. This event could be driven by several different situations, such as:

- An increase in the interest rate occurs without a corresponding increase in the payment rate; or
- An increase in the interest rate occurs and the payment cap restricts the payment from increasing to an amount sufficient to pay the interest due; or
- The borrower has the option to pay an amount less than the amount required to pay the interest due.

Negative amortization can be classified into two types, scheduled and potential. Scheduled Negative Amortization occurs when the underlying structure of the transaction provides for a pre-defined payment amount and repayment schedule where the payment is not sufficient to cover the interest dues at some time during the term. Potential Negative amortization occurs when the underlying structure of the transaction provides, at some time in the future, the opportunity for one of the situations listed above to occur. Typically these situations are associated with adjustable rate mortgages. Since we do not know what the exact interest rate will be *(at the change date)* when the transaction is initiated, we must define the event as on that may potentially occur.

If potential negative amortization exists, the amortized loan balance may not exceed 115% of the original loan balance.

Growing Equity Mortgage (GEM)

GEMs are fixed-rate, adjustable payment loans which allow low beginning payments that increase on a pre-determined schedule over time. As payments increase, equity build-up is accelerated; hence the amortization term is reduced.

Graduated Payment Mortgage (GPM)

A Graduated Payment Mortgage (GPM) is typically a 30-year, fixed rate mortgage aimed at increasing affordability by offering lower initial payments. The first years' payments are interest only. Payments increase by 1-2% annually for a specified period of time *(generally 4 to 8 years)*. On the last change date, the new monthly payment will be sufficient to fully amortize the outstanding principal balance over the remaining term of the loan. An acceptable GPM may begin with interest only payments; payments increase 1-2% annually for specified period of time. Once the payment becomes sufficient to fully amortize the loan, the monthly payment is fixed for the remaining term of the loan.

6. Interest rate of the mortgage

As we explained above, your lender charges you interest for borrowing the money you need to buy your home. The higher the interest rate, the higher your mortgage payment.

However, in comparing different loan products offered by different lenders, you should look at more than the interest rate. For example, lenders also charge **discount points** which are 1% of the loan amount. These points represent an upfront payment of interest to the lender. Typically, the higher the interest rate, the lower the discount points charged and vice versa.

To help consumers compare loan products, the lender must also show you the APR (*or Annualized Percentage Rate).* The APR includes points and other charges in the calculation of what your mortgage will cost on an annualized basis. APRs are helpful in comparing loan products with different interest rates, different discount points, and other charges.

Fixed-rate vs. Adjustable rate

You also have a choice of fixed-rate and adjustable rate options.

- With a fixed-rate loan, the interest rate charged by the lender never changes over the life of the loan. So, the P *(Principal)* and I *(Interest)* portion of your PITI payment will not change. *(However, the T (Taxes) and I (Insurance) portion may change if your taxes or insurance premium changes.)* Many people prefer the stability of a fixed-rate loan.
- With an adjustable rate loan, the interest rate can increase or decrease. The variety of adjustable rate mortgages *(also known as ARMs)* is staggering. There are loans with rates that change each year, or every three years, or every five years. In some cases, the rate increases may be capped *(for example, the rate will never be higher than 5 point over the original rate)*. With other ARMs, there are payment caps, and if the cap is reached, the difference between what you would pay without the cap and what you are actually paying is added to your loan balance. When the amount you owe the mortgage lender grows over time, it's called **negative amortization**.

If you are interested in an ARM, make sure that you thoroughly understand all of the terms of the loan. You should receive a detailed written disclosure from your lender. Read it carefully and ask as many questions as necessary. You don't want to run into unhappy surprises in the future.

7. Length or term of the mortgage

The period of time during which you pay back the loan will also determine the amount of your payment. For example, if you apply for a traditional 30-year term, you will pay back your loan in 360 payments *(30 years times 12 months)*. If you apply for a 15-year term, you will pay back your loan in 180 payments *(15 years times 12 months)*. The longer the term of the loan, the lower the mortgage payments, as illustrated below. For that reason, many first-time home buyers prefer a 30-year loan.

Monthly Principal and Interest Payment
Loan Amount = $100,000 and Interest Rate = 7%

30 YEAR LOAN	15 YEAR LOAN
$665	$899

In the early years, most of your mortgage payment is applied to interest while in the later years, most of it is applied to principal. See the chart below for an illustration of how a mortgage is amortized or paid down over its term of 30 years:

Loan Amount = $100,000
Interest Rate = 7%
Term = 30 years

PAYMENT NUMBER	MONTHLY PRINCIPAL AND INTEREST PAYMENT	PRINCIPAL PORTION OF PAYMENT	INTEREST PORTION OF PAYMENT	LOAN BALANCE REMAINING
12	$665.30	$87.38	$577.92	$98, 984.21
24	$665.30	$93.70	$571.60	$97,895.00
36	$665.30	$100.47	$564.83	$96,727.06
48	$665.30	$107.74	$557.56	$95,474.67
60	$665.30	$115.52	$549.78	$94,131.76
120	$665.30	$163.77	$501.53	$85,812.78
240	$665.30	$329.12	$336.18	$57,301.30
360	$668.28	$664.40	$3.88	$0.00

8. Credit

What else does the lender examine in calculating how much you can afford? Your credit history—the amount and type of debt you carry plus how you repay it—plays a key role.

Where does a lender obtain your credit history? There are three major credit agencies or repositories in this country that maintain credit databases. A lender can contact them or individual credit bureaus for a copy of your credit report. Here is what Angie's credit report from one of the three agencies looks like:

YOUR FILE NUMBER: 10145296348
PAGE 1 OF 1
DATE THIS REPORT WAS PRINTED: 03/15/01

SOCIAL SECURITY NUMBER: 555-45-XXXX
BIRTH DATE: 05/31/1966
YOU HAVE BEEN IN OUR FILES SINCE: 03/96

CONSUMER REPORT FOR:

ALLWORTHY, ANGIE
1234 YOUR STREET
WASHINGTON, DC 20016

EMPLOYMENT DATA REPORTED:

ALLWORTHY UNLIMITED
DATE REPORTED: 03/99

YOUR CREDIT INFORMATION

THE FOLLOWING ACCOUNTS ARE REPORTED WITH NO ADVERSE INFORMATION

CAPITAL ONE BANK	#XXXX990	REVOLVING ACCOUNT
		CREDIT CARD
UPDATED 02/01	BALANCE: $1,209	INDIVIDUAL ACCOUNT
OPENED 09/99	MOST OWED: $2,000	PAY TERMS: MINIMUM $10

STATUS AS OF 02/2001: PAID OR PAYING AS AGREED
IN PRIOR 12 MONTHS FROM LAST UPDATE NEVER LATE

NORDSTROMFSB	#XXXX22339	REVOLVING ACCOUNT
		CHARGE ACCOUNT
UPDATED 02/01	BALANCE: $0	INDIVIDUAL ACCOUNT
OPENED 12/2000	MOST OWED: $689	CREDIT LIMIT: $3500

STATUS AS OF 02/01: PAID OR PAYING AS AGREED
IN PRIOR 48 MONTHS FROM DATE PAID NEVER LATE

AMERICAN HONDA		
FINANCE	#XXX908	INSTALLMENT ACCOUNT
		AUTOMOBILE
UPDATED 02/01	BALANCE: $0	INDIVIDUAL ACCOUNT
OPEN 04/96	MOST OWED: $7000	PAY TERMS: 48 MO. $158

STATUS AS OF 02/01: PAID OR PAYING AS AGREED
IN PRIOR 34 MONTHS FROM DATE CLOSED NEVER LATE

FLEET MORTGAGE	X889XXXXX	MORTGAGE ACCOUNT
		CONVENTIONAL REAL ESTATE MTG
UPDATED 02/01	BALANCE $125,898	JOINT ACCOUNT
OPENED 07/98	MOST OWED $215,000	PAY TERMS: 360 MO. $1455

STATUS AS OF 02/01: PAID OR PAYING AS AGREED
IN PRIOR 35 MONTHS FROM DATE CLOSED NEVER LATE

ED LOAN SVCS	XXX980XXX	INSTALLMENT ACCOUNT
		STUDENT LOAN
UPDATED 02/01	BALANCE: $1213	INDIVIDUAL ACCOUNT
OPENED 11/00	MOST OWED: $5,000	PAY TERMS: 108 MO. $62

STATUS AS OF 02/01: PAID OR PAYING AS AGREED

THE FOLLOWING COMPANIES HAVE RECEIVED YOUR CREDIT REPORT. THEIR INQUIRIES REMAIN ON YOUR CREDIT REPORT FOR TWO YEARS.

INQUIRY TYPE	DATE	SUBSCRIBER NAME
INDIVIDUAL	09/99	CAPITAL ONE
INDIVIDUAL	10/00	ED LOAN SERVICES
INDIVIDUAL	11/00	NORDSTROM
INDIVIDUAL	02/01	CONSUMER DISCLOSURE

(NOTE: CONSUMER DISCLOSURE INQUIRIES ARE NOT VIEWED BY CREDITORS.)

As we can see, Angie has an excellent credit history. She pays all of her bills as agreed, on time. And she is not overloaded with debt. Angie has only one department store-issued credit card and one bank-issued credit card.

Unfortunately, we cannot give TJ Consumer the same high marks for his credit behavior. See his credit report below:

Prepared for
TJ CONSUMER
I. Report number
XXXXXXXXXX

Information affecting your creditworthiness

Below is a summary of the information
Contained in this report.

II. Potentially negative items listed	
Public records	2
Accounts with creditors and others	5
Accounts in good standing	1

III. Credit information about you

SOURCE	DATE OPENED/ REPORTED SINCE	DATE OF STATUS/ LAST REPORTED	TYPE/TERMS/ MONTHLY PAYMENT	RESPONSIBILITY	CREDIT LIMIT/ HIGH AMOUNT	RECENT BALANCE/ RECENT PAYMENT	COMMENTS
General Motors	08/96 9/96	10/00 10/00	Installment 48 months $308	Individual	$35,000	$0 NA	Status: 3 30 day late payments
First USA	10/98 11/98	03/01 03/01	Revolving NA $0	Joint	$14,600 $13,500	$12,909 $1,235	Status: 2 30 day late payments and 1 60 day late payment
Macy's	11/96 12/96	03/01 12/99	Revolving NA $0	Joint	$350 $350	$0	Status: 1 90 day late payment
Universal Card Service	10/90 05/94	03/01 12/99	Revolving NA $0	Joint	$25,000 $12,300	$22,120 $1,240	Status: 2 90 day late payments
Wells Fargo Card Service	10/90 05/94	03/01 02/01	Revolving NA $0	Individual	$30,000 $15,000	$13,521 $1,000	Status: Open/ Never late
Sears	10/90 11/96	03/01 02/01	Revolving NA $0	Joint	$2,500 $578	$578	Status: Referred to collection agency

IV. Public records

Sears account referred to collection agency in 10/99. Balance remains uncollected.

Judgment filed 08/99 in District of Columbia. Plaintiff: Acme Management Company. Amount: $1,500. Satisfied: 12/99.

On only one of TJ's accounts are there no late payments. And a judgment was filed against TJ in 1999. In that same year, Sears referred his account to a collection agency and remains unsatisfied to this day.

Credit scores

Credit bureaus also provide lenders with credit scores based on the data in the report. A credit score is a statistical method of measuring your management of credit. It predicts the relative likelihood that you will repay your mortgage.

A credit score is calculated based on:

- **Your previous credit performance:** Do you pay bills on time? If not, how recently did late payments occur? How long did you remain delinquent on any bill at one time? Is there derogatory *(that is, negative)* credit on a public record—like a judgment, lien, or bankruptcy? If so, how long ago did it happen?
- **Current level of your debts:** How many consumer loans and open charge accounts do you have? Are you 'maxed out' on your credit cards—that is, are you borrowing close to the maximum allowed?
- **How old your debts are:** How long have you had debt? Generally, the longer your history of good credit management, the stronger your score.
- **Whether you have recently added new debt:** Are you out shopping for a new car while shopping for a new house? Or signing up for department store credit cards? Not a good idea.
- **The type of debts you take on:** What type of debt do you have? Department store credit cards? Installment credit with a local furniture store? Generally, this factor is not a critical element in the credit score.

A credit score does not consider race, gender, color, religion, national original or marital status. It also does not consider income, employment status or where you live.

Many mortgage lenders use the credit score formula developed by Fair, Isaacs and Company. The higher the FICO score, the better you look as a potential borrower.

Correcting errors on your credit record

It is possible for errors to appear on a credit report. If this happens, your credit score and probability of being approved for a mortgage loan could be damaged. So it's very important that you obtain a copy of your credit report from all three agencies before you apply for your mortgage loan. You can contact them by phone or via the Internet. In six states, you can obtain a copy of your report for free. Elsewhere, you will be charged a fee. Be sure to contact all three agencies because the information contained in each database is not identical.

THE THREE CREDIT AGENCIES OR REPOSITORIES

Equifax (www.equifax.com)	1-800-685-1111
Experian (www.experian.com)	1-800-397-3742
Transunion (www.transunion.com)	1-800-916-8800

If you do discover an error in your report, contact the creditor directly in writing. Also report the error directly to the credit agency *(that is, to Equifax, Experian, or to Transunion)* so that the error can be removed. The agency must investigate and respond within 30 days. If there is an unresolved dispute still outstanding when you apply for your loan, be sure to tell your lender and provide copies of your correspondence with the credit agency.

The Federal Trade Commission makes excellent resources available on their web site—www.ftc.gov. The publication, *Building a Better Credit Record*, can be printed from this site and provides specific guidance on correcting credit report errors.

How To Improve Your Credit Profile

- We start with the most obvious—**pay your bills on time**. And the payment must be at least the minimum due—not some portion of the minimum due. Your creditor will consider the "less-than-minimum-due" payment to be a late payment. Of course, your creditor will be happy to accept a payment that is larger than the minimum due.
- **Don't "max out" on your credit cards.** Avoid ongoing balances that are at or near the maximum allowed by each card. Too much debt can be unhealthy.
- **Pay more than the minimum payment** due on your credit cards. One example—paying off $500 at 18% at a minimum monthly payment of $15 will take 47 months and cost over $190 in interest. Paying off that same $500 at $35 per month takes only 17 months and costs only $67 in interest.

- **Limit the number of credit cards you have.** Otherwise, it's too tempting to take down additional debt and become over loaded.
- **Avoid impulse buying on major purchases.** In fact, save up for such purchases to avoid relying on credit altogether.
- Also remember that you are responsible for all **joint accounts** you've opened with another individual and for all loans on which you're the **co-signer.** If the other party charges items on the joint credit account and neglects to make payments as agreed, the bad news appears on your credit report as well as on theirs.
- **Review your credit report at least once each year.** Get copies from all three major credit agencies—Equifax, Experian, and Transunion. As we discussed above, errors are always possible as is identity theft.

By law, most unfavorable credit information must be dropped after 7 years. A bankruptcy remains on your record for 10 years.

> **NOTE:** Beware of ads that promise to fix or repair your credit overnight. Some go so far as to provide false social security numbers so you can start a new credit history from scratch! Needless to say, such efforts are illegal and will cost you time, money, and aggravation.

Nontraditional credit history

What if you do not have any credit cards or other debts that would appear on a credit report? You can still apply for a mortgage loan but you must provide documentation of your "nontraditional" credit history. Lenders are typically willing to consider written proof that you have paid the following items on time:

- Rent
- Utilities like electricity, gas, water *(if not included in rent)*
- Telephone
- Cable TV

Lenders might also consider documented proof of on time *(non-payroll-deducted)* payments made for medical, car or life insurance premiums. Other possible items include child care payments, school tuition payments, and local store credit. Remember that your goal is to prove to your lender in writing that you pay your debts when they are due.

Lender Calculation—Summary

Again, what factors does the lender consider in deciding what you can afford?

1. Income and employment
2. Installment and revolving debt
3. Down payment
4. Cash available after closing
5. Type of mortgage product
6. Interest rate of the mortgage
7. Length or term of mortgage product
8. Credit

So How Can You Estimate What You Can Afford?

Before you contact a lender, how can you estimate what you can afford? There are a number of available options.

- For example, you can consult a table that shows loan amounts, interest rates, and mortgage payments calculated using a 33% housing expense ratio. *(Of course, this table does not take into account your other monthly debts.)*

Gross Annual Income	20,000	25,000	30,000	35,000	40,000	45,000	50,000	55,000	60,000	65,000	70,000
Interest Rate	ESTIMATED LOAN AMOUNTS										
6.5%	62,900	78,720	94,400	110,200	125,900	141,690	157,400	173,200	188,900	204,600	220,400
7.0%	60,600	75,800	91,000	106,100	121,300	136,500	151,600	166,800	182,000	197,100	212,300
7.5%	58,400	73,100	87,700	103,300	116,900	131,500	146,200	160,800	175,400	190,000	204,800
8.0%	56,400	70,500	84,600	98,700	112,800	126,900	141,000	155,120	169,200	183,300	197,400
8.5%	54,400	68,000	81,600	95,200	108,890	122,500	136,110	146,800	163,300	176,900	190,500
9.0%	52,500	65,700	78,800	92,000	105,150	118,300	131,400	144,600	157,700	170,900	184,000
9.5%	50,800	63,500	76,200	88,900	101,600	114,300	127,000	139,700	152,400	165,180	177,890
10.0%	49,100	61,400	73,700	86,000	98,300	110,600	122,890	135,185	147,470	159,700	172,000
10.5%	47,500	59,700	71,300	83,200	95,150	107,000	118,900	130,836	142,730	154,625	166,500
11.0%	46,000	57,600	69,000	80,600	92,100	103,675	115,200	126,700	138,200	149,700	161,200

- There are several mortgage calculators available on the Internet. You should work with more than one calculator, however, because it's sometimes unclear what assumptions underlie the formulas being employed. Several web sites are noted in the Resources section of this guide.
- We developed Worksheets for you to use at the back of this guide. You can calculate the traditional ratios *(a 33% housing expense ratio and 38% total debts ratio)* to get a handle on what you can afford.

But we also recommend that you take into account your overall cash flow. In other words, lenders do not include food, gas, child care, video rentals and other daily expenses in their calculations. You should. The dream of homeownership can become more than you bargain for if your income is stretched too thin. Remember—simply because a lender approves you for a particular loan amount does not guarantee that you will be able to make the mortgage payments on time and meet all of your other daily expenses.

For assistance in calculating what you can <u>really</u> afford, consider working with a housing counselor who can help you put together a picture of your current financial situation. In the Resources section of this guide you will find suggestions on how to locate a housing counselor in your area.

How Do You Find a Mortgage Lender with the "Best" Product for You?

There are a number of sources for locating a mortgage lender:

- Ask a friend, family member, or co-worker who recently bought a home
- Does the bank where you keep a checking and/or savings account offer mortgage loans?
- Are you a member of a credit union that offers mortgage loans?
- Your local state housing finance agency may make funds available for low down payment mortgage loans to those who meet income and/or other guidelines. *(In the Resources section of this guide is information on how to locate the housing finance agency in your state.)*
- If you are comfortable searching for information on the Internet, you can use this tool to locate mortgage lenders. For example, the Fannie Mae web site provides a list of lenders in whatever geographical area you designate.
- If you are working with a real estate sales agent, he or she should be able to recommend lenders.

However you locate the lender, make sure that you are comfortable with the lender representative. The loan officer should readily answer all of your questions and should clearly understand your financial situation before recommending a specific mortgage product.

Mortgage Brokers

You can also work with mortgage brokers or individuals who deal directly with the lender on your behalf.

Of course, mortgage brokers do not work for free. Make sure you understand, before signing any paperwork, exactly what fees will be involved—both upfront fees and fees charged at closing.

One resource for locating a mortgage broker is the National Association of Mortgage Brokers at their web site, www.namb.org.

"Predatory" Lenders

Unfortunately, there is always someone ready to take advantage of unsuspecting consumers. In the mortgage arena, these are known as "predatory" lenders. There is no single definition of "predatory lending practices"—federal law offers no specific guidance while states have adopted a variety of standards. So how can you tell whether a lender is predatory?

Watch out for:

- Lenders that require a **lump sum credit life insurance premium** be added to the loan amount. Borrowers rarely benefit from such policies while adding the premium to the amount you borrow will inflate your mortgage payments. In fact, it means that you will be paying interest on the premium for the life of the loan! Again, these policies and the way they are funded offer more benefit to the lender than to you.
- Lenders that charge **fees you do not clearly understand**. Never be rushed into signing documents. A mortgage is the largest financial transaction you will ever take on, so feel free to ask questions and demand clear answers—not just "well, that's the standard in the industry."
- If the **rates, points, and fees are excessive**, watch out. You will only know whether this is true if you do your homework and contact at least 3 lenders for information *(as we discuss below)*.
- Don't let anyone talk you into **borrowing more than you can afford to repay or signing you up for a loan that is larger than the value of the house you're buying**. As noted above, lenders do not consider daily expenses in approving your loan application and predatory lenders will not give such matters a second thought!
- Don't sign a document with blanks that the loan officer promises to fill in later. You may be unhappily surprised by what appears in those blanks!
- Don't listen to a loan officer who encourages you to lie or somehow 'fudge' some of the information on your application.

- Be extremely wary of any unsolicited offers that arrive **in the mail, via the phone, or at your door**. If someone is that anxious to lend you money, there's almost always a very large catch!
- Watch out for loans with one large **"balloon" payment** at the end. Though the mortgage payments leading up to the balloon payment may be easy to manage, you cannot avoid that final lump sum. You will probably have to refinance the loan at that point but interest rates may be considerably higher, making your new mortgage payments higher as well. Look for a balloon mortgage that caps the interest rate at which you will refinance the loan.
- Ask whether the lender **reports your mortgage payments to the three national credit bureaus**. "Predatory" lenders tend not to do so. They want to keep their customers to themselves for fear that "good" borrowers will sign on with other lenders. But this practice is a disservice to you because your good repayment record is not being added to your credit profile and credit score.
- Stay away from loans that charge **prepayment penalties that run for five or more years**. You want to retain the flexibility of prepaying your loan or refinancing it entirely without paying a penalty for doing so.

> For additional information on spotting predatory lending practices, access the web site www.stopmortgagefraud.com developed by the Mortgage Bankers Association. The information is also available in Spanish and includes a phone number to report predatory lending.

How Do You Compare Products?

Try to contact at least 3 lenders to compare their products and fees. They should be willing to provide basic information about rates, points, and fees over the phone. We provide a checklist for you to use at the back of this guide.

In making your choice, consider:

- **Rates.** Will the lender allow you to lock in the rate and points for a period of time? *(**Rate lock-ins** are a good idea because interest rates fluctuate daily and could be far higher on the day your loan closes.)*

- **Points.**
    - **Discount points**, as we discussed previously, represent the upfront payment of interest to the lender. The lower the interest rate, the higher the discount points and vice versa. Each point is 1% of the loan amount.
    - **Origination points** are charged to offset the administrative cost of processing your loan. Be sure to find out if the lender also charges fees such as a document preparation fee or underwriting fee as well. Each point is 1% of the loan amount.
- **Term.** The longer the term, the lower the monthly payment, as we saw previously.
- **Down payment.** What is the minimum down payment required? Will private mortgage insurance also be required? If so, what is the cancellation policy on the insurance premium?

Further details are provided in Worksheet #4.

How Do You Actually Apply for a Mortgage?

In Worksheet #5, we provide a checklist of the documents your lender will typically ask to see. Do your homework and have your paperwork ready up front. It may seem like a lot but you are asking to borrow a significant amount of money and your lender wants to be sure to make a wise decision—for all concerned.

> Note that if you have a change of heart AFTER formally applying for a loan, your lender will typically not be willing to return your fee. In fact, your application documents should specify that all or a portion of the fee is non-refundable. So do your homework up front!

Lender Responsibilities

Within three business days of applying for your loan, your lender *(or the mortgage broker you are dealing with)* must give you:

- a Special Information Booklet, which contains consumer information regarding various real estate settlement services.
- a Good Faith Estimate (GFE) of settlement costs, which lists the charges you are likely to pay at settlement. This is only an estimate and the actual charges may differ. If a lender requires that you use a settlement agent, then the lender must disclose this requirement on the GFE.
- a Mortgage Servicing Disclosure Statement, which discloses whether the lender intends to service the loan *(that is, collect the monthly mortgage payments)* or transfer it to another lender. It also provides information about complaint resolution.

- a Truth in Lending Disclosure that includes the total amount you are financing, all of the costs you will be paying on an annualized basis *(the APR)*, the payment schedule and total of payments you will make, the prepayment policy *(if any)* and late payment policy.

Your lender should also give you a copy of *Buying Your Home: Settlement Costs* and *Helpful Information*, a HUD publication. Take the time to familiarize yourself with the contents prior to your own closing or settlement.

SUMMARY OF KEY POINTS

Lenders examine several key factors in determining how much you can afford to borrow:

1. Income and employment
2. Installment and revolving debt
3. Down payment
4. Cash available after closing
5. Type of mortgage product
6. Interest rate of the mortgage
7. Length or term of mortgage product
8. Credit

It is important for you to understand each factor and its impact on your mortgage amount and mortgage payment.

You should also review your credit history before approaching a lender. If there are errors on the report, you should address them with the credit agencies before these errors damage your profile and credit score. In fact, it's a good idea to review your credit history on an annual basis to make sure that errors don't creep in. In this era of easy identity theft, it's wise to keep a watchful eye on your personal credit data!

In deciding how large your mortgage should be, don't rely solely on the lender's guidance. Remember that they are not examining your total cash flow situation in making their calculations. But you need to do so. You can use the worksheets at the back of this guide or consult a housing counselor to develop a profile of how much money is coming into your home and how much is going out. Will you truly be able to absorb a mortgage payment and related housing expenses?

Finally, watch out for predatory lenders! There is always someone willing to lend you money—but the terms are not necessarily in your best interests!

One way to avoid predatory lenders is to do your homework and obtain basic information on rates, points, and fees from at least three lenders. Then, after analyzing the best "fit" for your own situation, apply for the loan.

As always, the decisions are yours to make. Never let anyone talk you into something that leaves you feeling uncomfortable. Remember that your future home is at stake!

Chapter III

Homeownership: *You Finally Get the Keys!*

Lender Evaluates Your Mortgage Loan Application

Once you have supplied all of the documentation your lender requests, your lender will begin to evaluate or underwrite your loan application. In traditional underwriting, your lender examines Four C's in deciding whether to make you the loan:

1. **Collateral:** The lender will require that you pay for an appraisal of the property to determine its market value compared with other similar properties in the neighborhood. An appraisal helps to prevent the lender from lending you more than the property is worth. Remember that in the worst case scenario, if the lender forecloses on your mortgage, they will sell the house in order to compensate for their losses.
2. **Capacity:** Will you be able to repay the mortgage *(based on your income and employment history)?* Will you also be able to handle your other major debts *(car loans, student loans, credit card debt, and so on)?*
3. **Credit:** As we discussed in Chapter II, your lender will look at your credit history to determine how you repay your debts. Do you consistently pay your bills on time? Or is there a history of late payments? Are there any serious negative items, such as judgments or bankruptcies?
4. **Capital:** Do you have enough cash on hand for the down payment and closing or settlement costs? Will there be any cash left over once the closing is completed?

Automated Underwriting Systems

More and more lenders employ automated underwriting systems in examining loan applications. Automated underwriting is a computer-based approach that enables your lender to process your loan application more quickly, efficiently, and objectively. They also enable your lender to evaluate your loan using more sophisticated measures of risk. In the final analysis, however, a human being—the underwriter—makes the decision, not the computer. He or she will decide to accept or reject the system's recommendation.

Responding to Additional Lender Questions

While underwriting your loan, your lender may request additional documentation or ask additional questions. Don't hesitate to respond to these requests to avoid delaying your loan approval. Also don't hesitate to contact your lender to check on the status of your application.

Letter from Your Lender

The final decision will be forwarded to you via a letter. One of three results are possible:

1. Your loan application may be approved with no conditions—that is, you will not be asked to obtain and bring any additional documentation to the closing.
2. Your loan application may be approved with conditions that must be met.
3. Your loan application may be declined.
   - If your loan application is declined, make sure you understand exactly why and see whether there are any immediate steps you can take to reverse the lender's decision:
     - For example, if errors on your credit report resulted in your loan application being declined and you can document those errors, you may be able to persuade the lender to reverse the decision.
     - If your application was declined for insufficient income, are you about to receive a raise? Would your employer be willing confirm your raise in writing to your lender?
     - If your application was declined for insufficient funds for the closing costs and other expenses, would a family member be willing to make a gift to cover these costs? Are there local down payment or closing cost assistance programs available in your community? *(A housing counselor might be able to help you locate such programs.)*
   - Some of the reasons for declining your application may involve longer term remedies, for example:
     - Your credit report correctly reflects a history of overdue and late payments. Consider working with a credit counselor to get a handle on your spending habits.
     - Your credit report also correctly reflects too much debt. Again, consider working with a credit counselor to develop a spending plan and pay down your debts, bit by bit.

Discrimination

If you suspect that your application was declined on the basis of race, religion, age, color, national origin, receipt of public assistance funds, sex, or marital status, report your complaint to HUD. The U.S. Department of Housing and Urban Development is charged with enforcing the Fair Housing Act. For a list of HUD regional offices, consult their web site at www.hud.gov.

Contingencies

Even while waiting to hear from your lender, you shouldn't be idle. During this period, you should do the following:

- You need to meet any contingencies spelled out in the sales contract for the home *(as described in the Addendum on Shopping for Your Home).*
  - Probably the most important item from your perspective is the **home inspection**. Be sure to accompany the inspector on the visit. You will learn an enormous amount about your new home. A thorough inspection will provide you with a clear, detailed sense of the condition of your house—as well as any problems the seller must address before closing. The inspection may uncover problems you are not willing to live with or that the seller is unwilling to correct. If so, you may decide against proceeding any further. Work closely with your real estate sales agent to make sure that you are not forfeiting your earnest money deposit by doing so.
  - Other inspections will be taking place during this period that don't require your presence—the **pest or termite inspection**, for example. The seller typically pays for the termite inspection. The final report should confirm no infestation and no damage or describe the damage and outline the costs for repair.
  - The lender may also require a **survey** of the property to confirm boundaries. You will probably be charged for this cost.

NOTE: The **appraisal** requested by the lender will also be conducted during this period. Remember that an appraisal is intended to compare the value of the property to other similar properties. Unlike an inspection, the appraisal will not examine the condition of the home in detail—for example, whether there are leaking pipes or a faulty electrical system. You have a right to get a copy of the appraisal from the lender.

Preparing for the Closing

Once your lender approval letter arrives, can you sit back and take it easy? Not quite yet.

- **Select Closing Agent or Settlement Attorney**

  Your real estate agent or lender may recommend someone to deal with this final step. You should feel free, however, to shop around for the most reliable and cost-effective agent in your area. In addition, you should consider hiring your own real estate attorney to help you review the contract or closing documents, such as the HUD-1 Settlement Statement *(described below).*

- **Obtain Title Insurance**

  "Title" refers to the legal ownership of your new home. A **title insurance** company *(typically selected by your lender or settlement company)* will research public records to ensure that the seller holds legal title to the property. The search will also confirm whether there any claims by others against your new home *(sometimes known as "liens" or "encumbrances").* Your lender will require that you pay for a title insurance policy that protects the lender against loss resulting from claims by others against your home. You should also purchase a policy for yourself. It is usually less expensive if you purchase both the lender's policy and your own at the same time.

  There are a number of **options for holding title**. In the sales contract, you may have already identified the type of ownership interest you prefer. Before closing, you may also discuss your options with your real estate attorney. These options include:

  - ***Sole ownership.*** The title to the property is held in your name only.
  - ***Tenancy by the entirety.*** This option is available only to married couples. Both owners must agree before the loan can be refinanced or the home sold. When one spouse dies, the property is automatically inherited by the surviving spouse.
  - ***Joint tenancy.*** The property is owned by two or more persons, in equal shares. When one owner dies, the surviving owner(s) automatically inherit that share rather than the heirs of the deceased.
  - ***Tenancy in common.*** The property is owned by two or more persons but the interests need not be equal. If one owner dies, that share goes to his or her heirs, rather than to the surviving owner(s).

- **Obtain Hazard Insurance**

  If you are purchasing a single family residence, your lender will require that you obtain hazard insurance for the replacement value of the property. This insurance will reimburse you for damage to your home from certain hazards, like a tornado or a fire. If your home is in a federally designated flood area, you will be required to purchase flood insurance. Certain hazards are not covered in a standard policy—like earthquake damage, for example—so be sure to review the terms of the policy carefully.

  Standard coverage normally insures personal belongings at 50 to 70% of the value of the dwelling. You may want to increase this coverage to a higher percentage if it will cost a significant amount to replace these items.

  If you are buying a condo or townhouse, get a copy of the umbrella insurance policy from the homeowner's association. It is wise to consider getting your own individual insurance policy to cover your personal possessions.

- **Review HUD-1 Settlement Statement**

  It's your legal right to get a copy of this document 24 hours before the closing. Don't be shy about asking for it!

  The HUD-1 Settlement Statement itemizes all of the expenses you and the seller are paying in relation to the transfer of the property. Be sure to keep a copy of your HUD-1 Settlement Statement; some of the closing costs may be tax deductible.

  You can find a blank copy of the form on the following pages.

A. **Settlement Statement**

U.S. Department of Housing and Urban Development

OMB Approval No. 2502-0265

B. Type of Loan

1. ☐ FHA 2. ☐ FmHA 3. ☐ Conv. Unins.
4. ☐ VA 5. ☐ Conv. Ins.

6. File Number: 7. Loan Number: 8. Mortgage Insurance Case Number:

C. Note: This form is furnished to give you a statement of actual settlement costs. Amounts paid to and by the settlement agent are shown. Items marked "(p.o.c.)" were paid outside the closing; they are shown here for informational purposes and are not included in the totals.

D. Name & Address of Borrower: E. Name & Address of Seller: F. Name & Address of Lender:

G. Property Location: H. Settlement Agent:

Place of Settlement: I. Settlement Date:

J. Summary of Borrower's Transaction		K. Summary of Seller's Transaction	
100. Gross Amount Due From Borrower		**400. Gross Amount Due To Seller**	
101. Contract sales price		401. Contract sales price	
102. Personal property		402. Personal property	
103. Settlement charges to borrower (line 1400)		403.	
104.		404.	
105.		405.	
Adjustments for items paid by seller in advance		**Adjustments for items paid by seller in advance**	
106. City/town taxes to		406. City/town taxes to	
107. County taxes to		407. County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412.	
120. Gross Amount Due From Borrower		**420. Gross Amount Due To Seller**	
200. Amounts Paid By Or In Behalf Of Borrower		**500. Reductions In Amount Due To Seller**	
201. Deposit or earnest money		501. Excess deposit (see instructions)	
202. Principal amount of new loan(s)		502. Settlement charges to seller (line 1400)	
203. Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204.		504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506.	
207.		507.	
208.		508.	
209.		509.	
Adjustments for items unpaid by seller		**Adjustments for items unpaid by seller**	
210. City/town taxes to		510. City/town taxes to	
211. County taxes to		511. County taxes to	
212. Assessments to		512. Assessments to	
213.		513.	
214.		514.	
215.		515.	
216.		516.	
217.		517.	
218.		518.	
219.		519.	
220. Total Paid By/For Borrower		**520. Total Reduction Amount Due Seller**	
300. Cash At Settlement From/To Borrower		**600. Cash At Settlement To/From Seller**	
301. Gross Amount due from borrower (line 120)		601. Gross amount due to seller (line 420)	
302. Less amounts paid by/for borrower (line 220)	( )	602. Less reductions in amt. due seller (line 520)	( )
303. Cash ☐ From ☐ To Borrower		**603. Cash ☐ To ☐ From Seller**	

Section 5 of the Real Estate Settlement Procedures Act (RESPA) requires the following: • HUD must develop a Special Information Booklet to help persons borrowing money to finance the purchase of residential real estate to better understand the nature and costs of real estate settlement services; • Each lender must provide the booklet to all applicants from whom it receives or for whom it prepares a written application to borrow money to finance the purchase of residential real estate; • Lenders must prepare and distribute with the Booklet a Good Faith Estimate of the settlement costs that the borrower is likely to incur in connection with the settlement. These disclosures are manadatory.

Section 4(a) of RESPA mandates that HUD develop and prescribe this standard form to be used at the time of loan settlement to provide full disclosure of all charges imposed upon the borrower and seller. These are third party disclosures that are designed to provide the borrower with pertinent information during the settlement process in order to be a better shopper.

The Public Reporting Burden for this collection of information is estimated to average one hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number.

The information requested does not lend itself to confidentiality.

Previous editions are obsolete Page 1 of 2 form **HUD-1** (3/86) ref Handbook 4305.2

L. Settlement Charges		Paid From Borrowers Funds at Settlement	Paid From Seller's Funds at Settlement
700. Total Sales/Broker's Commission based on price $ @ % =			
Division of Commission (line 700) as follows:			
701. $	to		
702. $	to		
703. Commission paid at Settlement			
704.			
800. Items Payable In Connection With Loan			
801. Loan Origination Fee	%		
802. Loan Discount	%		
803. Appraisal Fee	to		
804. Credit Report	to		
805. Lender's Inspection Fee			
806. Mortgage Insurance Application Fee to			
807. Assumption Fee			
808.			
809.			
810.			
811.			
900. Items Required By Lender To Be Paid In Advance			
901. Interest from to @$	/day		
902. Mortgage Insurance Premium for	months to		
903. Hazard Insurance Premium for	years to		
904.	years to		
905.			
1000. Reserves Deposited With Lender			
1001. Hazard insurance months@$	per month		
1002. Mortgage insurance months@$	per month		
1003. City property taxes months@$	per month		
1004. County property taxes months@$	per month		
1005. Annual assessments months@$	per month		
1006. months@$	per month		
1007. months@$	per month		
1008. months@$	per month		
1100. Title Charges			
1101. Settlement or closing fee	to		
1102. Abstract or title search	to		
1103. Title examination	to		
1104. Title insurance binder	to		
1105. Document preparation	to		
1106. Notary fees	to		
1107. Attorney's fees	to		
(includes above items numbers:	)		
1108. Title insurance	to		
(includes above items numbers:	)		
1109. Lender's coverage	$		
1110. Owner's coverage	$		
1111.			
1112.			
1113.			
1200. Government Recording and Transfer Charges			
1201. Recording fees: Deed $; Mortgage $	; Releases $		
1202. City/county tax/stamps: Deed $; Mortgage $			
1203. State tax/stamps: Deed $; Mortgage $			
1204.			
1205.			
1300. Additional Settlement Charges			
1301. Survey to			
1302. Pest inspection to			
1303.			
1304.			
1305.			
1400. Total Settlement Charges (enter on lines 103, Section J and 502, Section K)			

Previous editions are obsolete Page 2 of 2 form **HUD-1** (3/86) ref Handbook 4305.2

As you can see, page one of the Statement summarizes the expenses paid by the borrower *(in the left-hand column)* and by the seller *(in the right-hand column)*. Page two itemizes these expenses.

Major categories include:

- **Fees payable to the lender** in connection with the loan are shown in lines 800 to 807. The lender will typically charge a loan origination fee to offset the administrative costs of processing and underwriting your loan. In addition, there may be loan discount points—the upfront interest payments we discussed earlier. And the lender will collect a fee for the appraisal and credit report.
- Other expenses are known as **prepays** and are listed in **lines 900 to 905**. Lenders typically require you to pay interest from the date your loan closes to the first monthly payment. For example, if your loan closes on March 15, your first mortgage payment will be due on May 1. At closing, you will pay interest to cover the period from March 15 to April 1. Then your May 1 payment will include interest for April 1 through May 1—known as interest paid "in arrears."

  The lender may also collect one full year's premium payments to cover your mortgage insurance and hazard insurance.
- As we discussed earlier, lenders typically collect 1/12 of the annual payments due on your property taxes plus hazard and mortgage insurance policies and then make the payment on your behalf. To set up these **escrow accounts**, you may be asked to prepay these payments, as detailed in **lines 1000 to 1008**.
- Charges related to the **title search and title insurance** are itemized in **lines 1100 to 1113**. Remember that it is wise to obtain title insurance for yourself *(Owner's coverage—line 1110)*.
- Some of the documents you sign at closing will be **recorded in the local county registry or town clerk's office**. The charges for this service are outlined in **lines 1200 to 1205**.
- Finally, any additional settlement charges are noted in **lines 1300 to 1305**.

> An excellent line by line description of the HUD-1 Settlement Statement can be found in the HUD publication—Buying Your Home: Settlement Costs and Helpful Information. Your lender should give you a copy of this brochure when you apply for your loan. To print out additional copies, access HUD's web site at www.hud.gov.

If you agree with the costs as presented, you will need to get a cashier's check for the amount of money you owe—shown on line 303.

Schedule the Final Walk-Through

A day or so before the closing is scheduled, you should walk through the property to make sure that everything the seller agreed to leave behind is there and that everything is in proper working order.

Get Ready to Move

- Also during this period, you will be packing your belongings. If you plan to hire professional movers, get at least three cost estimates and confirm references.
- Don't forget to contact the utilities to cut off service at your current residence and begin service at your new home on the appropriate day.
- Pick up change of address forms at the post office to ensure you don't miss any magazine or other regular deliveries.
- You may have to purchase appliances, such as a refrigerator or washer/dryer, if your new home will not be equipped with these necessities.

> **NOTE:** Now is not the time to rush out and buy a houseful of new furniture or a new car! The old sofa and dining room set will work just fine for a few months while you settle in and confirm that you can handle all the new expenses of owning your home.

The Big Day Finally Arrives!

In some areas of the country, closings occur in an attorney's office; in other places, they may occur in the office of the title insurer or escrow agent.

- **What to Bring**
  - Cashier's check for the amount you owe *(noted in line 303 of the HUD-1 Settlement Statement)*
  - Photo ID – like your driver's license
  - Copy of hazard insurance policy
  - Anything else required by the lender in the approval letter

- **What to Expect**
  - You will sign what appear to be hundreds of forms. The major documents include:
  - **Note—**your promise to repay the loan according to the terms specified in the Note. The Note details where the mortgage payment should be sent and by what date, for example.
  - **Mortgage or Deed or Trust—**recorded evidence of your promise to repay the loan; if the loan terms not met, the lender may take over the property.
  - **Affidavit confirming your identity**

- **HUD-1 Settlement Statement** *(described above)*
- **Truth-in-Lending Statement**—Within three days of applying for your mortgage loan, your lender gave you a Truth-in-Lending statement showing the APR *(annual percentage rate)* for your loan plus a list of loan fees and expenses. At closing, you will receive an updated Truth-in-Lending statement if the final APR differs significantly from the original disclosure. *(Remember that the APR reflects the cost of your mortgage as a yearly rate and is provided to allow easier loan to loan comparisons.)*

Take your time – be sure you understand each document BEFORE you sign it. If you hired a real estate attorney, he or she should attend the closing and review each document before you sign it. You should receive from the seller not only the keys to the property but the deed, properly signed and notarized.

It's finally over! You are now a homeowner!

SUMMARY OF KEY POINTS

Once you have formally applied for your mortgage, you are in a "wait and see" mode while your lender underwrites your loan. This waiting period can be nerve-wracking and you may have second thoughts about taking such a major step at this time in your life. It's only natural to feel some anxiety—in fact, it's a healthy indication that you recognize the challenges you face!

If your lender asks for additional information, be as prompt as possible in supplying it to avoid delays. If you are hearing nothing at all, feel free to contact your loan officer to find out what's up.

If your lender does not approve your application, work with your loan officer to understand exactly what can be done in the short and long term.

If you are approved for your loan with conditions, begin meeting them immediately, again to avoid delays.

During the pre-closing period, you will be busy with the home inspection, obtaining a hazard insurance policy, and reviewing the HUD-1 Settlement Statement, among other items. You may decide to hire a real estate attorney to accompany you to the closing and help you review the documents you will be signing.

Do NOT take on any additional debt during this period—like buying a houseful of new furniture!

On the big day, you will be making a legal promise to repay your mortgage at specified rates and times. Once you've signed reams and reams of paper, you will receive the deed to your new home and the keys! You are now officially a homeowner!

Chapter IV

Homeownership:
In The Long Run

Moving In

- **Meet your neighbors!** They can be a great source of information about your new community and neighborhood. Knowing your neighbors can also help increase your sense of security in new surroundings. It's always a good idea, for example, to let your neighbors know if you'll be away for a few days.
    - If you are moving into a condo or townhouse, seriously consider participating in homeowner association board meetings. Their decisions will influence critical matters, like the amount of your monthly fee and the maintenance/upkeep of the property.

- **Some safety/security recommendations**
    - Change all the door locks. You have no way of knowing how many individuals have copies of the keys to the current locks.
    - Find out the location of the nearest hospital, police precinct, fire station and veterinary office, if you own pets. Post emergency numbers near the phone for easy access. *(Confirm whether "911" serves as an all-purpose emergency number in your community.)*
    - You should buy two fire extinguishers and install one near the kitchen and one near the main living area. For large houses, keep additional extinguishers in the garage, the basement, and on each floor.
    - Conduct a fire drill with your family to make sure that everyone knows the quickest route outside. Decide where your family will gather outside to wait for the fire department to arrive. If you have an agreed-up meeting spot already decided, it will be easier to determine if all family members have reached safety.
    - Contact your local fire department to see whether they provide fire prevention inspection tours of homes. In some communities, a fire inspector will visit your home to determine if any fire hazards exist.
    - Install a smoke detector outside each bedroom and near the living room. Check them as soon as you move in to guarantee that they are in working order. Then be sure to check them twice a year *(for example, when you adjust your clocks in the spring and fall)* to ensure that they remain in working order.
    - Install a carbon monoxide detector near the sleeping area and the heating source. Carbon monoxide (CO) is colorless, odorless, and deadly. In today's more energy-efficient, airtight homes, carbon monoxide may be trapped inside and remain undetected.
    - Store your valuables *(including your closing documents)* in a safe place. Consider buying a fireproof box or renting a safe deposit box in your bank.

- **Insurance coverage**
  - *Hazard or homeowner's insurance*

    Your **hazard insurance policy** may include an inflation rider which automatically increases the coverage as the value of your property increases. If not, check the amount of the replacement value each time you renew your insurance to ensure that it reflects the current value of your home. Otherwise, if you need to make a claim, you may not be reimbursed for the full amount of the damage.

    As discussed above, also consider increasing the coverage to a higher percentage to cover the replacement value of your personal belongings. In fact, you may decide to purchase additional coverage for special items such as your computer equipment or a valuable coin or stamp collection.

  - *Mortgage life insurance*

    You may already have been approached by your lender or another financial organization about mortgage life insurance. This insurance pays off the balance of the mortgage should the policyholder die or, in some cases, become disabled. Before you purchase this coverage, confirm that your existing life insurance policy does not already provide for this situation.

- **Home warranty**

  You may have purchased a home with a home warranty in place. If so, confirm the details of what the warranty covers and when it expires. Generally, a warranty covers the breakdown of major appliances as well as plumbing, electrical, heating, and air-conditioning systems.

  If you are considering buying a home warranty, be sure you clearly understand precisely what is covered. Also confirm that the organization issuing the warranty is legitimate and will still be around when you file a claim. This industry is not regulated, so it pays to do some careful research upfront.

Maintaining Your Property

As a tenant, you may never have had to bother with mowing the lawn, or raking leaves, or cleaning gutters. Unless you have bought a condo or townhouse, you are now facing these new responsibilities. We have provided a checklist at the back of this guide that outlines some of the basic items to keep in mind. If you are conscientious about general upkeep, you will prevent major *(and expensive)* problems from occurring and maintain the value of your property.

You should also seriously consider setting up an emergency reserve account to cover unexpected household needs. One rule of thumb is to have 1% of the purchase price of the home in such an account. In the early days of homeownership, you may be too pinched to contribute to this account, but don't forget it in the days to come.

Repairs

The wonderful day will arrive when something breaks down or springs a leak or simply refuses to turn on. To prepare for that inevitable day, consider taking home repair courses now. Sources of such information include:

- Your local community college or utility or Cooperative Extension Service may provide home repair classes.
- Major hardware stores post a schedule of basic how-to-do-it courses year-round.
- Your public library and local bookstore stock home maintenance manuals.
- Local nonprofit housing agencies may also provide how-to classes.
- You can access dozens of web sites on the Internet devoted to home maintenance.

At some point, you will encounter a repair that calls for expert assistance. Ask your neighbors, co-workers, or your real estate agent for recommendations for reliable plumbers, heating contractors, etc. Make sure you know upfront how much the repair may cost. And don't let anyone into your home without proper identification!

A Popular Scam

Watch you for anyone who comes to your door, saying they just happened to be in the neighborhood repairing a roof *(or siding or whatever)* and noticed that your roof *(or siding or whatever)* needs attention. Thank them politely for their interest and close the door. Do NOT let them into your home and do NOT hire them!

Home Improvements

The day may also arrive when you decide to update your kitchen or add a bathroom. If you are confident of your own expertise in such matters, you may choose to face the challenge yourself. The rest of us will hire a contractor. Here are some pointers:

- Interview several contractors. Again, ask your neighbors, friends, family members, and co-workers for recommendations. Find out what specific kinds of work the contractor does and the amount charged.
- Ask for and check references. Does your county or city license home improvement contractors? If so, get the list. Also contact the local Better Business Bureau for any outstanding complaints.
- Get an estimate from at least three contractors. Be sure that you give each of them the same requirements for the job to ensure consistency. The more definite your specifications, the more realistic the estimates.
- The contractor's bid should include a work write-up and specifications that describe all of the work to be done, the type, brand, and/or grade of material they will be using, and how much it will cost.
- Be sure that your contract specifies exactly what work is to be done and when payments are due. There should be both start and completion dates. Always hold back part of the payment until the job is completed to your satisfaction.
- Research the following with your contractor:
  - Will the job require building permits? If so, who is responsible for obtaining them?
  - Will the work need to be inspected?
  - Is the contractor insured and bonded? Ask for copies of the contractor's liability insurance and worker's compensation coverage and, if required in your area, licenses or certifications.

To pay for major repairs or remodeling projects, consult at least three lenders regarding available mortgage options. *(We discuss some of these options in Chapter V under Taking Advantage of Your Equity.)*

Energy Efficiency

You can take some immediate steps to increase the energy efficiency of your home and decrease your costs of homeownership. Every time you feel a cold draft in the winter, you are throwing money out the window. But how do you know where to begin? Consult the experts:

- See whether your local utility conducts **home energy audits**. This audit will tell you where energy is used and wasted in your home. With this information, you can decide what steps to take and their priority.
- Or, contact your state energy office to have a **Home Energy Rating Systems (HERS) survey** done. The HERS audit examines the energy performance of the heating, cooling, and hot water use of your home. The higher your HERS rating is, the better. Again, you can use the results of the study to decide which energy-saving steps to take.

Some Energy-Saving Opportunities

- **Water usage**
  - Repair leaky faucets—particularly hot water faucets—quickly. They can waste gallons of water in a surprisingly short period.
  - Install low-flow showerheads and shut-off valves. These are inexpensive to buy and can cut your hot water use by up to 25%.

> A family of four, each taking a 5-minute shower a day under inefficient showerheads, can use 700 gallons of water in a week. That is a 3-year supply of drinking water for one person.

- **Water heater**
  - Reduce the temperature on your water heater to 120 degrees Fahrenheit. *(However, first check to see that your automatic dish washer has a temperature boosting component that will bring the temperature back up to 140 degrees when washing dishes.)*

> The U.S. Department of Energy estimates that each 10-degree Fahrenheit reduction in the hot water heater setting will save you up to 13% off your water heating bill.

- **Insulation**

  More heat per square foot travels through your ceiling than any other part of your house. That's why it's important to make sure it is adequately insulated.

  Measure your attic insulation with a ruler and multiply the number of inches by the R-value of that particular insulation to get an insulation rating on your home. Also make sure that there are no gaps in the insulation that would allow heat to escape.

  Do you have two different types of insulation? If so, then measure them separately and find out the R-value for each one. Then add them together. Take a sample to an insulation company or hardware store if you're unsure about what type of insulation you have. *(Wear gloves and a good particle filter over your nose and mouth when measuring or taking samples.)*

> The R-value measures the resistance to heat flowing through the insulation over time. Insulation with greater resistance *(higher R-value)* to heat flow means that heat enters or leaves your home more slowly. Slower heat flow means lower heating and cooling costs. The U. S. Department of Energy has mapped out recommended R-values for the entire country. You can find out the recommendation for your area on their web site at www.doe.gov.

- **Heating, Ventilation, and Air-Conditioning (HVAC) System**
  - Have your HVAC system checked once a year.
  - Change or clean the filters at least every other month.
  - Install and use a programmable thermostat that will automatically change the temperature whether you're at home or not.

- **Appliances**
  - When it's time to buy a new appliance, look for the Energy Star® label that indicates the appliance has met the highest energy standards.
  - Check with your local utility company to see if they offer rebates or incentives for the purchase of energy-efficient appliances.
  - Some states also offer sales tax incentives for the purchase of Energy Star appliances.

The U.S. Environmental Protection Agency (EPA) and the U.S. Department of Energy (DOE) promote the use of energy-efficient equipment by awarding the Energy Star label to products that exceed minimum national efficiency standards. These high-performance products reduce energy costs each month they are in use. For a list of Energy Star appliances and local stores where you can buy them, access www.energystar.gov.

There is a more detailed checklist of energy-efficient steps to take plus a list of additional resources at the back of this guide.

SUMMARY OF KEY POINTS

Immediately after moving in, take steps to make your new home as safe and secure as possible. Also consider taking home repair courses, if you are not already handy around the house. The happy day will certainly arrive when such skills will come in handy.

If you do decide to hire a contractor for major improvements, be sure that you have researched their background and capabilities. There are too many horror stories about contractors who don't show up for weeks at a time or whose work product is substandard.

Also look into energy-efficient steps. These can range from big-ticket items like purchasing energy-efficient appliances to small items like reducing the temperature on your water heater. Your local utility and Cooperative Extension Service should provide a substantial information and resources on this topic.

Chapter V

Homeownership: *The Financial Side*

Your Mortgage Payment

Be absolutely sure that you understand all the terms of your loan:

- **Confirm the following—**
  - Amount you pay each month
  - Where you send the payment
  - When you send the payment

    Some lenders provide **payment books** and rely on you to mail in the payment each month with the appropriate coupon from the payment book. Other lenders send **monthly billing statements**. Still others will arrange to **automatically deduct** your payment from your checking or savings account. *(Automatic deductions are a simple way to avoid forgetting to write a check. Of course, you have to be very careful to have the correct amount of money available in the account on the designated drafting day.)* And some lenders allow you to make **online payments** using the Internet.

    Whatever method you choose, remember that the payment is typically due on the first day of each month—check your Note to confirm the due date. You will be charged a late fee if your payment is not received after the 15th day of the month. Remember—the critical date is NOT the date on which you put the check in the mail but the date on which that check is RECEIVED by the lender.

- **ARM loans**

  If you have an adjustable-rate mortgage, your mortgage payments may change as the interest rate changes. Review your Note to make sure you understand when these adjustments will occur.

  Also, carefully review the adjusted payment schedule when you receive it. Lenders can make mistakes. If you are at all unsure, call your lender!

- **Other monthly housing-related fees**

  If you live in a condo, townhouse or Co-op, you may also be paying a monthly homeowner or condominium association fee. Remember that if this fee is not paid as agreed, you could face foreclosure proceedings initiated by the homeowners association.

- **Interest-Only Loans**

Interest-only loans are not a type of mortgage. Interest-only is an option that can be attached to any type of mortgage. In contrast to traditional mortgages, where you make payments of principal and interest during the entire term of the loan, Interest-Only loans offer an initial period during which you only pay the interest payments. After the interest only period, the loan converts to payments of both principal and interest. Interest-Only loans may have either a fixed or adjustable interest rate. In either case, payments of interest made during the interest-only period will not reduce the principal balance remaining on your loan. Payments due after the interest-only period will be higher for the remaining term of the loan than those made during the interest-only period. For most "Interest-Only" loans, the principal and interest payments are calculated so that the loan is paid in full on the date of maturity.

Example: Traditional 30-year Fixed Rate, Fully Amortized Mortgage vs.
30-Year Fixed Rate Mortgage with an Interest-Only Feature.

The examples below are based on a $100,000, 30-year loan with a 5.5% interest rate.

	30-Year Fixed Rate Mortgage, Fully Amortized	30-Year Fixed Rate Mortgage with 10-Year Interest-Only Period
Original Principal Balance	$100,000	$100,000
Monthly Payment Years 1-10	$567.79 (PRINCIPAL & INTEREST)	$458.30 (INTEREST ONLY)
Principal Balance at the end of Year 10	$82,541	$100,000
Monthly Payment Years 11-20	$567.79 (PRINCIPAL & INTEREST)	$687.89 (PRINCIPAL & INTEREST)
Principal Balance at the end of Year 30	$0.00	$0.00

This example assumes that no prepayments of principal have been made during the interest-only period. With many interest only loans, you have the right, but not the obligation, to make payments of principal during the interest only period. A payment of principal during the interest-only period will reduce subsequent interest-only payments.

- **Prepaying Your Mortgage**

  Unless your mortgage contains a prepayment penalty clause *(that is, you are not allowed to pay down the mortgage for a specific period of time without paying a penalty)*, you may consider making additional principal payments. In the early years of your mortgage, of course, such prepayments may be difficult, as you adjust your finances to the new reality of homeownership. But later on, consider adding even $10 or $25 to each mortgage payment to increase the speed at which you pay off the loan.

> You will probably receive invitations from your lender to switch your loan to a biweekly status. In other words, instead of paying once each month, you are making half of the regular payment every other week. This arrangement results in 13 monthly payments being made over the course of a year. The catch is that the lender will require an upfront fee to make the switch in their system. You can achieve the same result by simply making an additional principal payment on your own.

- **Transfer of Servicing**

  The process of collecting mortgage payments, maintaining escrow accounts for taxes and insurance, and paying taxes and insurance premiums is known as servicing. In many instances, the lender that approved your loan will not service it. This transfer of responsibilities does not affect the terms of the mortgage itself, however. The loan amount, interest rate, due date, and so on remain unchanged.

  If your loan has been transferred to another servicer, you should receive two written notices—one from the original lender and one from the new servicer. Do NOT forward your mortgage payment to a new entity unless you have heard from your lender! If you have any doubt, contact your lender to confirm the new arrangements.

  After a loan is transferred, there is a 60-day grace period during which you cannot be charged a late fee if you mistakenly send your payment to the old lender or if your payment does not arrive at the new servicer by the due date. Also, any error during this 60-day grace period cannot be reported as a late payment to the credit agencies. However, once the grace period has ended, you must comply with the terms of the loan repayment to the newly-designated servicer.

- **Adjustments to your Taxes and Insurance Payments**

  Even if you have a fixed rate mortgage and the interest rate on your loan never changes, your mortgage payment may change because of the T *(taxes)* and I *(insurance)* components. For example, the value of your property may increase, resulting in a higher property tax assessment. By the same token, an increase in your property value might trigger an increase in the amount of your insurance coverage and the premium you pay.

- **Annual Escrow Statements**

  Even if there are no changes whatsoever in your mortgage payment, you will receive an annual escrow statement from your servicer. The statement will detail the amount of money collected for taxes and insurance and when these funds were paid out.

  Study the statement carefully—again, you may uncover an error. For example, let's say that the servicer has been collecting too little for your property taxes over the past 12 months. They receive your property tax bill, discover the error, and tell you to immediately forward the difference. Not a situation you want to face!

- **Mortgage Insurance Premiums**

  As we discussed above, if you have a conventional loan (*a loan not insured or guaranteed by the government),* you should be able to cancel your private mortgage insurance at some point. Depending on the terms of your mortgage product, if you have a good payment record and have paid off 20% of the original loan amount, you may request that your private mortgage insurance be canceled. For FHA loans and some conventional loans, the cancellation occurs automatically when you have paid off 22% of the original loan amount. Confirm with your servicer when or if such cancellation is possible.

- **Preparing Your Federal Tax Submission**

  In the past, you may not have filled out the more detailed federal tax form and itemized your deductions. Now that you are a homeowner, it's time to do so! You should be able to deduct your mortgage interest and property taxes plus some of your closing costs. If you have questions, consult a tax professional or get a copy of the IRS brochure listed in the Resources section of this guide. You might also consider adjusting the amount withheld by your employer for federal taxes to offset your new deductions. In other words, it may not be necessary to withhold as much from each paycheck now that you are a homeowner. Again, if you have questions, consult a professional financial advisor.

Financial Emergency

What if a crisis occurs? Let's say that the major wage earner in your household is laid off or disabled. Or you may face a mountain of hospital bills for a sick child undergoing extensive medical treatments. Don't just stop making your mortgage payment and hope that no one notices. This payment should be your most important financial obligation. It ensures that you and your family have a roof over your heads.

If you start having problems, look for help right away.

- Could you borrow from a relative?
- Could you borrow from an insurance policy or 401(K) plan?
- Can you get a second job or overtime pay?
- Can you cut back on other, less essential expenses?

Avoid the temptation of taking a cash advance against your credit cards *(the interest rates charged are typically very high)* or a short-term loan from a loan company. You may only dig yourself in deeper.

You should also consider contacting a credit counselor at your local Consumer Credit Counseling Services (CCCS) office to discuss alternatives. They may be able to help renegotiate the terms of your credit card debt, for example, if that debt is making it difficult for you to repay your mortgage.

Contact Your Servicer

Don't miss even a single payment—it will be that much harder to catch up. Even if you are working with a credit counselor, don't delay making the difficult phone call to your servicer. Be prepared to discuss the following:

- Explain why you are unable to make your mortgage payment
- Get the name of the person you talk with and write a follow-up letter. Include in the letter:
  - Your name
  - The mortgage loan number
  - Property address
  - Your daytime and evening telephone numbers
  - Brief explanation of your financial situation

Your servicer should be willing to work with you. And, of course, it helps if you have been making your payments on time up to this point! The servicer wants to avoid foreclosure if possible. It is much preferable for you to remain in your home and to get back on your feet. Foreclosures cost money and the servicer may not be reimbursed for the full costs they incur.

Alternatives to Foreclosure

The type of alternatives your servicer will discuss with you depends on your mortgage. For example, if you have an FHA or VA loan, the foreclosure alternatives are determined by the U.S. Department of Housing and Urban Development and the Veterans Administration, respectively. If you have a conventional loan that was purchased by Fannie Mae or Freddie Mac *(the two largest mortgage investors),* your options will be guided by their directives to lenders.

Some of the options your servicer may present, depending on your financial circumstance, include:

- **Forebearance:** Under the terms of this formal, written agreement, your mortgage payments would be reduced or suspended for a specific period of time. At the end of the period, you would be required to resume your regular monthly payments plus an additional amount.
- **Loan modification:** With a loan modification, one or more of the terms of the mortgage are changed to help you bring a defaulted loan current. This option is generally used for borrowers whose financial problems are expected to be long-term.

If it appears that you simply will not be able to recover from the emergency, you can still avoid the stigma of a foreclosure. For example:

- **Assumption:** You or the lender may find a new buyer who is willing to assume your mortgage. However, not all mortgages are assumable—a fact your servicer will be able to confirm.
- **Preforeclosure sale:** In this situation, the servicer agrees to accept the proceeds from the sale of your home, even though the amount is less than you owe.
- **Deed-in-lieu of foreclosure:** You can voluntarily give the deed to your property to your servicer and then move out. This option is usually considered by a servicer only after all other alternatives have been explored.

NOTE: There are two messages to remember in case a financial emergency arises:

1. Contact your servicer as soon as you realize you will not be able to make your mortgage payment.
2. There are alternatives to foreclosure and your servicer is as anxious to explore them as you are.

The B Word—BUDGET

For many of us, the word 'budget' is like the word 'diet'—we know it's good for us but we just can't bring ourselves to get started. Maybe we should use a different word altogether. Instead of saying 'budget,' let's talk about Making Our Money Work.

To Make Our Money Work, we need to walk through a few introductory steps.

1. **First of all, how much money comes in the door each month?** In Worksheet #8 at the back of this guide, add up all of your take-home pay—that is, your income after taxes and other deductions are taken out by your employer.
   - If you are paid weekly, multiply your take-home pay by 52 and divide by 12 to get your monthly income figure.
   - If you are paid every other week, multiply your take-home pay by 26 and divide by 12 to get the monthly figure.

   Do NOT include bonuses, gifts, occasional overtime, or any other infrequent source of income. For now, we are interested in what flows in on a regular basis each month.

2. **What are your regular monthly expenses?** List these in Worksheet #9. For expenses that occur only once or twice a year, break them down to a monthly number. For example, if you pay $400 twice a year for car insurance, that comes to $800 per year. Divide the annual $800 payments by 12 to arrive at the monthly expense of $66.66.
   - For your **housing expense**, be sure to include your entire mortgage payment plus any homeowner association or condo fee.
   - Even if you have not yet moved into your new home, you can still get a sense of what your **utility costs** will be. Most utility companies will tell you the average monthly costs for a specific address. Don't forget to include all utilities—gas, electric, water and sewage, and trash collection.

   > See whether your local utility has a "budget" or "average payment" plan under which they estimate your annual bill and divide it into 12 monthly payments. Once a year, the utility will re-visit the calculation to see whether your actual usage was higher or lower and then adjust your monthly payment accordingly.

   - Add a monthly setaside for a **home maintenance allowance**—of around 1% of the purchase price of your home. For example, if you are paying $96,000 for your home, you should save 1% of $96,000 or $960. Divide the $960 by 12 months; you should plan on adding $80 per month to your home maintenance allowance.

- You should also establish an **emergency fund**. Financial advisors suggest saving 5% of your take-home pay. So if your monthly take-home pay is $3,000, you should place 5% or $150 in your emergency fund. And never, ever touch this fund until a real emergency arrives.
- **Credit cards—**a great convenience and, for many of us, a great curse. We discuss in Chapter II some steps to take to get your credit cards under control.

How Much Debt Is Too Much?

One way to get an answer to this question is to divide your total monthly debt payments *(excluding your housing expenses)* by your net take-home pay.

- If the ratio is less than 15%, you are OK.
- If the ratio is between 15% and 20%, you should look for ways to cut back on your debts.
- If the ratio is greater than 20%, you're in the danger zone of debt and should consider working with a credit counselor!

3. **How do your Total Monthly Expenses compare with your Total Take-Home Pay (Worksheet #9)?** If your expenses are more than your take-home pay, there's a problem. And it's wiser to address this problem head-on now, rather than wait for it to explode later on. Again, you don't want to risk losing your home and all of the money you have invested in it.

So now we get into the really tough section—

4. **Where can you cut back?**
   - Some expenses are **fixed**—the amount does not change every week or every month. Other expenses are **discretionary—**that is, you are in control of how much you spend in these areas. For example, you decide how many nights you eat out each week. Or how many first-run movies you see in a month. Or whether to subscribe to the deluxe cable package or basic service. Do the fixed vs. discretionary split in Worksheet #10.
   - Then decide which of the discretionary items you cannot live without—**needs**—and which are simply nice to have—**wants**. The needs vs. wants split is also found on Worksheet #10.
   - After all that list-making, here's the final pay-off—the "want" list is where you begin to make cuts. You know that these items are in your control and you've admitted that they are not absolutely necessary for your survival, so **prioritize their disappearance**.

In the long run, of course, completing lots of worksheets isn't the same as living within your means and Making Your Money Work for you. That takes daily reminders of what is important and must be had RIGHT NOW vs. what can be purchased next year *(or even not at all).*

It's a lifestyle choice. Some of us feel we absolutely must have the latest and biggest SUV with all possible bells and whistles attached—even if that means a monthly car payment of $575. Or that wide screen, high definition TV that costs $150 per month. Others are content with a used compact car with monthly payments of $185 and a 23" TV that was paid for in cash.

Just remember—you're in control. You are the decision maker. If you feel that you're in over your head, there are many sources of help. We list several resources in the back of this guide.

Taking Advantage of Your Equity

As we discussed earlier, as you pay down the amount you owe, you build up equity in your property. Your equity also increases if the value of your home increases. For example:

Current value of home	$135,000
Mortgage amount due	-85,000
Equity	$ 50,000

How can you tap into this equity without selling your home?

- **Second mortgage**

  You can take out a second mortgage on your property. It's known as a "second" mortgage because this lender will be second in line to be repaid in case of a foreclosure.

  You might consider a second mortgage if you want to make a major improvement, such as adding a bathroom or re-doing your kitchen. The interest rate you pay will typically be higher than the rate on your first mortgage.

- **Home equity loan/line of credit**

  You can also take out a loan secured by your home, known as a home equity loan. In fact, you may receive a blizzard of invitations to do just that as soon as you move in! You can use the home equity loan for most any reason—to consolidate debt, pay for college tuition, remodel your kitchen or add a bathroom, and so on.

  Because the debt is secured by the home, all or part of the interest is deductible on your taxes. Interest is not deductible on that amount of the loan that exceeds the value of the home, however.

You can either borrow a fixed amount and repay it in equal installments or take down a line of credit. Be sure that you understand the difference and the rates/fees you'll be paying.

NOTE: Remember that if you take out any kind of debt backed by the equity in your home, you risk losing your home if you cannot repay that debt! So resist the hard sales pitches unless you are confident of your ability to handle the additional payments! For example, those ads that talk about being "debt-free" by repaying your credit cards debt via a home equity loan? You've just transferred your debt from one place to another—and tied it to your home!

Refinancing

As mortgage rates decrease, they may reach a level below what you are currently paying. If so, you may consider refinancing your current mortgage with a new, lower rate loan. However, be sure to do your homework and compare fees charged by lenders. You will probably encounter most of the closing expenses you did the first time around, for example. So it's wise to do the math and compare the total amount you will pay to refinance with the amount you will save in a lower monthly payment. *(Double-check your mortgage documents to ensure that you do not have a prepayment penalty as well.)*

Prepaying

At some point, you may discover that it's easier to manage your mortgage payment as your household income increases. In fact, you may decide to make additional payments occasionally in order to pay off the mortgage more quickly. If you can make even one extra payment per year, you will cut years off your mortgage. Even an occasional $25 per month will have a dramatic impact. *(Double-check your mortgage documents to ensure that you do not have a prepayment penalty, however.)*

Reverse Mortgages

Older homeowners have a special way to access the equity in their homes. Reverse mortgages work like an 'ordinary' mortgage but in reverse. The senior homeowner *(aged 62 or higher)* will receive funds according to a schedule they select—regular installments, a lump sum payment, or a line of credit.

The amount owed is generally not repaid until after the senior leaves or sells the home or the home passes into an estate. Even then, neither the senior nor the senior's estate can ever be required to pay more than the value of the home.

SUMMARY OF KEY POINTS

Clearly, the financial side of owning your home is of critical importance. It's your responsibility to understand the terms of your mortgage—where your payments should be sent and when.

If you do encounter a financial crisis, do not hesitate to contact your mortgage servicer. Missing even one payment will make it that much harder to catch up. And your servicer is as interested in keeping you in the home as you are. There are a number of options available, depending on the severity of your situation.

To help you make it through a financial crisis, drawing up a spending/savings plan is a wise step. You can use the Worksheets at the back of this guide to analyze how much money is coming into your household each month and how much is being spent. You can further break down your expenses into fixed and discretionary items—with the latter serving as your starting point for cutting back.

If you would like to consult professionals who can help you work out a livable spending and savings plan, turn to the Resources section of this guide for suggestions.

Addendum

Shopping for Your Home

Before you begin house-hunting, take a few moments to decide clearly what you need as well as what you want in a new home. In fact, start by checking below what you absolutely must have *(your NEEDS)* vs. what would be nice to have *(your WANTS)*.

	NEEDS	WANTS
Type of Home:		
SFD, condo, townhouse		
Construction:		
Lot Size:		
Rooms — # and Type:		
Bedrooms		
Bathrooms		
Eat-in Kitchen		
Dining Room		
Living Room		
Family Room		
Office		
Basement		
Fireplace		
Garage		
Porch		
Deck		
Wiring for Computer Access		
Other		
Other		
Heater: type of fuel:		
Water heater: type of fuel/size		
Neighborhood:		
Transportation Requirements:		
Proximity to:		
Work		
School		
Place of worship		
Shopping		
Recreation		
Mass Transit		

Even spending just a few moments now on these decisions can save you an enormous amount of time later on AND will help guarantee that you end up with the home you really do need!

- Determine the type of home you are interested in. And don't forget that there are alternatives beyond the traditional single family detached house with a white picket fence. For example:
  - **Condo.** As a condo owner, you own your individual living unit and share ownership of the common space *(for example, elevators or recreational areas)*. You pay a homeowner association or condo fee monthly to pay for the upkeep of these common areas. If you are not interested in mowing the lawn or cleaning out gutters, you might consider a condo. Just be sure to check the overall 'health' of the entire physical structure and of the association's financial situation.
  - **Townhouse**. You own your individual townhouse living unit and share ownership of the common areas.
  - **Co-op**. Co-ops or cooperatives are typically found only in certain sections of the country *(for example, in New York City and Washington, D.C.)*. As a Co-op owner, you own a share in the corporation that owns the entire building. You do NOT own your own individual unit.
  - **Planned Unit Development (PUDs)**. Some subdivisions or neighborhoods include a common area that is owned by a homeowner's association and maintained for the use of PUD unit owners. Such developments may also allow the homeowner's association to dictate how unit owners maintain their individual properties. If this is the case, make sure that you are comfortable with someone else telling you what color your front door should be painted.
  - **Manufactured housing**. These units are factory-built or prefabricated dwellings. Depending on the location, you may own or rent the land on which the unit is placed. Make sure that the home meets all HUD and state building codes.

> **NOTE:** Be sure to think long term. Are you planning on starting a family within the next few years? Will an elderly relative who has difficulty with stairs be coming to live with you in the near future?

- Looking for leads. You can find out about existing homes for sale in a number of ways.
  - Newspapers—most newspapers highlight real estate ads on a particular day each week.
  - Word of mouth—do family members or co-workers know of any homes about to be placed on the market?
  - For sale signs in neighborhoods you're targeting—drive around neighborhoods that you are interested in.
  - Internet resources *(for example, www.realtor.com)*

NOTE that federal agencies *(such as HUD and the VA)* as well as major investors *(for example, Fannie Mae and Freddie Mac)* sell homes on which they have foreclosed. You can access these lists via HUD's web site as detailed in the Resources section of this guide. However, please be aware that these properties will typically be offered at whatever price the market will bear. So you won't necessarily be getting a bargain!

- Work with a real estate agent. It's not absolutely essential to work through a real estate agent but most of us do. The real estate agent will not only be able to guide your search *(via access to the Multiple Listing Service or MLS)* but can provide professional insights into the overall housing market as well as the community. The agent can also offer advice on mortgage lenders, closing agents, and title companies. Before you sign on with a real estate agent, however, you should understand how they are paid.
  - There are two broad categories of agents—those who represent the seller in the transaction and those who represent the buyer. When you visit an Open House, for example, that agent is representing the seller's interests and is paid a percentage of the sales price. So the seller's agent is motivated to sell the property for the highest reasonable price.
  - In contrast, the buyer's agent represents your interests. Typically, you will not be paying a direct fee for their services. The agents involved in the transaction will split the commission. However, confirm that this arrangement is in place before signing any agreement with a particular buyer's agent.

For a list of agents in your area, access:
- the National Association of REALTORS® web site at www.realtor.com
- the National Association of Exclusive Buyer's Agents web site at www.naeba.com
- the National Association of Hispanic Real Estate Professionals web site at www.realestateespanol.com.

Keep good records as you tour various homes. After awhile, it's easy to lose track of what you've seen. Some people even use a camera or camcorder to take pictures of the properties they visit. There are two versions of the Housing Evaluation Checklist below—use the one you find most helpful in your search:

Your Housing Evaluation Checklist—Version 1

Make copies of this page and use it to keep track of the properties you visit. Compare the items noted below with your list of "Needs" and "Wants."

Property Address: ______________________________

Type of Home:	Existing	New	
	Ranch	Split-Level	
	Traditional	Contemporary	
Construction:	Brick	Wood siding	
	Cement	Cedar shingles	
	Other		
Lot:	Size	Type	
Rooms: # and type:	Bedrooms	Bath	
	Dining Room	Eat-in Kitchen	
	Living Room	Family Room	
	Office	Basement	
	Other		
Heat:	Forced air	Radiator	Other
HVAC	Size	Age	
Fuel:	Gas	Oil	Other
Air-conditioning	Central	Window	None
Water heater:	Size	Type of Fuel	
Insulation: R-values in:	Attic	Walls	Basement
Extras:	Fireplace	Garage	
	Porch	Deck	
	Wiring for computer access throughout the house?		
Neighborhood:	Ideal	Acceptable	Poor
Transportation Requirements:			
Proximity to:			
School			
Place of worship			
Shopping			
Recreation			
Mass Transit			

Comments: ______________________________

____

____

Your Housing Evaluation Checklist—Version 2

Use this list, prepared with assistance from the National Association of REALTORS®, for rating properties as you visit them. Make copies of this checklist and take them with you on your house-hunting trips.

Property Address:			
THE MLS PRINTOUT BY THE REAL ESTATE SALES AGENT SHOULD PROVIDE THE FOLLOWING:			
The asking price?			
The annual property taxes?			
The average monthly utility costs?			
What is the seller's current mortgage balance and monthly payments?			
Is the seller willing to take back a second mortgage?			
Is the seller's current mortgage assumable? If so, what is the interest rate?			
NEIGHBORHOOD	**Ideal**	**Acceptable**	**Poor**
Are many houses for sale in the area? If so, why?			
Are there plans underway to change the zoning regulations? If so, how will that affect the neighborhood?			
Is it convenient to public transportation?			
To shopping?			
To recreational facilities?			
To schools?			
To places of worship?			
WHETHER THE HOUSE IS NEW OR OLD, BOTH THE QUALITY OF THE BUILDING MATERIALS AND THE CRAFTSMANSHIP, AS WELL AS THE CONDITION, ARE IMPORTANT CONSIDERATIONS.			
Type of home and construction			
How well insulated is the house?			
Are the windows energy efficient?			
Is the roof in good condition?			
Does the house appear to have been well maintained?			

Floor plan: good traffic flow from one room to another?	
Bedroom(s)	Number:______ On which floor(s)?______
Bathroom(s)	Number:______ *(full)* ______ *(half)* On which floor(s) ______
Dining room	
Kitchen *(space for eat-in table/chair **OR** not)?*	
Any built-in appliances?	
Family room	
Laundry room	
Basement	
Is the basement finished? Does it flood after every heavy rain?	
Attic space	
Storage	
Floors and covering	
Heat	
Fuel	Gas **OR** oil **OR** passive solar **OR** other
EXTRAS	
Fireplace *(gas OR wood-burning)*	
Garage: # of cars:	
Porch **OR** Deck **OR** Patio	
Pool	
Irrigation **OR** Sprinkler system	
Air-conditioning *(Central OR Room)*	
Security System	
REMARKS	

Keep a cool head. Don't fall in love with a property at first glance. If you fear that you've done so, bring along an unbiased and honest friend with you on a second visit. Also don't be pressured into making an offer on a property until you're sure you want it. If there is a seller's market *(that is, each home is receiving multiple offers from interested buyers),* it may be difficult to withstand this pressure. Just remember that you are making the largest financial decision of your life! *(How's that for pressure?)*

- **Making the Offer**
  - Get a list of **recent sales prices for comparable homes** *(CMA – Comparable Market Analysis)* from your real estate agent or from the Internet.
  - Get as much information as possible on **seller's situation**. For example, is he frantic to sell because of a job-related transfer to Italy?
  - **Condition of the home**—will you be able to move in without doing extensive repairs?
  - Factor in the **overall housing situation**. In a heated seller's market, you may have to offer more than the asking price. You won't feel that kind of pressure in a buyer's market.
  - And, of course, **how much you can afford**. Again, don't get in over your head!

  The offer will include more than just the price you're willing to pay. The sales contract will specify the legal description of the property, which items *(like window treatments)* will 'convey' with *(or be included in)* the sale, the amount of your earnest money deposit and down payment, and how you will finance the purchase. In addition, the contract will note dates for the closing and occupancy as well as the length of time the offer is valid. And, finally, the offer will include certain **contingencies—**some of which protect the seller and some of which protect the buyer. Many of these contingencies are standard and non-negotiable.

- Home inspection. One negotiable contingency that protects your interests is a home inspection. In a hot seller's market, you may be tempted to make an offer without requiring that the home satisfy a basic inspection—particularly if you are competing with other offers that are not requiring such an inspection. If you do so, you are taking the risk of purchasing a leaky roof or flooding basement or outdated electrical wiring. So be aware of the potentially expensive consequences you may face.

  The Resources section provides information on locating a qualified home inspector. Don't rely on Uncle Harry to come over and nose around. Hire someone who is specifically trained to inspect the property and provide a detailed assessment.

- **Negotiating the Offer**
  - Offer may be accepted—if so, hurrah!
  - Offer may be rejected—if so, make a counteroffer *(if you can afford to do so).*

- **Earnest money**
  - Your earnest money deposit indicates to the seller that you are serious about your offer. This money is considered part of your overall down payment.
  - If your offer is accepted, your check will be held in escrow by the real sales company. You will forfeit these funds if you do not meet the contingencies in the contract *(for example, if you are not approved for a mortgage by the date specified).*

Worksheets

WORKSHEET #1

Calculating Your Gross Monthly Income

Remember that your lender is interested in your gross monthly income—what you make before taxes and other payroll deductions. You should also include all other sources of regular income, if they are likely to continue for three years. Be sure to list the income of everyone who will be signing the Note.

	AVERAGE MONTHLY AMOUNT	
	YOURSELF	CO-BORROWER
Gross pay *(before taxes and other deductions)*	$	$
Gross pay *(before taxes and other deductions)* for a second job	$	$
Regular overtime	$	$
Bonuses/tips	$	$
Alimony, child support, or other maintenance income	$	$
Pension/Social Security benefits	$	$
Dividend/interest earnings	$	$
Business earnings	$	$
Veterans Administration benefits	$	$
Unemployment compensation	$	$
Public assistance	$	$
Other	$	$
Other	$	$
Total for each Co-Borrower	$	$
Grand Total = Gross Monthly Income	$	

WORKSHEET #2

Calculating Your Monthly Debt Payments

Remember that your lender wants to be sure that your income will be enough to cover your mortgage payments and other monthly debts—those debts that will not be paid off in the next ten months. Be sure to include the debts of anyone who is signing the Note.

	AVERAGE MONTHLY AMOUNT	
	YOURSELF	CO-BORROWER
Car loan	$	$
Installment loan payment *(e.g., loan for furniture or an appliance)*	$	$
Installment loan payment *(e.g., loan for furniture or an appliance)*	$	$
Credit card # 1 average monthly payment	$	$
Credit card # 2 average monthly payment	$	$
Credit card # 3 average monthly payment	$	$
Student loan	$	$
Medical/health care payment *(not an insurance premium automatically deducted from your paycheck)*	$	$
Alimony/child support payment	$	$
Other	$	$
Other	$	$
Total for Each Co-Borrower	$	$
Grand Total = Monthly Debt Payments	$	

WORKSHEET #3

Calculating Your Maximum Mortgage Payment and Mortgage Amount

You can use the ratio method for calculating the maximum mortgage payment a lender may allow, based on your income and debts. In this worksheet, we employ 33% for the housing expense ratio and 38% for the total debt ratio. These ratios are typically used for affordable housing mortgage products that target first-time home buyers and/or those with limited income and savings.

HOUSING EXPENSE RATIO

Total Gross Monthly Income *(from Worksheet #1)*	$ ______	
times 33%	x .33	
Maximum Mortgage Payment *(covering PITI and homeowner association or condo fee)*	$ ______	(a)

TOTAL DEBT RATIO

Total Gross Monthly Income *(from Worksheet #1)*	$ ______	
times 38%	x .38	
Maximum Mortgage Payment plus Monthly Debt Payments *(covering PITI and homeowner association or condo fee)*	$ ______	(b)

So these two calculations show you the maximum allowed under such mortgage products for your (a) mortgage payment and for (b) your mortgage payment plus monthly debt payments. Now let's subtract your current monthly debt payments from (b) above to see how much is left over for your mortgage payment:

MINUS CURRENT MONTHLY DEBT PAYMENTS

Maximum Mortgage Payment plus Monthly Debt Payments *(covering PITI and homeowner association or condo fee)*	$ ______	(b)
minus Monthly Debt Payments *(from Worksheet #2)*	-$ ______	
Maximum Mortgage Payment *(covering PITI and homeowner association or condo fee and minus Current Monthly Debt Payments)*	$ ______	(c)

Choose the lower of (a) or (c). This figure is the maximum allowable for your mortgage payment given your current income and debt.	$__________ (d)

As we know, your mortgage payment has four components—or PITI—principal, interest, taxes, and insurance. In order to calculate the mortgage amount made possible by (d), we need to include only the P and I components. So multiply (d) by 80% to arrive at the P and I portion of the payment.

$__________ (d) x .80 = $__________ (e) = (P and I portion only)

Divide (e) by the factor below for the interest rate or rates currently being offered by mortgage lenders for 30-year fixed-rate loans.

INTEREST RATE	P & I FACTOR FOR 30 YEAR TERM
5.5%	.00568
6.0%	.00600
6.5%	.00632
7.0%	.00665
7.5%	.00699
8.0%	.00734
8.5%	.00769
9.0%	.00805
9.5%	.00841
10.0%	.00878
10.5%	.00915
11.0%	.00953

$______________ (e) divided by P&I Factor ______________ =

$__________________ Maximum Loan Amount

Remember that these calculations are based on one set of ratios—33% for housing expense and 38% for total debts. Other mortgage products have different ratios.

Also remember that the calculations take into consideration only some of your monthly expenses. They do not include groceries, utility payments, the cable bill, and so on. You should consider your **total cash flow situation** to make sure that you will be able to afford your new home and new mortgage payments.

WORKSHEET #4

Shopping for a Mortgage

Lender's name	(1)	(2)	(3)
Contact's name			
Phone number			
Web site			
Loan amount you need	$	$	$
Type of mortgages available *(conventional, FHA, VA, fixed-rate, ARMs)*			
Interest rate			
Points			
APR			
Rate lock-in: • After loan approval or at application? • Written agreement? • Lasts how long? • Covers both rate and points?	______ Yes or No ______ Yes or No	______ Yes or No ______ Yes or No	______ Yes or No ______ Yes or No
Loan terms available			
FEES:			
• Application	$	$	$
• Origination	$	$	$
• Credit report	$	$	$
• Document preparation	$	$	$
• Underwriting	$	$	$
• Appraisal	$	$	$
• Survey	$	$	$
• Courier	$	$	$
• Flood certification	$	$	$
• Assumption *(if applicable)*	$	$	$
• Lender's attorney	$	$	$
• Title search and insurance	$	$	$
• Other	$	$	$
• Other	$	$	$

Are escrows required for taxes and insurance?	Yes or No	Yes or No	Yes or No
Minimum down payment required • with PMI • without PMI	 $ ______ $ ______	 $ ______ $ ______	 $ ______ $ ______
If PMI is required • Upfront cost • Monthly premiums • Automatically cancelled at what point?	 $ ______ $ ______	 $ ______ $ ______	 $ ______ $ ______
** Prepayment penalty: • Is there one? • If yes, how long is it in effect?	Yes or No	Yes or No	Yes or No
Is the loan assumable?	Yes or No	Yes or No	Yes or No
** Is credit life insurance required? • If yes, how is the premium paid?	Yes or No	Yes or No	Yes or No
Application options • Face-to-face meeting • Via telephone and fax • Online application	 ______ ______ ______	 ______ ______ ______	 ______ ______ ______
Payment options • Monthly • Biweekly • Automatic deduction • Other?	 ______ ______ ______ ______	 ______ ______ ______ ______	 ______ ______ ______ ______
** Do you report payment data to the national credit bureaus?	Yes or No	Yes or No	Yes or No
FOR ARMS ONLY:			
• Initial interest rate • Adjusted how frequently? • Index • Margin	______ ______ ______ ______	______ ______ ______ ______	______ ______ ______ ______
Rate Caps • Periodic • Lifetime			

Payment Cap • Can negative amortization occur? • If so, is the maximum LTV also capped?	Yes or No Yes or No	Yes or No Yes or No	Yes or No Yes or No
If convertible: • When can the loan be converted to a fixed-rate? • What fees are charged? • What index is used? • What margin is used?			

****Remember the possible warning signs of a "predatory" lender****

- Prepayment penalty of five years or longer
- Requirement that credit life insurance premium be added to the mortgage loan amount or otherwise paid as a lump sum at closing
- Does not report your mortgage payment history to the three national credit bureaus

WORKSHEET #5

Checklist of What to Bring When Applying for Your Mortgage

- Personal check for the loan application fee
- Copy of sales contract for the property you are buying
- Copy of real estate listing for the property you are buying
- Photocopy of the earnest money check

Each individual on the loan application must bring:

- Payroll stub(s) from employer or W-2 forms for the past two years or other proof of employment and salary.
- If self-employed: balance sheets, tax returns for the past two years, and year-to-date profit and loss statement
- Copies of last three monthly bank statements for all checking and savings accounts
- Company name, number, and value of stocks and bonds you own
- Make, year, and value of all cars you own
- If establishing a nontraditional credit history: canceled checks or money order receipts as evidence of rental, utility, or other payments made on time *(information on nontraditional credit histories can be found in Chapter II)*

WORKSHEET #6

Energy Efficiency Checklist

Use this checklist to determine opportunities for increasing energy efficiency and decreasing your utility and water bills.

Windows • Are the windows Energy Star rated? • Are the windows double-glazed or are there storm windows? • Are the windows *(and doors)* weather stripped?	
Skylight • Is the skylight windstorm resistant and properly sealed and caulked?	
Heating system • Is the type of fuel used the most economic available in your area? • Has the system been checked by a professional at least once each year? • Are filters cleaned or changed at least every other month? • Is there a programmable thermostat?	
Ventilation • Are there exhaust fans in each bathroom? • Does the kitchen range hood exhaust to the outside?	
Air-conditioning • Is the equipment correctly sized for the area being air-conditioned? • Has the system been checked by a professional at least each year?	
Ductwork • Have the ducts been tested for leaks?	
Water heater • Is the type of fuel used the most economic available in your area? • Is the water heater drained annually? • If an older model, has the water heater been insulated?	
Insulation • Are the attic, walls, and crawl space/basement insulated? • Is the R-value of the insulation appropriate for your area of the country? • Are there any gaps in the insulation?	
Appliances • Are any of the appliances *(refrigerator, washer, dryer, for example),* Energy Star rated? • Is the dishwasher used only when fully loaded?	
Water • Are there low-flow showerheads and faucets installed? • Are there low-flow toilets installed?	
Outdoors • Do all gutters drain into splashblocks that carry the water away from the foundation?	

WORKSHEET #7

Maintenance Checklist

Use this checklist to remind you of ongoing maintenance responsibilities:

In the Fall:

Windows and Doors	
• Check all weather stripping and caulking. Replace and/or repair as necessary.	
• Take down screens *(if the removable type);* clean and store them.	
Heating system	
• Have the system checked by a professional at least once each year.	
• Change or clean filters.	
Air-conditioning	
• Have the system checked by a professional at least once each year.	
• Remove window air-conditioners or put weatherproof covers on them.	
Water heater	
• Drain the hot water heater and remove sediment from the bottom of the tank.	
Insulation	
• Check insulation wherever possible; replace or add as necessary.	
Appliances	
• Clean refrigerator coils.	
Smoke and carbon monoxide detectors	
• Check batteries on all smoke and carbon monoxide detectors.	
Water	
• Check all faucets for leaks; replace washers if necessary.	
Outdoors	
• Drain outside faucets.	
• Clean gutters and drain pipes of leaves.	
• Check roof for leaks; repair as necessary.	
• Check flashing around vents, skylights, and chimneys for leaks.	
• Check chimney flue; clean any obstructions and make sure the damper closes tightly.	
• Inspect wood frame for termites; re-treat as necessary.	

In the Spring

Window and Doors	
• Check all weather stripping and caulking. Replace and/or repair as necessary.	
• Take down storm windows *(if the removable type);* clean and store them.	
• Check all door and window screens; patch or replace as needed; put screens up.	
Heating system	
• Change or clean filters.	
Air-conditioning	
• Have the system checked by a professional at least once each year.	
• Replace filters on air-conditioners.	
Water heater	
• Drain the hot water and remove sediment from the bottom of the tank.	
Insulation	
• Check attic for proper ventilation.	
Appliances	
• Clean refrigerator coils.	
• Check seals on refrigerator and freezer.	
• Check and clean dryer vent, stove hood, and room fans.	
Water	
• Check all faucets for leaks; replace washers if necessary.	
• Check basement wall and floors for dampness; if too moist, consult a professional.	
Outdoors	
• Check the exterior for cracked or peeled paint; caulk and repaint as necessary.	
• Check for cracks or surface deterioration if you have a concrete or block foundation. Consult a professional if you have any leaking or severe cracking.	
• Check roofs for leaks; repair as necessary.	
• Clean garage doors; refinish and/or repair as necessary.	

WORKSHEET #8

Making Your Money Work for You—Monthly Net Income

Unlike Worksheets 1 through 3, we are going to work with your net take-home pay *(that is, your income AFTER taxes and other items are deducted from your paycheck)* in the following Worksheets.

	AVERAGE MONTHLY AMOUNT	
	YOURSELF	CO-BORROWER
If you are paid **weekly**:		
$__________ x 52 divided by 12 =	$	$
If you are paid **every other week**:		
$__________ x 26 divided by 12 =	$	$
Second job	$	$
Regular overtime	$	$
Bonuses/tips	$	$
Alimony, child support, or other maintenance income		
Pension/Social Security benefits	$	$
Dividend/interest earnings	$	$
Business earnings	$	$
Veterans Administration benefits	$	$
Unemployment compensation	$	$
Public assistance	$	$
Other	$	$
Other	$	$
Total for Each Co-Borrower	**$**	**$**
Grand Total = Monthly Net Income	**$**	

WORKSHEET #9

Making Your Money Work for You—Monthly Expenses

HOUSING EXPENSES	
Mortgage Payment	$
Homeowner association or condo fee *(if applicable)*	$
Utilities:	$
• Gas	$
• Electricity	$
• Water	$
• Oil	$
• Other	$
Home Maintenance Allowance***	$
Total Housing Expenses	$
OTHER EXPENSES	
Food	
• Groceries	$
• Meals away from home *(including daily lunch)*	$
Child care or child support	$
Transportation	
• Car payment(s)	$
• Car insurance premium	$
• Car maintenance and gas	$
• Parking, tolls, etc.	$
• Public transportation fees	$
Credit cards	
• Card #1	$
• Card #2	$
• Card #3	$
Communication	
• Telephone	$
• Internet service provider fee	$
Education	
• Student loan	$
• Tuition/school fees	$
Clothing	$
Entertainment	
• Cable TV	$
• Video/DVD rentals	$
• Sports, concerts, movies	$
• Other	$
Pets	
• Food/toys	$
• Vet care	$

Charity/church	$
Medical • Expenses not covered under insurance plan	 $
• Medications/Prescriptions	$
Emergency Fund***	$
Cash Outlays	$
Other	$
Other	$
Other	$
Total Other Expenses	$
Grand Total of All Monthly Expenses	$

*** Remember to set aside funds each month for a home maintenance allowance—of around 1% of the purchase price of your home. For example, if you are paying $96,000 for your home, you should save 1% of $96,000 or $960. Divide the $960 by 12 months and you get $80.

***You should also establish an emergency fund. Financial advisors suggest saving 5% of your take-home pay. So if your monthly take-home pay is $3,000, you should place 5% or $150 in your emergency fund each month. And never, ever touch this fund until a real emergency arrives.

WORKSHEET #10

Making Your Money Work for You—Income vs. Expenses

Monthly Net Income *(from Worksheet #8)*	$
MINUS	–
Monthly Expenses *(from Worksheet #9)*	$
RESULT	$

- If your income is larger than your expenses, good work!
- If very little or nothing is left over each month *(that is, your monthly expenses are larger than your income)*, go directly to Worksheet #11.

WORKSHEET #11

Making Your Money Work For You—Deciding Where to Cut Back

Decide which of your monthly expenses are **fixed** *(that is, you cannot change the amount spent)* and which are **discretionary** *(that is, you could change the amount spent)*:

	FIXED	DISCRETIONARY
Mortgage Payment		
Homeowner association or condo fee *(if applicable)*		
Utilities		
• Gas		
• Electricity		
• Water		
• Oil		
• Other		
Home Maintenance Allowance		
OTHER EXPENSES		
Food		
• Groceries		
• Meals away from home *(including daily lunch)*		
Child care or child support		
Transportation		
• Car payment(s)		
• Car insurance premium		
• Car maintenance and gas		
• Parking, tolls, etc.		
• Public transportation fees		
Credit cards		
• Card #1		
• Card #2		
• Card #3		
Communication		
• Telephone		
• Internet service provider fee		
Education		
• Student loan		
• Tuition/school fees		
Clothing		
Entertainment		
• Cable TV		
• Video/DVD rentals		
• Sports, concerts, movies		
• Other		

	FIXED	DISCRETIONARY
Pets		
• Food/toys		
• Vet care		
Charity/church		
Medical		
• Expenses not covered under insurance plan		
• Medications/prescriptions		
Emergency Fund		
Other		
Other		
Other		

Now decide which of the discretionary expenses you checked above are needs and which are wants:

DISCRETIONARY EXPENSES			
NEEDS: CAN'T LIVE WITHOUT		WANTS: NICE TO HAVE	
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$

Prioritize your Want list and then decide how much you can really afford to pay for each item each month:

WANTS: NICE TO HAVE			
ORDER OF PRIORITY		AMOUNT YOU NOW PAY	AMOUNT YOU CAN REALLY AFFORD TO PAY
#1		$	$
#2		$	$
#3		$	$
#4		$	$
#5		$	$
#6		$	$
#7		$	$
#8		$	$
#9		$	$
#10		$	$
TOTAL		$	$

TOTAL Amount You Now Pay	$
MINUS	–
TOTAL Amount You Can Really Afford to Pay	$
Your Potential Savings	$

Working through each of these steps can help you get a clearer picture of where your money is going each month AND where you may be able to cut back!

Resources

Buying a Home Means Borrowing Money

Credit

Three Major Credit Reporting Agencies

- www.equifax.com: Equifax
- www.experian.com: Experian
- www.transunion.com: Transunion

  In addition to ordering credit reports and credit scores online, each site provides helpful consumer information on credit and credit reports.
- www.fairisaac.com: Fair, Isaac and Company—includes consumer information on credit scoring and how you can improve your FICO score.
- www.ftc.gov: Federal Trade Commission has a number of helpful consumer publications that you can download, including *Building a Better Credit Record*. On the initial screen, select News Releases, Publications & Speeches; on the following screen, select Publications—Consumer & Business.

Shopping for a Mortgage

- www.va.gov: The web site for the Veterans Administration includes information on the VA loan program and its eligibility requirements.
- www.hud.gov: The web site for the U.S. Department of Housing and Urban Development (HUD) provides information on the FHA mortgage product and extensive background material on the home-buying process.
- www.rurdev.usda.gov/rhs: The site of Rural Housing Services within the U.S. Department of Agriculture provides information on their mortgage loan programs
- www.ncsha.org: The National Coalition of State Housing Agencies provides a Directory of State Housing Agencies on this web site.
- www.mbaa.org: The Mortgage Bankers Association of America is the trade group for mortgage bankers. Their site includes some basic consumer information on the mortgage process.
- www.namb.org: The National Association of Mortgage Brokers (NAMB) is a trade group for mortgage brokers. Their site includes a search feature to locate NAMB members in your area.

Predatory Lending

- www.stopmortgagefraud.com: Helpful pointers for detecting potential predatory lending practices, published by the Mortgage Bankers Association. Also available in Spanish.
- www.fanniemaefoundation.org: The Fannie Mae Foundation has produced a series of publications related to home-buying. The credit publication, *What You Don't Know Can Hurt You*, focuses on predatory lending warnings. These publications are available in six languages.

- www.dontborrowtrouble.com: Freddie Mac's consumer awareness campaign combines public education and counseling services to help homeowners avoid lending practices that strip away equity.

You Finally Get the Keys!

Closing/Settlement Process

- www.hud.gov: The HUD web site provides consumer information on the mortgage process, including *Buying Your Home: Settlement Costs and Helpful Information* which can be printed from the site.
- www.alta.org: The American Land Title Association is a national association for title insurance companies. The Consumer section of their web site provides a detailed description of the closing process, from the perspective of the title insurer and title searcher.

In the Long Run

Energy Efficiency

- www.energystar.gov: Use this site to locate the brands of clothes washers, refrigerators, dishwashers, and room air-conditioners, and other appliances with the Energy Star label. There is also a search tool for locating stores that sell these brands in your area of the country.
- www.homeenergysaver.lbl.gov: The Home Energy Saver is an Internet-based tool for calculating energy use in homes. It is designed to help you identify how best to save energy and find the resources to do so. It is sponsored by the U.S. Department of Energy (DOE) and the Environmental Protection Agency.
- www.eren.doe.gov: The Office of Energy Efficiency and Renewable Energy within DOE developed a very helpful publication known as *Energy Savers (available online)* that supplies basic steps on how to make your entire home—from top to bottom—as energy-efficient as possible.

The Financial Side

Taxes and Homeownership

- www.irs.ustreas.gov: Via the IRS web site, you can print a copy of Publication 530—*Tax Information for First-Time Homeowners.* This publication provides details on which homeownership expenses you may and may not deduct from your federal tax return and how to do so. From the main IRS screen, select Individuals. Then, under Resources, select Forms and Publications.

Mortgage Insurance Cancellation

- www.privatemi.com: The Mortgage Insurers of America provide specific information on how and when private mortgage insurance may be canceled. They also provide a link to HUD's explanation of how and when FHA mortgage insurance premiums may be canceled.

Housing Counselors

- www.hud.gov: HUD's web site includes lists of agencies that are approved by HUD to provide housing counseling.
- www.fanniemae.com: The For Home Buyers & Homeowners section of the Fannie Mae web site provides lists of local agencies that provide both housing and credit counseling.

Credit Counselors

- www.nfcc.org: The National Foundation for Credit Counseling provides information on 2,000 member agencies in the U. S. and in Canada that provide credit and housing counseling via face-to-face meetings, telephone discussions, and over the Internet.

Shopping for Your Home

Real Estate Agents

- www.realtor.com: National Association of REALTORS®—includes listings of properties for sale and of members who are Accredited Buyer Representatives.
- www.naeba.com: The National Association of Exclusive Buyer Agents web site allows you to e-mail a request for the names of local member agents.
- www.realestateespanol.com: The web site of the National Association of Hispanic Real Estate Professionals provides a tool for searching for local agents as well as property listings.

Real-Estate Owned (or REO) Properties

- www.hud.gov: From the HUD web site, you can access lists of homes for sale from several federal agencies as well as from Fannie Mae and Freddie Mac.

Sales Data on Comparable Properties

- www.homegain.com: One of several web sites that access registries and report historical sales data for whatever area *(a single address or an entire street)* you designate. Be wary of their "valuation" report, however.

Finding a Home Inspector

- www.ashi.org: American Society of Home Inspectors, Inc.—search feature allows you to locate local home inspectors with one of the following designations:

  Members (M) Members of ASHI have met certain requirements:
  - Passed the National Home Inspector Examination and ASHI's Standards and Ethics Examination.
  - Had inspection reports successfully verified for compliance with ASHI's Standards of Practice.
  - Submitted valid proof of performance of at least 250 fee-paid home inspections that meet or exceed the ASHI Standards of Practice.

  Candidates w/ Logo (CL) Candidates with Logo Use Privilege have met most of the requirements for Member status:
  - They have passed the National Home Inspector Examination and ASHI's Standards and Ethics Examination.
  - ASHI has verified performance of 50 fee-paid inspections in substantial compliance with the Standards of Practice.

  Candidates (CN) Candidates have not yet met the ASHI Member requirements, however:
  - Candidates may be highly experienced inspectors who have just joined ASHI, or they may be novice inspectors who have completed training or otherwise entered the profession.

Overall Guidance on the Home-Buying Process

- www.fanniemae.com: The For Home Buyers and Homeowners section of the Fannie Mae web site provides a variety of resources, including several calculators and lists of housing counselors and lenders.
- www.freddiemac.com: Freddie Mac provides an interactive home buyer guide, as well as information on maintaining healthy credit habits. Their CreditSmart material is available in both English and in Spanish.
- www.fanniemaefoundation.org: The Fannie Mae Foundation has produced a series of publications related to home-buying. These publications can be printed from their web site or ordered online and are available in six languages.

Glossary

Adjustable Rate Mortgage (ARM)	The interest rate on an adjustable rate mortgage loan changes at specific times over the life of the loan based on changes in an independent index. Interest rate or payment changes may be capped; if the latter occurs, negative amortization may result.
Amortization	A loan is repaid in equal installments, calculated over the term or life of the loan. In the early years, most of the loan payment is applied to interest while in the latter years, most is applied to principal.
Annual Escrow Statement	Each year, the servicer will forward an itemized statement showing the payments collected over the prior 12 months and how they were applied to principal, interest, taxes, and insurance. The statement should also disclose when the tax and insurance payments were made.
Annual Percentage Rate (APR)	The total cost of a loan calculated on an annualized basis. APRs make it easier to compare loan products with different rate and point combinations.
Appraisal	Appraisals estimate the market value of a home based on comparisons with similar properties. Unlike a home inspection, the appraisal does not produced a detailed assessment of the systems or structure of the property.
Appreciation	The value of a property may increase, or appreciate, over time. Two factors that influence the value of a home are the economic health of the region and how well the property is maintained.
Assumption	Under an assumption, an individual takes over the existing mortgage of a property with the approval of the servicer. However not all mortgage products may be assumed.
Automated Underwriting	Automated underwriting is a computer-based approach that enables a lender to process a loan application more quickly, efficiently, and objectively—and use more sophisticated measures of risk.

Biweekly	For most loans, payments are made on a monthly basis. However, with biweekly mortgages, payments are made every other week. Because each payment is equal to one-half the monthly payment, the equivalent of 13 monthly payments are made over a year. *(In other words, 52 weeks divided by 2 equals 26 biweekly payments; 26* biweekly payments equal 13 monthly payments.)
Closing Costs	The costs paid at closing by the buyer and seller. These costs are itemized on the HUD-1 Settlement Statement. Closing costs may range from 3% to 10% of the sales price of the home.
Closing	At the closing or settlement, ownership of the property is legally transferred from the seller to the buyer.
Community Property	Property acquired by husband, wife or both during marriage which gives each spouse an interest in the property whether each appears in title or not.
Condominium	A type of property ownership in which the owner holds title to an individual living unit and shares ownership of the common areas.
Contingency	A condition on the sales contract that must be met to make the contract legally binding. Typical contingencies include financing and appraisal.
Conventional Mortgage	If a mortgage loan is not insured or guaranteed by the federal government, it is considered to be a conventional loan.
Co-op	Co-ops or Co-operatives are a type of property ownership in which each Co-op owner holds a share in the corporation that owns the entire building.
Credit Score	A credit score is a statistical method of measuring an individual's management of credit. It predicts the relative likelihood that the individual will repay a mortgage or other forms of debt. Most mortgage lenders use the credit score formula developed by Fair, Isaacs and Company, known as the FICO score.
Deed-in-lieu of Foreclosure	The servicer agrees to accept the deed to your property in case of loan default. This option is typically considered only after all others have been explored.

Depreciation — The value of a property may decrease, or depreciate, over time. Two factors that influence the value of a home are the economic health of the region and how well the property is maintained.

Discount Points — One discount point is 1% of the loan amount. These points represent interest paid up front to the lender, rather than over the life of the loan. Typically, the higher the interest rate, the lower the discount points, and vice versa.

Discretionary Expense — Discretionary expenses are within the control of the individual *(food, entertainment, etc.),* unlike fixed expenses which cannot be changed *(car payment, cable bill, etc).*

Down Payment — The portion of the sales price paid in cash. Down payments typically range from 3% - 5% for first time home buyers.

Earnest Money — A portion of the down payment that is placed in escrow with the real estate agent when the sales contract is accepted. The earnest money deposit indicates the buyer's firm intention to purchase the property in question. If the contract is accepted by the seller, these funds will be for the purchaser's down payment and closing costs.

EnergyStar® — The U.S. Environmental Protection Agency (EPA) and the U.S. Department of Energy (DOE) award EnergyStar labels to products that exceed minimum national efficiency standards. These high-performance products reduce energy costs each month they are in use.

Equity — The difference between the value of the property and the amount owed on the mortgage. Equity increases over time as the mortgage is paid down or if the property increases in value.

Escrow Accounts — Lenders typically collect 1/12 of the annual payments due on property taxes plus hazard and mortgage insurance premiums. These monthly payments are placed in an escrow account, from which the lender draws the tax and premium payments when they fall due.

Fixed-Rate Loan — The interest rate on a fixed-rate mortgage loan will not change throughout the life of the loan.

Forebearance	Under the terms of a formal, written agreement between the borrower and the servicer, the borrower's mortgage payments are reduced or suspended for a specific period of time. At the end of the period, the borrower is required to resume regular monthly payments plus an additional amount to make up for the past-due amount.
Foreclosure	The legal process by which a lender sells a property because the loan is in default.
Four C's	In traditional underwriting, the lender examines the Four C's to determine whether to grant the loan—Collateral, Capacity, Credit, and Capital.
Good Faith Estimate	Within three days of taking an application, the lender or mortgage broker must provide to the borrower an estimate of the closing or settlement costs.
Government Mortgages	Mortgage loans that are insured or guaranteed by the federal government.
Gross Monthly Income	The amount an individual earns before taxes and other deduction are taken out of the paycheck.
HVAC	HVAC refers to the heating, ventilation, and air-conditioning system of a home.
Home Energy Audit	A home energy audit reviews where energy is used and wasted in a home.
Home Energy Rating System (HERS)	A HERS audit examines the energy performance of the heating, cooling, and hot water use of a home in comparison with a "standard" home. The results of the study can be used to decide which energy-saving steps to take.
Home Equity Loan	Loans secured by a home that can be used for a broad variety of purposes—to consolidate loans, pay college tuition, take a vacation in New Zealand. The interest on home equity loan or lines of credit may be tax deductible. Please consult your tax advisor for details. Borrowers should carefully review the terms of such loans and whether they are affordable—because, in the end, the home is at stake!

Home Inspection	A home inspection, conducted by a certified inspector, includes a detailed review of the structure and systems of the home. The inspection report itemizes the condition of each item inspected and makes recommendations on how to address any deficiencies. This inspection is not required by a Lender, but is strongly recommended.
Home Warranty	Home warranties generally cover repairs to a specified part of a home, such as major appliances or the plumbing, electrical, heating, and air-conditioning systems.
Housing Expense Ratio	In traditional mortgage underwriting, the housing expense ratio is used as a guideline to calculate how large the monthly housing expense payments should be, based on gross month income. For example, if a mortgage product has a housing expense ratio of 33%, the borrower's monthly housing expenses should not exceed 33% of his or her gross monthly income.
HUD-1 Settlement Statement	The HUD-1 Settlement Statement is required at closing. It itemizes all of the closing or settlement costs paid by both the buyer and the seller. Both parties have the right to review the HUD-1 statement 24 hours before the scheduled closing.
Joint Tenancy	A form of ownership under which owners have equal interest in the property and may sell their interest to whomever they choose. When one owner dies, the surviving owner(s) automatically inherit that share.
Loan Modification	With a loan modification, the servicer changes one or more of the terms of the loan to help the borrower bring the defaulted amount current. This option is generally used with borrowers whose financial problems are expected to be long-term.
Loan Officer	Unlike a mortgage broker who has relationships with dozens of lenders, a loan officer works for only one lender. The loan officer should work with an applicant to make the best "match" between the applicant's financial situation and the lender's loan products.
Loan to Value (LTV)	The loan to value is calculated by dividing the unpaid loan balance by the current value of the property.

Manufactured (Chassis-Built) Home	A factory built home on a permanent frame with a removable transportation system, delivered and permanently attached to a site-built foundation.
Modular Home	A home constructed on an assembly line on conventional home floor joists and delivered to the site on a trailer.
Mortgage or Deed of Trust	The Mortgage or Deed of Trust is the recorded evidence of the promise to repay the loan; if the loan is not repaid as promised, the lender may take over the property.
Mortgage Broker	A mortgage broker acts as the intermediary between a borrower and the lender. Brokers must specify up front exactly how they are being paid for their services.
Mortgage Insurance	Mortgage insurance reimburses the lender or investor for losses incurred during a foreclosure. The borrower pays the monthly mortgage insurance premium.
Multiple Listing Service	A listing of properties for sale maintained by local members of the National Association of REALTORS®.
Negative Amortization	Negative amortization may occur on adjustable rate mortgage loans with payment caps. If the cap is reached, the difference between what the borrower is paying and what he or she would pay without the cap is added to the loan balance—resulting in negative amortization.
Nontraditional Credit	If an individual has no traditional history of credit—credit cards or student or car loans—he or she may document a good payment record using other sources, including rent, utilities, telephone, cable payments, and other accounts.
Note	The Note is signed by the borrower at closing and is the formal promise to repay the mortgage loan according to the terms specified in the Note.
Origination Point	Lenders may charge origination points to offset the administrative costs of processing and underwriting the loan. Each point is 1% of the loan amount.

Panelized Home	Walls, floors and roof in small panel form are assembled at the site and attached to a foundation.
PITI	A mortgage payment includes four parts—Principal, Interest, Taxes, and Insurance.
Pre-cut Home	Lumber is cut to specific lengths at the factory and then the home is constructed by workmen at the permanent site.
Predatory Lenders	There is no single, clear-cut definition of predatory lending. Basically, a lender exhibits predatory behavior when placing its interests above the interests of the borrower. For example, a predatory lender will not hesitate to approve someone for a loan amount they cannot possibly afford.
Preforeclosure Sale	Under this arrangement, the servicer agrees to accept the proceeds from the sale of a home even though the amount is less than owed.
Prepayment Penalty	If the borrower makes an additional principal payment or pays off the loan more quickly than the prescribed payment schedule, that borrower could incur a prepayment penalty.
Prepays	The lender may collect certain expenses at closing in advance of when they are due, such as collecting one full year's premium for mortgage insurance and/or hazard insurance to set up the escrow accounts.
R-value	The R-value measures the resistance to heat flowing through insulation over time. Insulation with greater resistance *(and a higher R-value)* means that heat enters or leaves more slowly. The U.S. Department of Energy has determined the appropriate R-values for each area of the country.
Rate Lock-In	A written agreement under which the lender will lock in or guarantee an interest rate/point combination for a period of time after taking the loan application.
Refinance	Paying off one mortgage with the proceeds of another mortgage on the same property—usually to reduce the interest rate and mortgage payment.

Reverse Mortgage	For homeowners aged 62 or older, it is possible to take down a reverse mortgage, under which they receive funds according to a schedule they select. The amount owed is typically not repaid until after the senior leaves or sells the home or it passes into an estate. Even then, neither the senior or the senior's estate can be required to pay more than the value of the home.
Second Mortgage	Second mortgages are so-called because the loan is subordinated to the first mortgage. In other words, the second mortgage lender stands in line behind the holder of the first mortgage in case of a foreclosure.
Servicing	The process of collecting monthly loan payments is known as servicing the loan. The original lender may service the loan or may transfer the servicing to another lender. In fact, servicing transfers may occur at any point over the life of the loan. But the basic terms of the mortgage loan remain unchanged.
Sole Ownership	Under sole ownership, title to the property is held in one person's name only.
Survey	A drawing or map of the precise boundaries of the property as well as easements, rights of way and other physical features.
Tenancy By Entirety	Married couples may hold title as "tenants by entirety." When one spouse dies, the property is automatically inherited by the surviving spouse.
Tenancy In Common	If title to the property is held using this option and one owner dies, that ownership may go to his or her heirs, rather than to the surviving owner(s).
Term	The term is the maximum period of time over which the mortgage is re-paid.
Title	A legal document evidencing the legal ownership of a property.
Title Insurance	Title insurance protects the holder of the policy against loss resulting from disputes over ownership of the property. The borrower is required to buy a policy for the lender and should also buy a policy to protect their own interests as well.

Total Debt Ratio

In traditional mortgage underwriting, the total debt ratio is used to calculate how large the monthly payments on housing expenses and other debts *(like student and car loans, credit card debt,etc.)* should be, based on gross monthly income. For example, if a mortgage product has a total debt ratio of 38%, the borrower's housing expenses plus other debts should not exceed 38% of his or her gross monthly income.

Townhouse

A type of condominium in which one owns an individual townhouse living unit and shares ownership of the common areas.

Transfer of Servicing

At any point, the lender or servicer collecting the mortgage payments may transfer that responsibility to another servicer. The basic terms of the mortgage will remain unchanged and borrowers have a 60-day grace period in case their payments go to the wrong place.

Truth in Lending

Within three days of taking an application, the lender or mortgage broker must provide a borrower with a Truth in Lending Disclosure statement, showing the total amount to be financed, all of the costs to be paid on an annualized basis *(the APR),* the payment schedule and total of payments you will make, the prepayment and late payment policy.

800.966.4PMI (4764)

www.pmi-us.com

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