The Knowledge Resource FOR Mortgage Funding

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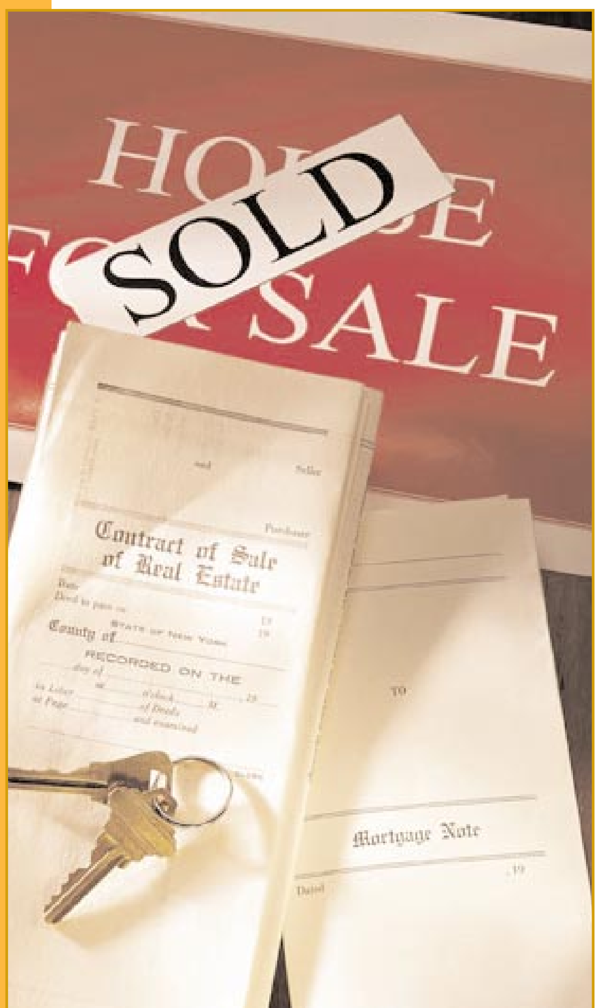
Mortgage Basics

Simply put, a mortgage is a loan you take out to finance the purchase of your home. It's also a legal contract stating that you promise to pay back the loan on a monthly basis. Your monthly payment typically goes toward interest, taxes and insurance as well as the principal.

There are several varieties of mortgages. Fortunately, there are just a few basics you need to know in order to understand most of them.



Fixed-rate mortgages have a fixed interest rate over the term of the loan. By far, most mortgages closed each year are fixed-rate mortgages. The advantage of a fixed-rate mortgage is that your monthly payment never changes. The disadvantage is that if interest rates fall below your fixed-rate and you want to lower your rate and consequently lower your payment, you'll have to refinance.

Adjustable-rate mortgages (ARMs) start with a lower rate than a fixed-rate for an introductory period – typically 1, 3, or 5 years – after which the rate adjusts – usually annually – based on a pre-determined index. An ARM is a good choice if you're expecting to live in your home for less than five years and ARMs can also help you qualify for a larger loan.

The **term** of your mortgage is how many years you have to pay back the loan. Most people opt for 30-year terms, but 15- and 20-year terms are available.

How much should you put down? The down payment is the difference between how much you borrow and the purchase price of your home. And, in spite of what most people think, you don't need a big down payment to buy a home.

Getting Prequalified

Reasons to Get Prequalified…

- With prequalification, you have plenty of time to determine which loan program best fits your needs and which programs you qualify for. (List of loan programs to follow).
- You will know exactly how much you are qualified for. It’s no fun to find the ideal home and then find out you can’t afford it.
- Your monthly payment will be set. This will allow you to budget your money before making this large investment.
- You will learn what the down payment and closing costs will be.
- If you are a first-time buyer, you may be able to qualify for a special program which may expand your buying power by giving you a lower rate or supplementing your down payment.
- If you feel that you can afford a higher mortgage payment but are not able to meet qualifications, co-mortgagor financing may be available to you.

Most Real Estate Agents and Lenders recommend that home buyers get prequalified with a lender before selecting a home to purchase. This way you will have the best information about your price range.

Types of Loans

Adjustable Rate Mortgage	Adjustable rate mortgages have an interest rate that is adjusted at certain intervals based on a specific index during the life of the loan.
Balloon Payment Loan	A fixed rate that becomes due and payable at the end of a certain term. The final payment is larger than the preceding payments and pays the note in full.
Buy-Down Loan	Buy-Down loans are fixed rate loans where the interest rate and the payment are reduced for a specific period of time by paying the interest up front to subsidize the lower payment.
Community Home Buyer's Program	A fixed rate loan for first-time buyers with a low down payment, usually 3-5%, no cash reserve requirement and easier qualifying ratios. Borrower must meet income limits and attend a four-hour training course on homeownership.
Conventional Loan	Conventional loans are sometimes more lenient with the appraisal and condition of the property. When you are buying a "fixer upper," you may need to use a conventional loan. Homes purchased above the FHA loan limit are usually financed with conventional loans.
FHA Loan	FHA loans are insured by the Federal Housing Administration under H.U.D. They offer a low down payment and are easier to qualify for than conventional loans.
Fixed Rate Loan	A fixed rate loan has one interest rate that remains constant throughout the life of the loan.
Graduated Payment Mortgage	A fixed rate loan that has payments starting lower than a standard fixed rate loan, which then increases by a predetermined amount each year for a set number of years.
Non-Qualifying Loan *(Assumable)*	Non-Qualifying loans are preexisting loans which can be assumed by a buyer from the seller without going through the qualifying process. The buyer pays the seller for his or her equity and then starts making payments.

The Loan Process

Prequalification/Interview

- Application interview
- Lender obtains all pertinent documentation

Order Documents

- Credit report, appraisal on property, verifications of employment, mortgage or rent, and funds to close, landlord ratings, preliminary title report

Loan Submission

- The loan package is assembled and submitted to the underwriter for approval

Documentation

- Supporting documents come in
- Lender checks on any problems
- Requests for any additional items are made

Loan Approval

- Parties are notified of approval and conditions prior to documentation

Documents Are Drawn

- Loan documents are completed and sent to escrow
- Borrowers come in for final signatures

Funding

- Lender reviews the loan package
- Funds are transferred by wire

Recording of Documents

- Title company records the deed of trust at the county recorder's office
- Escrow is now officially closed

Points Explained

What is a point?
One point is equal to 1% of the NEW Loan Amount.

Why do Lenders charge points?
Whenever governmental regulation, state usury law and/or competitive practices prohibit the lender from charging a rate of interest which would make the real estate loan competitive with other fields of investments, the lender must seek some method of increasing the yield for investors. By charging "points," the lender can bring the real estate loan up to those other investments.

Are points called by different names?
Yes: Loan Origination Fee, Commitment Fee, Discount Fee, Warehousing Fee, Funding Fee, etc.

Who must pay the points?
FHA: The Buyer is usually charged with the Loan Origination Fee; the Discount Fee can be paid by the Buyer or Seller.

VA: The Buyer is usually charged with the Loan Origination Fee and the Funding Fee.

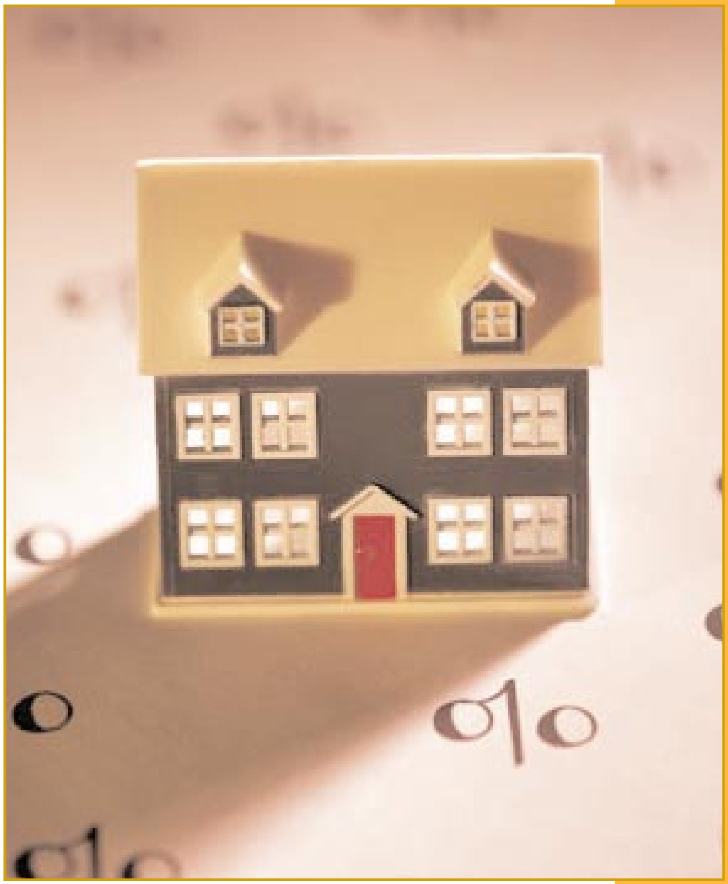
Conventional: Points can be paid by the Buyer, the Seller, or split between the two. Should be stated on Contract of Sale!

City/County/State government sponsored loans: as published by them.

Other names for points:
Loan Origination Fee, Commitment Fee, Discount Fee, Warehousing Fee, Funding Fee

Does the number of points charged fluctuate?

Yes. If rates on mortgage loans are lower than other investments (such as stocks, bonds, etc.), funds will be drawn away from the mortgage market. Also, when there is a heavy demand upon the money market because of business needs or government borrowing, money for home mortgages becomes scarce and more expensive. When this occurs, more points can be charged. Points balance the market. Points are not set by government regulation, but by each lender individually.



On VA loans, is there any way to lock in the number of points?

Not without jeopardizing the sale. Even when a lender stipulates in writing the number of points to be charged, that guarantee states "if the interest rate is not changed by the government." Points charged on an FHA or conventional loan are usually not changed from commitment time to settlement.

Is FHA or VA financing unfair to sellers?

No. Homes can sell faster because more buyers can qualify with the lower down payment requirement and lower interest rates. Sellers receive all cash for their equity to reinvest in a new home or other investment. The purpose of these loans is to provide purchasers the opportunity to buy homes with minimal cash investment, thus providing a bigger market for sellers.

Are points deductible for income tax purposes?

Points on a home mortgage are deductible if points are generally charged in the geographical area where the loan is made, and are consistent with the number of points generally charged in that area. If you are in doubt about points being deductible, you should contact your tax return preparer.

The Appraisal

Having an idea of what is involved in appraising a piece of property can greatly help the seller arrive at a fair asking price and the buyer determine what to offer. An appraisal consists of several steps. The following are the major steps in the process:

1. Research the property as to size, bedrooms, baths, year built, lot size, condition, and square footage.

2. Gather data of recent sales in the neighborhood. The appraiser needs to locate at least three and preferably more similar-sized homes which have sold and closed escrow in the neighborhood. The homes need to be within one mile of the subject and sold within the past six months. These homes are considered the "Comparable Properties, " or "Comps" for short.

3. Field inspection consists of two parts: first the inspection of the subject property, and second, the exterior inspection of the comparable properties.

The subject inspection consists of taking photos of the street scene, front of the home and rear of the home, which may include portions of the yard. The appraiser will make an interior inspection for condition, noting any items that would detract from or add to the value of the home. He will also draw a floor plan of the home while doing the inspection.

The more that is known about the property prior to inspection, the better the appraiser can focus on researching the most similar comparables.

The inspection of the comparable properties is limited to an exterior inspection. For features that cannot be seen from the street, the appraiser has reports from Multiple Listing Services (MLS), county records, and appraisal files along with other sources to help determine the condition and amenities of the comparables. After the field inspection has been completed, the appraiser must determine which comparable properties most resemble the subject, making slight adjustments in value for any differences between them. After making the required adjustments, the appraiser must go through the reconciliation process with the three comparable properties to determine a final estimated value. This method of estimating value is called the ‘‘Direct Sales Comparison Approach to Value,’’ and it accounts for nearly all of the considerations in determining the value of single family homes.

It is important to consider that the appraiser will be taking photos of the street scene and of the front elevation of the subject. The street scene gives the lenders some idea as to the type of neighborhood in which the home is located. The photo of the front of the home gives the lender an idea of its condition and its curb appeal. And lastly, a photo of the back of the home and part of the rear yard is taken. Many homeowners don't take care of the rear portion of their homes and backyards, so for this reason the rear photo is required.

In most cases (over 90% of the time), the condition of the exterior of a home is indicative of the interior.

An appraiser will call in advance to set up the appointment to inspect the home. At that time, any information about recent improvements or additions to the home should be provided.

In order to facilitate the transfer of property from one owner to another, the best escrow companies will:

- Prepare, review and/or revise escrow instructions.
- Determine the legal ownership and status of the property through a "title search."
- Request a beneficiary's statement if a debt is to be assumed by the buyer.
- Confirm property meets requirements imposed by lender and/or buyer.
- Prorate all related financial matters (e.g., taxes, insurance) involved in the ownership transfer.
- Ensure all legal documentation is complete, including recording deed.
- Comply with time limits imposed in instructions.
- Close escrow when all instructions (buyer's, seller's and lender's) have been fulfilled.
- Disburse funds as instructed, including all related fees (title fees, commission if any, payoffs, etc.)
- Prepare final statement for all concerned parties.

The Escrow

You may have already heard phrases such as "the house fell out of escrow," or "we're waiting for escrow to close." So just what is escrow anyway? And what does it mean to a home buyer or seller?

Simply stated, escrow is the involvement of an impartial third party in a real estate transaction. This neutral third party acts as an intermediary between the buyer and seller, and also collects and remits funds as instructed. Buyer's funds are deposited with the escrow company, which then remits to the seller on the buyer's behalf. The basic concept of escrow is to ensure that both the buyer and seller are protected during any real property transaction. Not only is "escrow" the concept of a third party receiving and disbursing funds, but it also includes other valuable transaction services.

Escrows can be performed by banks, savings & loans and title companies, as well as independent escrow firms. In addition, escrow companies furnish the state with annual audits of their books, and all escrow funds must be kept in trust accounts. Thus, the state helps ensure that escrow companies are properly managed and act as truly impartial parties to any real property transaction.

Escrow companies are generally held liable if any instructions are violated during the course of an escrow. No changes may be made to any escrow instructions if changing them would be detrimental to any party involved. It is possible to change instructions once a property has "entered escrow," however, only by mutual agreement. Finally, all escrows have clearly defined time limits. If, for some reason, all instructions cannot be carried out by the end of the time limit, all parties involved are entitled to the return of documents, fees, funds and other related materials. They also may mutually agree to extend the time period by changing the instructions.

The term "escrow" has come to mean "neutral protection" for the seller, the lender and the buyer. All parties involved in the transfer of real property are impartially protected during the transaction, and are serviced by professionals intent on ensuring a smooth, trouble-free sale. Look for an escrow company that clearly defines its services, and which lists all fees and charges upfront.

Escrow is an indispensable necessity in today's marketplace. If you need further explanations during the process, always consult your escrow officer. The escrow company is, indeed, a neutral third party and its job is to make sure all sale conditions are met quickly and efficiently.

Look for
an escrow company that clearly defines its services, and which lists all fees and charges upfront.

Who Pays What

The SELLER can generally be expected to pay for:

- Real estate commission
- Document preparation fee for deed
- Documentary transfer tax
- Any city transfer/conveyance tax (according to contract)
- Loan fees if required by contract
- Payoff of mortgage balance on subject property
- Interest accrued to lender being paid off
- Statement fees, reconveyance fees and prepayment penalties
- Termite inspection (according to contract)
- Termite work (according to contract)
- Home warranty (according to contract)
- Any judgements, tax liens, etc., against the seller
- Tax proration (for any taxes unpaid at time of transfer of title)
- Any unpaid homeowner's dues
- Recording charges to clear all liens of record against seller
- Any bonds or assessments (according to contract)
- Any delinquent taxes
- Notary fees
- Escrow fees
- Title insurance premium

The BUYER can generally be expected to pay for:

- Title insurance premium upgrade
- Escrow fee
- Document preparation (if applicable)
- Notary fees
- Recording charges for all documents in buyer's names
- Termite inspection (according to contract)
- Tax proration (from date of acquisition)
- Homeowner's transfer fee
- All new loan charges (except those required by contract for seller to pay)
- Interest on new loan from date of funding to 30 days prior to first payment date
- Assumption/change of records fees for takeover of existing loan
- Beneficiary statement fee for assumption of existing loan
- Inspection fees (roofing, property inspection, geological, etc.)
- Home warranty (according to contract)
- City transfer/conveyance tax (according to contract)
- Fire insurance premium for first year

Yours or Theirs - The Personal vs. Real Property Dilemma

The distinction between personal property and real property can be the source of difficulties in a real estate transaction. A purchase contract is normally written to include all real property; that is, all aspects of the property that are fastened down or an integral part of the structure. For example, this would include light fixtures, drapery rods, attached mirrors, trees and shrubs in the ground. It would not include potted plants, free-standing refrigerators, washer/dryers, microwaves, bookcases that aren't built-in, swag lamps, etc. If there is any uncertainty whether an item is included in the sale or not, it is best to be sure that the particular item is mentioned in the purchase agreement as being included or excluded.

Glossary of Mortgage Terms

Adjustable Rate Mortgage Loans (ARM): A mortgage that offers a low interest rate for 1, 3, or 5 years, after which the interest rate adjusts periodically based on a pre-determined index (i.e. *Wall Street Journal* prime rate).

Amortization: The gradual reduction of debt over the term of the loan. Amortization occurs through repayment of principal.

Annual Percentage Rate (APR): The yearly cost of a mortgage including interest and other expenses such as mortgage insurance and points, that are spread over the life of the loan.

Appraisal: A written estimate of a property's current market value.

Closing: The conclusion of your real estate transaction where legal documents are reviewed and funds are disbursed.

Closing Costs: Expenses over and above the cost of the property and can include items such as title insurance, appraisal, processing, underwriting and surveying fees.

Conventional Loan: Loans that are not made under any government-housing program.

Credit Report: A report from an independent agency detailing credit history and previous and current debt to help determine creditworthiness.

Credit Score: A mathematical formula that predicts an applicant's creditworthiness based on credit card history, outstanding debt, type of credit, bankruptcies, late payments, collection judgments, extent of credit history and number of credit lines.

Deed: The legal document that transfers property from one owner to another.

Down Payment: The amount of your home's purchase price that you pay upfront.

Earnest Money: Deposit made by a buyer toward the down payment to show good faith when the purchase agreement is signed.

Equity: The difference between the current market value of a property and the total debt obligations against the property. On a new mortgage, the down payment represents the equity in the property.

FHA Loans: Fixed- or adjustable-rate loans insured by the Federal Housing Administration. FHA loans are designed to make housing more affordable, particularly for first-time home buyers.

Glossary of Mortgage Terms

Good Faith Estimate: Written estimate of the closing costs the borrower will likely have to pay to obtain the loan.

Interest Rate: The percentage rate that a lender charges to borrow money.

Lock or Lock-In: A lender's guarantee of an interest rate for a set period of time. The lock-in protects you against rate increases during that time.

Points (or Discount Points): Points are upfront fees paid to the lender at closing. One point equals one percent of your total loan amount. Points and interest rates are inherently connected. The more points you pay, the lower your interest rate.

Principal: The balance — not counting interest — owed on a loan.

Private Mortgage Insurance (PMI): Insurance to protect the lender in case the borrower defaults on the loan. With conventional loans, PMI is typically not required with a down payment of 20% or more of the home's purchase price.

Term: How many years you have to pay back the loan.

Title: Document that shows ownership of a property.

Title Search: Examination of municipal records to ensure that the seller is the legal owner of a property and that there are no liens or other claims against the property that would prevent a transfer of ownership.

Underwriting: In mortgage lending, the process of determining the risks involved in a particular loan and establishing suitable terms and conditions for the loan.

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