# BECOMING A HOMEOWNER

## The Home Buying Process

Finding and purchasing a home can seem like a daunting task to the first-time buyer. However, learning about the process and being well prepared can make buying a home feel less overwhelming. Many people have done it before, and you can do it too!

**The steps to homeownership**

- Save for down payment and other homebuying costs
- Address credit reports and scores
- Get pre-approved for loan
- Choose real estate agent
- Search for property
- Choose property
- Submit offer
- Offer accepted
- Pre-closing period
- Sign paperwork at closing and receive keys
- Transfer of ownership recorded in public records
- Move into new home

## Saving for Homeownership

The first step to homeownership - saving - should ideally begin well before you purchase a home. There are several things you should save for, including:

- **Down payment:** Most of the money you save will likely go toward this. While a down payment of at least 20% was commonly required in the past, today many lenders will accept less. You may even be able to get a loan that does not require any down payment or a first mortgage to cover 80% and a second mortgage to cover 20%, but these types of loans are not always available. If you do not save anything, you may find it difficult to get a loan.
- **Closing costs:** Closing costs include all of the fees required to execute the home sale. They typically average 3-5% of the home's purchase price. You may have to pay the fees yourself, although sometimes the seller will pay them or you can have them financed (included in the mortgage).
- **Post-purchase reserve funds:** You may need to show the lender that you will have savings left over after you purchase the home, so that the mortgage can be paid even if you are experiencing cash flow problems. This can provide not only assurance to the lender but you as well. For example, if you lose your job, you won't have to take drastic measures to come up with your mortgage payment money. At least three months' worth of mortgage payments is a good amount to have in reserve.
- **Repairs, renovations, and furniture:** If you plan to buy a fixer-upper, a home that does not come with the major appliances included, or you know you will want new furniture (like a $3,000 leather sofa), these costs can be included in your savings plan.

The sooner you start saving, the more money you will have at purchase time. For example, if you put $200 a month in a savings account earning 3% interest for five years, at the end you would have $12,929. If you only saved for one year, you would have $2,433. However, if you would like to purchase a house soon and have saved little or nothing, do not get discouraged. Saving whatever you can is beneficial.

Regularly setting aside money is one way to get the cash you need, but it is not the only one. Many first-time buyers get financial assistance from their parents or other family members, but it is common for lenders to restrict who you can get money from and to require a letter from the giver stating that the money does not need to be repaid. You can also take inventory of your assets to see if anything can be sold for cash, such as a motorcycle or stocks. (Remember, you may have to pay taxes on the profit.) Some people withdraw money from a retirement fund for a down payment, but think carefully before doing this. If you withdraw from a 401(k), not only do you have to pay regular taxes on the withdrawal, but you also have to pay a 10% early withdrawal penalty. You may be able to avoid an early withdrawal penalty if you take the money out of an IRA, but you are still leaving yourself less money for retirement.

**Addressing Credit Reports and Scores**

Importance of your credit score
In order to get a mortgage, especially one with a low interest rate, you usually need to have a strong credit score. The most common scoring model is the FICO score, issued by the company of the same name. Scores range from 300 to 850. Generally speaking, the higher the score, the more likely you are to be approved for financing. Scores are calculated using data from your credit reports, which are compiled by three main bureaus: Equifax, Experian, and TransUnion. A lender may check your scores from all three bureaus or only one. Many lenders require a score of at least 620 to get a mortgage, and those with scores in the mid-700s and above usually get the best interest rates. If your score is lower than 680, you may only qualify for sub-prime loans – which usually have high interest rates – or find it difficult to get any loan.

There are several categories of credit information used to determine your FICO score. Your payment history is extremely important. If you make a late payment, your score will take at hit. The more recent and frequent the late payments are, the lower your score. Having a bankruptcy, repossession, judgment, or collection account can significantly drop your score. Another factor that plays a large role is your level of outstanding debt. Even if you make your payments on time, your score may be low if you carry large balances on revolving debt, like credit cards, particularly if those balances are close to the credit limits. Other factors that have an effect on your score are the length of your credit history (the longer, the better), variety of accounts, and creditor inquiries. As a general rule of thumb, it's a good idea to only apply for the credit you truly need.

Some lenders use other models instead of the FICO score. While the score range and weighting can be different, credit scoring models generally look at the same factors. Making your payments on time and keeping your balances low is always beneficial, regardless of the scoring model used.

**Focusing on your credit score**
If you do not know what your credit scores are, it is a good idea to check them well before you plan to purchase a home. Improving low scores can take time, but don't despair if your scores are not as high as you want them to be. Remember, you can make changes.

Making payments on time will help your credit scores, per information released by FICO. If you have no open accounts with which to establish a positive payment history, consider getting a secured credit card. Secured credits cards are usually the easiest type of credit to get because they require a deposit, which the creditor gets to keep if you do not make payments. If your balances are high on any of your revolving accounts (like credit cards or lines of credit), focus on paying them down and not incurring further debt. Also remember that time is your friend. What has happened in the past two years has more of an impact than what happened before that, and after seven years have passed, most negative information is removed from your credit reports.

If you are purchasing a credit score in preparation for a mortgage loan application, make sure you know which scoring model the lender will be using and purchase that score. For example, if the lender will be using a FICO score, you can purchase a score from www.myfico.com.

**Check for errors before applying**
It is a good idea to check your credit reports from all three credit bureaus at least 60 days before you plan to apply for a mortgage. Even if you think your credit is perfect, know that many reports contain errors. You can get a copy of each credit report free once a year from the Annual Credit Report Request Service. The reports can be accessed online at www.annualcreditreport.com or by calling 877-322-8228. You can only get the reports for free, not the scores. However, if you are just checking your reports for errors, the scores are not necessary. If you see any errors, submit dispute forms online at www.equifax.com, www.experian.com, and www.transunion.com. The credit bureaus will check your claims and correct any errors that were made.

**Non-traditional credit score**
What if you have no credit and, thus, no credit score? You may still be able to get a mortgage. Some lenders will evaluate a non-traditional score, which, as the name implies, uses factors not considered in a traditional score, such as rent, insurance, and utilities payments. You must provide documentation of your on-time payments. If your traditional credit score is low and you want to use a non-traditional score instead, you are usually out of luck. Lenders typically only consider it if you do not have a traditional score, and some do not use it at all. The easiest way to get a mortgage is to build a traditional credit history.

**Getting a Mortgage Loan**

**Getting pre-approval**
It's a good idea to talk to a mortgage lender before searching for a home so that you can get pre-qualified or pre-approved. When you are pre-qualified for a house, the lender gives you an estimate of what mortgage amount you can qualify for. It is not a commitment from the lender to provide financing or a guarantee you can get financing for a particular amount. Getting pre-qualified is a good idea for people who are just starting a home search and want an idea of what they can afford. However, since it is not a guarantee, consider getting pre-approved before making an offer on a home. When you are pre-approved, you get a commitment from the lender to provide a mortgage for up to a certain amount, barring any major changes in your financial situation or problems with the house. You typically have to pay an application fee, and pre-approval only lasts for a certain period of time, usually a few months.

Why get pre-approved before searching, instead of waiting until after you put in an offer to get financing? First, it lets sellers know you are a serious buyer. Many sellers will not consider offers from those without pre-approval. Second, it gives you a limit as to what homes to look at. Why put an offer on a house that requires a $500,000 mortgage if you can only get approved for a $300,000 mortgage? Third, it makes your life easier. You do not have to scramble to get a mortgage or risk losing the home you put an offer on because you could not find financing in time.

**Finding a lender**
Applying at financial institutions where you already have a pre-existing relationship is often a good place to start. Some lenders let you apply for a mortgage online, but as a first-time buyer, you may want to apply in person with a loan officer who can answer questions. Be careful with who you choose. Most lenders are honest and legitimate, but there are some who are not. Predatory lenders tend to target those who do not know their rights or understand the lending process. These individuals or companies use a variety of methods to separate you from your money, including:

- Selling you a home for more than it is worth.
- Falsifying your income, expenses, or assets so you can qualify for a loan.
- Asking you to sign a blank document, saying they will fill in the rest later.
- Adding fees for unnecessary or nonexistent products and services.
- Pressuring you into a risky or unaffordable loan.

If you come across a lender employing these tactics, do not use them!

**Application process**
Lenders consider many factors when deciding whether or not to approve a loan and how much to approve you for. They typically include:

- **Your credit score:** As mentioned before, many lenders require a score of at least 620 for approval and mid-to-high 700s for the best interest rate.
- **The down payment amount and your assets in general:** Most lenders set a maximum allowable loan-to-value ratio, which measures how much of the home purchase can be financed through the mortgage. For example, if a lender sets a 95% loan to value ratio, the loan cannot be for more than 95% of the purchase price of the house, meaning you need a down payment of at least 5% of the purchase price. Aside from the money for the down payment, most lenders like to see that you have additional assets that can be used to pay the mortgage in case of emergencies.
- **Your employment history:** In order to know that you are capable of handling a mortgage, lenders usually want to see a stable employment history, as indicated by at least two years of consistent employment in the same field.
- **Your income:** Traditionally, lenders have required that the mortgage payments, including taxes and insurance, not exceed 28-33% of your gross income. This is called the housing expense or front-end ratio. In recent years, many lenders have raised that ratio. Most lenders also require you to provide two years worth of Form W-2s and/or paystubs to document your employment and income. If you are self-employed, you usually need to provide two years worth of tax returns and balance sheets.
- **Your existing debt (including credit cards and car, personal, and student loans):** Many lenders require that your existing debt payments plus your mortgage payment not exceed 36-38% of your gross income, although some allow a higher percentage. This is called the total debt or back-end ratio.

After collecting the necessary information, the lender will approve your loan or deny it. Many lenders use automatic, computerized systems and can tell you right away if your loan is approved. With other lenders, a person makes the decision, and you may have to wait a few days before hearing back. If your loan is denied, the lender should tell you why. You will probably be disappointed, but use the feedback provided by the lender to make changes. If the loan is approved, the lender will tell you the maximum amount you can borrow and the interest rate. They should also give you a pre-approval letter that can be shown to a seller when making an offer.

Since lenders adjust their interest rates frequently, the interest rate you are told when you are approved will likely not be the same one they use when you close your loan. Many lenders offer the option of locking in the interest rate you are given at approval, although most charge a fee for this service. Locking is only beneficial if the interest rate increases between the time you apply and close, but the direction of interest rate fluctuations can be hard to predict. Think about your own risk tolerance when deciding whether or not to lock in your rate. Within three business days of receiving your loan application, the lender must give you a Loan Estimate, which shows the amount financed (borrowed), total amount that will be paid back over the life of the loan, APR (annual percentage rate, which is the yearly cost of the loan expressed as a percentage), finance charge (total cost of the loan expressed as a dollar amount), total number of payments, amount of payments, late payment policy, and prepayment penalty, if there is any. Be sure to read the statement carefully, and ask for clarification from the lender if you have any questions.

**Types of mortgages**

There are several types of mortgages available. The most common ones are the:

- **Fixed-rate mortgage:** Fixed-rate mortgages come with an interest rate that remains constant over the life of the loan. 30-year mortgages are the most common, but you may also be able to get a 40-year, 20-year, 15-year, or 10-year mortgage. The interest rate is initially higher than for other types of mortgages. However, because the interest rate and payments are fixed, fixed-rate mortgages provide a stability that is appealing to many buyers.
- **Adjustable-rate mortgage (ARM):** Adjustable-rate mortgages have a period of fixed interest, but once that ends, the interest rate and payment adjust at specific intervals. The interest rate is calculated as an index plus a margin. For example, it could be the rate of 12-month US Treasury securities plus 3 percentage points. An ARM can have several caps: an overall cap, which limits how much the interest rate can increase over the life of the loan, a periodic cap, which limits how much the interest rate can increase from one period of adjustment to the next, and a payment cap, which limits the amount the monthly payment can increase at each adjustment.

  In general, the interest rate and monthly payment for an ARM start off lower than for a fixed-rate mortgage of the same amount. However, they often become higher once a few adjustments occur. An ARM may be a good option for people who plan to sell in a few years or expect their income to increase significantly, but it can be risky. Expectations do not always equal reality. Maybe you cannot sell your house because the market has slowed down. Maybe you did not get the promotion you expected. Many people who have taken out ARMs have lost their homes because they were not able to afford the payment increase.
- **Interest-only mortgage:** With an interest-only mortgage, you pay just interest for a specific period of time, usually between 3 and 10 years. Once that period is over, the payment rises to include both principal and interest. Interest-only mortgages typically last for a total of 30 years. The initial payment is lower than for a fixed-rate mortgage of the same amount since you are not paying any principal in the beginning. However, once the interest-only period is over, the monthly payment becomes higher because you are paying down the principal in a shorter period of time. Like with the ARM, there is a risk you will not be able to afford the mortgage once the payments increase.

You do not have to rely on a loan officer to tell you what type of mortgage is right for you. Issues to consider when deciding what mortgage to get include how long you plan to stay in the house, if you expect your income to increase, and what your risk tolerance is.

### Government loans and first-time home buyer programs
Loans offered through federal government programs often come with better terms than conventional loans. The government does not directly loan money; rather, it acts as an insurer, paying your lender if you stop making payments. Lenders must get special approval to be able to offer these loans. The two most popular loan programs are:

- **VA loans:** VA loans are insured by the Veterans Administration and are only available to eligible veterans. No down payment is required.
- **FHA loans:** FHA loans are insured by the Federal Housing Administration, a department of HUD (the U.S. Department of Housing and Urban Development). A down payment of at least 3%-5% of the purchase price is required.

Many states and cities offer programs specifically for first-time home buyers, especially in high-cost areas. The details vary from place to place, but programs generally take one of three forms:

- **Below market rate units:** Some cities require developers to set aside a certain percentage of units to be sold for less than the market rate. For example, a regular one bedroom unit may be sold for $450,000, while the below market rate one is sold at $250,000.
- **Loans:** Like with VA and FHA loans, the state or local government may insure a loan to allow you to get a lower interest rate or other attractive terms.
- **Down payment assistance:** Some programs give you money for a down payment, which usually has to be paid back. However, the repayment terms are normally generous. For example, you may not be charged interest or have to pay back the loan until you sell the house or refinance.

Most first-time home buyer programs set certain income limits, so not all first-time buyers will qualify. To find out about the affordable housing programs offered in your area, ask a lender or call your city or state housing authority. If you are teacher, firefighter, police officer, or other public employee, you may be eligible for special programs.

### Closing costs
Getting a mortgage is not free. Along with the interest you must pay monthly, you usually have to pay fees to close the loan and transfer the home from the seller to you. Theses fees are called closing costs. The lender is required to give you an estimate of the closing costs in the Loan Estimate. Closing costs can include:

- **A loan origination fee:** This is the fee the lender charges for processing and providing your loan.
- **Points:** One point equals one percent of the mortgage amount. By paying a point, you are prepaying mortgage interest to the lender, and they give you a lower interest rate in return. The lender should be able to tell you exactly how much a point will decrease your interest rate.
- **A title search and title insurance:** A title company searches through public records to make sure that the seller is the home's owner and there are no liens against the property. The lender will require you to pay for lender's title insurance, which protects the them against loss in case the title company misses something in their search, but you should also consider purchasing owner's title insurance for your own protection. If there is a lien against the property that is not paid off before you purchase the home, you become responsible for it.
- **An appraisal:** The lender may require an appraisal of the house to ensure that they are not lending you more than its market value.
- **A survey:** A survey confirms the legal, recorded boundaries of the property. This helps avoid conflict, like your neighbor and you fighting over who owns the driveway between your houses.
- A recording fee: This is a fee that is charged to record the transfer of ownership in the county or town records.
- **Mortgage interest:** At closing, you will likely have to pay the interest that will accrue on the mortgage between closing and your first payment date

### Mortgage payment components
Most of your mortgage payment goes toward repaying the mortgage loan. Loan payments can be divided into principal (the amount you borrowed from the lender) and interest (the cost of borrowing money from the lender). With most fixed-rate and adjustable-rate mortgages, early payments go mostly toward paying off interest. As you continue to make payments, a higher percentage goes toward principal. This is called amortization. You are charged interest each month on the amount that is still remaining on the loan, so as the principal is paid down, the interest decreases.

If you have an interest-only mortgage, no principal is paid initially. If you have an option ARM, you are given a few choices for the monthly payment amount. With the minimum payment option, you can pay less than the interest charges. The remaining interest is added to the loan balance, so the principal balance increases instead of decreases. This is called negative amortization. Even if you have the option to pay less than the interest charges, it is rarely a good idea.

Part of your mortgage payment may consist of money that the lender collects on your behalf for property taxes, homeowners insurance, and, in some cases, private mortgage insurance (PMI). PMI protects the lender against loss if the borrower defaults on the loan and may be required for people with less than a 20% down payment. Every month, the lender puts aside the money for these expenses in an escrow account and pays them when they are due. This allows the lender to ensure that these important bills are paid. Together, the principal, interest, tax, and insurance payments are often referred to as PITI.

While many lenders require property taxes and insurance to be put in escrow, not all do. If your lender gives you the option of paying them on your own, think carefully before doing this. Generally, these expenses are only paid once or twice a year. People who choose to pay on their own sometimes find it difficult to put aside the money themselves and are unable to make payments when the bills come.

## Looking for a Home

### Finding a real estate agent

Once you are pre-qualified or pre-approved for a mortgage, you are ready to start your home search. People often wonder whether they should search by themselves or use a real estate agent. Having a real estate agent makes the home buying process easier and can provide you with a valuable resource on housing issues specific to the areas in which you are looking. He or she can find available homes for you, arrange showings, and help you write an offer. Best of all, using a real estate agent is usually free. In most cases, the seller pays the agent, not you.

There are several steps you can take to find a real estate agent you will be happy with:

- **Ask for referrals:** You probably have many friends and relatives who have bought and sold their homes through real estate agents. Make some phone calls and get the names of the agents they had a good experience with.
- **Search by area:** You can find out which real estate agents specialize in the kind of home or area you want by looking in the phone book, searching the web, or reviewing the newspaper's real estate classified ads. You can also drive though your desired neighborhoods and note the names on the "For Sale" signs.
- **Comparison shop:** Talk to several prospective real estate agents and ask questions about the areas and types of homes you are interested in. Do they seem knowledgeable? Is their personality a good fit with yours?
- **Avoid using the seller's real estate agent:** Many people go to open houses by themselves and choose the real estate agent selling the house they put an offer on. This is usually not a good idea. Because the real estate agent is working for you and the seller, he or she is not really able to be an advocate for you.

Some real estate agents ask their clients to sign exclusivity agreements, which say that you will not use another agent, and they must get paid if you purchase a house, even if their services are not used to buy that house. Real estate agents do this to avoid not getting paid for the work they do. However, signing is not necessarily in your best interest because you may wind up not liking the agent or want to purchase a home from a seller who does not pay commission. If the latter is the case, the commission will have to come out of your pocket. You may want to ask the agent to show you houses for a day before signing. If the agent does not listen to you and shows you all the wrong houses, you know not to sign. Also, you can see if the agent is willing to accept a non-exclusive agreement. With this type of agreement, your real estate agent is only entitled to commission if he or she introduces you to the property you purchase.

### Consider what is affordable

An important part of the home search is determining what you can afford. Many people get in over their heads because they buy an expensive house that has all of the features they want. After all, why not splurge and get the house with a pool and huge closets? Just remember that your your first home does not need to be your dream home.

By taking the time to examine your finances and see what you can afford, you can enjoy your home and not have to worry about where the money will come from to pay the mortgage.

If you were pre-approved, you may wonder why you would have to examine your finances since the lender already told you what you could borrow. However, the amount your lender qualifies you for and the amount you can afford are not always the same. Lenders only look at a few factors, namely your income, debt, and down payment. However, you have more expenses than your debt. If you have to pay $1,000 a month in daycare, that reduces the money you have available for your mortgage. By creating a budget (you can use the Budget Worksheet on page 13) that doesn't include your current housing expenses, you can see what you can afford to spend on housing each month. While your income and expenses can change after the home purchase (for example, net income often increases due to the tax benefits of owning a home, and utilities often increase too since houses tend to be larger than apartments), creating a budget gives you a better idea of what you can afford than just basing it on a pre-approval amount.

Keep your housing allowance in mind when searching for a home. Let's say a house that costs $170,000 catches your eye. Your budget shows that you can spend $1,100 a month on housing expenses, and you have a $10,000 down payment. The first step is to calculate what the monthly payments would be for a $160,000 mortgage. You can use an online mortgage calculator.

If you were pre-approved for a mortgage with a 4.25% interest rate, the monthly mortgage payment would be $787. However, you also need to consider non-loan housing costs, like property taxes, homeowners insurance, maintenance, and possibly PMI and/or homeowners association dues. How can you find out what all these costs are before you purchase a home? To find out the property tax rate in your community, call the local property tax office or ask your real estate agent. You can probably get an estimate for what homeowners insurance will cost from an insurance agent. While you cannot know exactly what maintenance will cost until you move in, many experts recommend setting aside 1% of the home's price yearly (for stand-alone homes). Your lender should be able to give you an estimate of what you will pay for PMI, if that is required, and the seller should disclose what the homeowners association dues are, if there are any. Once you have the numbers, you can add everything together and see if the house is affordable.

| **Sample monthly housing payment for a $160,000 house** | |
|---|---|
| Mortgage payment (principal and interest) | $787 |
| Property taxes ($160,000 x 1.2% / 12) | + $160 |
| Homeowners insurance (estimate) | + $75 |
| PMI (estimate) | + $60 |
| Maintenance allowance ($160,000 x 1% / 12) | + $133 |
| Homeowner association dues | + $0 |
| **Total Payment** | **= $1,215** |

As you can see, a $160,000 house would not be affordable based on your budget, so you know to redirect your housing search toward cheaper houses. This process can be time-consuming, but it does not have to be done for every house you look at, only the ones you are seriously interested in.

### Consider other features

While price is one of the most important features of a home, it certainly is not the only one. Your housing search will be more efficient and focused if you think beforehand about what you want. Features to consider include:

- Number of bedrooms
- Number of bathrooms
- Condition of home
- Size
- Parking
- Type of flooring
- Whether or not there is a fireplace
- Type of home (such as single family home or condo)
- Style of home (such as Victorian or Craftsman)
- Layout
- Outdoor space
- Whether or not there is a basement
- Location
- School district
- Safety
- Noise
- Whether unpermitted work was done for repairs or renovations that require a permit, such as additions and extensive plumbing work

Most first-time home buyers' budgets are limited, so you may not be able to get everything you want. Think about what is most important. You may not be able to get granite countertops and hardwood floors, but if you have three children, you probably do not want a one bedroom, one bathroom house!

**Types of homes**
When buying a home, there are several types to choose from. The most common ones are:

- **Single family residence (SFR):** You own the house and the land around it. You are not restricted by any rules, except local laws, and are solely responsible for maintaining the home.
- **Duplex or other multi-unit building:** This is similar to a single family home, but you own more than one legally divided unit. Often people will live in one unit and rent out the other unit(s) or let a family member, like an adult child or elderly parent, live there.
- **Planned unit development (PUD):** You own the house and land directly around it, but the development as a whole is owned by the residents. PUDs generally restrict what you can do to the outside of your house, so you may not be able be able to paint it hot pink, should you desire. Have you ever noticed neighborhoods where all of the houses look the same? Those are often PUDs.
- **Condominium (Condo):** Condos consist of multiple units in one building. You own the interior of your condo (everything inside the walls), and the building as a whole is owned by the homeowners association (HOA), which consists of all of the units' owners. The HOA is responsible for maintaining the physical structure of the building (such as fixing a leaking roof), and you are responsible for maintaining the interior of your unit. You must pay HOA dues and follow the rules they set, called the covenants, conditions, and restrictions (CC&Rs). For example, you may not be allowed to have pets or put hardwood floors in your unit. Many first-time home buyers purchase condos because they usually cost less than single family residences.
- **Townhouse:** Townhouses are similar to condos in that there is a HOA and the units are attached, but with a townhouse you own the complete unit, including the roof, exterior walls and land it directly sits on.
- **Manufactured housing:** Manufactured housing is built in a factory and shipped to the location where it will be placed. Depending on the community, you may own the land underneath the unit or pay to rent a lot. Generally, manufactured housing is less expensive than the above mentioned options.
- **Cooperative (Co-op):** In a co-op, you purchase shares in a corporation that owns property. Purchasing the shares allows you to reside in a unit, but you do not individually own the unit you live in. Many co-ops are limited equity, meaning the price you can sell your shares for is restricted. Like with condos, you have to pay HOA dues and follow the community rules, but co-ops tend to be cheaper than comparable condos. However, in order to purchase in a co-op, you are often required to make a large down payment and be approved by the co-op board, which is not the case for condos. You cannot get a regular mortgage if you purchase a co-op – you must get a share loan, which few lenders offer.

What type of home you should you get? There is no right or wrong answer. Look at your preferences and lifestyle. For example, if you do not like to do maintenance, a condo may be the best option. If you would like your mother to live with you, you may want to look at duplexes.

**The home search**
If you use a real estate agent, he or she can find available houses for you by looking them up on the Multiple Listing Service (MLS). You can also drive around the neighborhoods you are interested in and look for "For Sale" signs. Then your real estate agent can either bring you to open houses for the properties, which are usually on Sunday afternoons, or arrange showings at another time.

If you look at a lot of houses, it can be easy for them to all blend together. Taking pictures and filling out a checklist can help you remember the features of each house. You can use the checklist on pages 14-15. For any home you are considering making an offer on, try to visit it more than once and during different times of the day. This way you will know if, for example, your neighbors are loud at night or the traffic is very heavy during the day. If you work, try doing a test-run commute during rush hour to see how long it takes you to get to work from your potential home. If you see any neighbors outside, ask them how they like neighborhood, or if you are brave, knock on their doors and ask. Your real estate agent should have information on the neighborhood as well.

When searching for a home, try to avoid being distracted by things that are easy to change. A house could have the perfect location and square footage, but you find yourself dwelling on the outdated décor and the color of the walls. Remember, the furniture is not staying with the house, and painting walls is a fairly easy and cheap task. Of course, this does not mean you should ignore major issues, like a hole in the roof or flooded basement.

If you are interested in a condo or other type of development with a homeowners association, it is beneficial to research it. What are the HOA dues? Are they reasonable based on the community and the amenities it has? Look at the bylaws of the community. Can you live with the rules? If you have three dogs, you need to find a community that allows them. Also look at the financial statements of the HOA and minutes from previous meetings. How much does the homeowners associations have in reserves? Those that have little are more likely to face a special assessment if repairs or upgrades are needed. A special assessment is a large, lump sum bill assessed on top of the regular dues to finance a specific renovation or repair. Looking at the notes from past meetings can give you a better sense of the issues the community is dealing with. Are people complaining about graffiti? Does an expensive repair need to be done soon?

**Special circumstances**

In searching for a home, you may run across houses being advertised as short, estate, or foreclosure sales. You may be able to get a good deal on these houses, but they come with special conditions. In a short sale, a seller who is no longer able to pay his or her mortgage is trying to sell the house for less than the amount left on the mortgage. Short sale homes usually come with low price tags, but patience is needed if you are interested in one of these homes. The seller must get your offer approved by the lender. The process can take months, and ultimately the lender may not even approve the sale.

In an estate sale, the executor of the estate is selling the house for the owner after the owner's death. Like with short sales, houses sold through estate sales are usually cheaper. However, estate sale houses are generally sold "as is." When houses are sold as is, that means the seller will not fix any problems in the home before closing.

When a lender forecloses on a home, it is typically sold at a foreclosure auction. Anyone can attend a foreclosure auction and bid, but this is an extremely risky way to buy a home, especially if you are a first-time home buyer. You may not be able to view the house or have it inspected before the auction, and you cannot cancel the deal afterward if the home is not in good condition. Additionally, if the home has any liens on it, in most cases you will inherit those liens. Many auctions are cash-only (meaning you have to pay the bid immediately with cash or a cashier's check). At the very least, you generally will have to make a cash deposit and have mortgage pre-approval.

If there are no other bidders at the foreclosure auction, the house reverts back to the lender, who will most likely try to sell it. Buying a bank-owned home (also called an REO) is less risky than buying a home at auction, and you can still usually get a great deal. Because the seller is an institution, it can sometimes take longer for them to respond to your offer and be ready for closing than if you purchase a home from a normal seller, but the process is often quicker than if you go the short-sale route. Like with estate sales, REOs are typically sold as is.

**Making an offer**

Once you find the house you want to purchase, your real estate agent will prepare an offer. Offers typically have at least three components: the purchase price, the closing date (the date ownership of the house transfers from the seller to you), and how long the offer is good for. Your real estate agent can help you determine an appropriate offering price. He or she will probably look at "comps" – similar houses that have sold in the neighborhood – to help determine a price. Other considerations are how long the house has been on the market and whether there are other buyers making a competing offer. In slow housing markets, where houses have been for sale for months, it is common to offer less than the asking price. Conversely, in hot markets, where it is not unusual for there to be multiple offers on one house, it is common to offer more than the asking price.

When selecting a closing date, think about when you have to move out of your current place. Since closing can be delayed, there should be a buffer between closing and the date you have to move out of your current home. It is not a good idea to select the 29th as the closing date if you need to move out of your apartment by the 30th. You should also consider how long it will take your lender to prepare for closing. Even if you are pre-approved, the lender will not be ready to disburse the mortgage funds the day after your offer is accepted. When you are applying for the mortgage, it is a good idea to ask the loan officer how much time they need.

Many offers have additional components, such as seller concessions, inclusions, and contingencies. Seller concessions are costs the seller pays for the buyer, which reduce the amount of money the seller receives. They can include:

- **Closing costs:** You ask the seller to pay for all or part of the closing costs.
- **Cash back:** You ask the seller to give you cash back to pay for a specific cost, such as repairing the roof or putting in hardwood floors. For example, you got a $350,000 mortgage, and the seller agreed to $5,000 cash back. The lender gives $345,000 to the seller and $5,000 to you. Asking for cash back only makes sense if you have not saved the money to finance the renovations or repairs yourself since you pay interest on cash you receive from the lender. Most lenders limit the amount of cash you can get back and what you can use it for, and some do not allow it at all.
- **Homeowners association dues:** You ask the seller to pay for the homeowners association dues for a specific period of time, such as one or two years.
- **Inclusions refer to what stays in the house.** You should not assume that the seller is leaving the oven or the washer and dryer. If you want the appliances, blinds, chandeliers, or anything else to stay, put it in the offer.
- **Contingencies refer to the conditions that must be met for the sale to go through.** They can include:
- **A home inspection:** Having a home inspection protects you. Would you want to find out the foundation needs $10,000 worth of repairs after you move in? Probably not. The home inspector will go through the house to see if there are any problems and then issue a report describing the findings. If there are any problems, you have a few options: do nothing, ask the seller to fix them before closing, ask the seller for cash back to pay for repairs, ask for a reduction in the sale price, or walk away from the house. If the seller declines your request, you must decide if you want to proceed with the sale. Even if the house is being sold "as is," you can still put in a home inspection contingency. This allows you cancel your offer if there are serious problems or at least know what you need to fix.
- **Financing:** This contingency makes your offer conditional on finding financing for a mortgage. You can add this even if you are pre-approved because pre-approvals are sometimes revoked.
- **An appraisal:** Your lender may require you to include this as a contingency to ensure that the sale price is not overinflated. They may send an appraiser to the house or use a computerized process.
- **Other:** You can put as a contingency anything that was not resolved before the offer was made that may cause you to not want the house. For example, if you put an offer on a condo and have not yet seen the bylaws of the homeowners association, you can make your offer contingent on reviewing that.

Your real estate agent will either send or present the offer to the seller and his or her agent. Along with the offer, it is customary to give the seller earnest money, also called a good faith deposit. Usually the amount is between 1% to 3% of the offered purchase price, but customs vary from place to place. This money is part of the down payment and shows the seller you are serious about purchasing the house. Avoid giving the earnest money directly to the seller because if the deal falls through, he or she may not give it back. If the offer is accepted, the earnest money can go into an escrow account for safekeeping until closing. Escrow accounts can usually be set up with a title company or legal firm. Neither you nor the seller has access to the money until the escrow company releases it to the appropriate party. The seller will accept, counter, or reject your offer. If the seller accepts the offer, the house is taken off the market, and you are in contract (also called entering escrow). Once your offer is accepted, it becomes a binding contract. You cannot simply rescind the offer because later you find another house you like more. The only way to legally cancel the contract is if a contingency is not met. Otherwise, if you walk away from the house, you lose your earnest money deposit.

When sellers counter, usually it is with a higher purchasing price, but they can also counter on the closing date, concessions, inclusions, and contingences. You can accept the counter or respond with your own counter. When buyer and seller are countering, negotiations can sometimes reach an impasse. Often the difference is very small, but neither the seller nor buyer will budge because both want to feel that they dictated the price. It helps to keep things is perspective. The difference between the monthly payment of a 30-year, 6% mortgage of $345,000 vs. $350,000 is only $30 a month. Certainly, though, the difference between what you want and what the seller wants can be fairly large. At some point, you will have to decide if you want to continue negotiating with the seller.

If the seller outright rejects your offer, usually it is because he or she has accepted an offer from another buyer or feels that your offering price is so low that your offer is not serious. If your offer is rejected for the second reason, you can submit another one. Whatever the reason for the seller rejecting the offer, try to not be too disappointed if you do not get the first house you put an offer on. There are likely many houses out there that meet your needs.

## The Pre-Closing Period and Closing

### Pre-closing period

Once your offer is accepted, you can arrange for the home inspection, which should be done by an independent, qualified professional, and either apply for a mortgage if you have not already done so or let your lender know you found a home if you were pre-approved. The lender will start to prepare for closing and may need additional documentation from you, such as proof of homeowners insurance (which needs to be purchased before closing). As mentioned above, an appraisal must be done that meets the lender's specifications. During the escrow period, it is a good idea to periodically check in with the lender and make sure they have everything they need. Otherwise, your closing may be delayed.

Occasionally, buyers who were pre-approved later get their loan denied. For example, you may be denied a loan for a particular house if the appraisal comes in too low. Also, your lender will likely check your credit report right before closing. Your loan may be denied if there have been major changes since you first applied, so avoid charging $15,000 to your credit card! However, if there are no problems, your loan will get final approval, and the lender will be ready to pay out the mortgage funds.

If you are purchasing the home with another person, you will have to decide how to hold the title and then the title company know. There are several ways for two or more people to hold the title, such as:
Tenancy by the entirety: This is only available to married couples. In tenancy by entirety, both ownershave claim to the whole, undivided title. Permissionis needed from both spouses to sell or refinance the property.

Joint tenancy: The title is split in equal shares among the owners, and there is a right of survivorship, meaning if one of the owners dies, his or her share automatically goes to the surviving owners.

Tenancy in common: Ownership of the house can be split by any percentage. For example, you could own 75% percent of the home, while the other titleholder owns 25%. With tenancy in common, there is no right of survivorship, so if you die, your ownership share goes to whomever you left it to in your will.

About a day or so before closing - ideally after the seller has moved out - consider doing a final walkthrough of the property. In the walkthrough, you should make sure the seller left everything he or she agreed to leave and that the property is in the same condition it was before. This is the best time to bring up any problems - such as a stain on the carpet - since the seller has not yet gotten paid. Once closing happens, your options for getting the seller to do something are limited.

### Closing

Closing is the day the mortgage is finalized, and the title of the house is transferred to you. In many states, the closing is handled by the title company. If not, it may be handled by a closing company or attorney. The lender will send its documents and the mortgage funds to the company handling closing, and the title documents needed to record the transfer of ownership in the public records will be prepared. This is usually recorded with the city or county, depending on where you live. Before closing, the title company will also do the title search to make sure the seller is the current legal owner of the home and see if there are any existing liens that must be paid before the seller can receive any money.

Three days before you close you will receive the Closing Disclosure, which lists your actual closing costs. If you do not receive it, ask for it. If your actual closing costs differ significantly from the estimates given in Loan Estimate, ask the lender why.

The closing may take place in the office of the company handling closing, or they may send a notary public to your office or home so you can sign the papers. You and the seller may attend the closing together or separately. You will need to bring photo identification, proof of insurance for the home, and a cashier's check for the amount you are paying for closing costs and the down payment. You are going to sign a lot of paperwork, so be prepared for a sore hand! Do not feel rushed. Make sure you understand everything before signing it. You may want to hire a real estate attorney to accompany you to closing and explain what everything means. The documents you may be signing include the:

- **Mortgage note:** The mortgage note is your promise to pay the lender according to the specified terms.
- **Mortgage or deed of trust:** This gives the lender the right to the title of the home if you do not pay the mortgage.
- **Affidavits:** You may have to sign affidavits confirming particular requirements or facts, such as an affidavit of occupancy confirming you will occupy the home.

After you sign all of the documents, you will receive the keys to your new home. The title or closing company will disburse the funds to the seller and bring the title paperwork to the county or town office to record the transfer of ownership. You are now a homeowner!

### Tax Benefits of Homeownership

Your mortgage payments will probably be higher than what you are paying now for rent, but owning a home can provide a nice tax break. If you itemize your deductions, you can usually deduct some home-related costs, the most common ones being mortgage interest and property taxes. Since deductions lower your taxable income, your tax liability decreases. For example, if your marginal tax rate (the tax rate that is applied to the last dollar you earn) is 25%, paying $3,000 in property taxes and mortgage interest would save you $750 in taxes.

Filling out a new Form W-4, available on the IRS's website at www.irs.gov, allows you to see if you can reduce the amount of taxes being withheld from your paychecks. In order to fill out the form properly, you must know, or at least be able to reasonably estimate, what your property taxes and mortgage interest are for the year. At closing, or soon after, you should receive a form from the tax assessor's office letting you know your property tax rate. To calculate your interest payments for the year, you can use an amortization table.

If you do not adjust your tax withholding you may get a big refund. While a big refund may sound nice, it is not necessarily beneficial. A refund is just the government giving you back excessive money that was withheld from your paychecks, money you essentially loaned to them interest free for the year. It is better to reduce the taxes withheld from your paycheck and increase your net income. You can use the extra money to pay down interest-charging debts, like credit cards and car loans, or put it in a savings account to earn interest. Of course, you should avoid decreasing your withholdings so much that you wind up owing the IRS at the end of the year.

While mortgage interest and property taxes are the most common deductions, you may also be able to deduct other home-related expenses, such as PMI and points. Although points are paid at closing, the IRS generally requires you to deduct them over the life of the loan. In order to deduct the full amount paid for points in the year you close, you must meet several conditions, listed on the IRS's website. If you do not already do so, once you purchase a home, you may want to have your tax return done by a tax specialist to ensure that you are getting all of the deductions you are entitled to and do not claiming anything you are not entitled to.

### Summary

Buying a home involves a lot of work. It is not always easy. However, once you overcome any challenges you may face, you get a big reward: your home!

## BUDGET WORKSHEET

| Monthly Income | Gross | Net |
| --- | --- | --- |
| Job | | |
| Spouse's job | | |
| Part-time job | | |
| Commissions/ bonuses | | |
| Government benefits | | |
| Child support/ alimony | | |
| Other | | |
| Total Income: | | |

| Monthly Expenses | Current | Proposed |
| --- | --- | --- |
| Rent/mortgage | | |
| Second mortgage | | |
| HOA dues | | |
| Property taxes | | |
| Homeowners insurance | | |
| Gas/electric (house) | | |
| Water/sewer/garbage | | |
| Telephone | | |
| Groceries | | |
| Household items | | |
| Health insurance | | |
| Co-pays (medical) | | |
| Car payment #1 | | |
| Car payment #2 | | |
| Gasoline | | |
| Repairs (house) | | |
| Repairs (cars) | | |
| Auto insurance | | |
| Auto registration | | |
| Tolls/parking | | |
| Public transportation | | |
| Daycare/babysitting | | |
| Alimony/child support | | |
| Tuition/lessons | | |
| Student loan payment | | |
| Taxes (payment plan) | | |

| Monthly Expense | Current | Proposed |
| --- | --- | --- |
| Life insurance | | |
| Union dues | | |
| Donations | | |
| Storage fees | | |
| Beauty/barber | | |
| Movies/videos | | |
| Internet access | | |
| Cable/satellite | | |
| Dining out/ snacks | | |
| Sports/hobbies | | |
| Gym membership | | |
| Vacation/travel | | |
| Books/music | | |
| Clothing purchases | | |
| Laundry/dry cleaning | | |
| Pool/hot tub service | | |
| Gardening | | |
| Alarm system | | |
| Gifts/cards | | |
| Pet care | | |
| Cell phone/pager | | |
| Transaction fees | | |
| Postage | | |
| Cigarettes/alcohol | | |
| Savings | | |
| Debt payment | | |
| Debt payment | | |
| Debt payment | | |
| Other: | | |
| Other: | | |
| Other: | | |
| Other: | | |
| Other: | | |
| Other: | | |
| Other: | | |
| Total Expenses: | | |

## HOME SEARCH CHECKLIST

| | | |
|---|---|---|
| Address of property | | |
| Asking price | Square footage | Date of visit |
| Number of bedrooms | Number of bathrooms | Date built |
| Is there a homeowners association? ❑ Yes ❑ No | | HOA dues $ |
| Notes | | |

| **Neighborhood** | Additional Description | Good | Average | Poor | N/A |
|---|---|---|---|---|---|
| Condition of nearby homes/ businesses | | | | | |
| Traffic | | | | | |
| Safety | | | | | |
| Street parking | | | | | |
| School system | | | | | |
| Public transportation | | | | | |
| Proximity to fire department | | | | | |
| Proximity to police station | | | | | |
| Proximity to hospital | | | | | |
| Proximity to work | | | | | |
| Proximity to restaurants/shops | | | | | |
| Proximity to supermarket | | | | | |
| Proximity to recreation/parks | | | | | |
| Other: | | | | | |
| Other: | | | | | |
| Other: | | | | | |
| Other: | | | | | |

| **Common Space** | Additional Description | Good | Average | Poor | N/A |
|---|---|---|---|---|---|
| Lobby | | | | | |
| Hallways | | | | | |
| Laundry room | | | | | |
| Gym | | | | | |
| Pool | | | | | |
| Playground | | | | | |
| Garden | | | | | |
| Other: | | | | | |
| Other: | | | | | |

| **Home** | Additional Description | Good | Average | Poor | N/A |
|---|---|---|---|---|---|
| Layout | | | | | |
| Size of rooms | | | | | |
| Closet space | | | | | |
| Basement | Finished: ☐ Yes ☐ No | | | | |
| Attic | | | | | |
| Fireplace | ☐ Wood ☐ Gas ☐ Decorative | | | | |
| Flooring – living room | Type: | | | | |
| Flooring – kitchen | Type: | | | | |
| Flooring – bedrooms | Type: | | | | |
| Flooring – bathrooms | Type: | | | | |
| Appliances – kitchen | Color: | | | | |
| Appliances – washer and dryer | | | | | |
| Countertops | Type: | | | | |
| Cabinets | | | | | |
| Vanities (bathroom) | | | | | |
| Showers/tubs | | | | | |
| Interior walls condition | | | | | |
| Ceiling height | | | | | |
| Plumbing | | | | | |
| Water pressure | | | | | |
| Electricity | | | | | |
| Cable/internet hook-ups | | | | | |
| Light fixtures | | | | | |
| Air conditioning | | | | | |
| Heat | Type: | | | | |
| Exterior appearance | Style: | | | | |
| Outdoor space | Type: | | | | |
| Fence | | | | | |
| Parking | Type: | | | | |
| Windows | | | | | |
| Roof | Age: | | | | |
| Gutters and downspouts | | | | | |
| Water heater | Age: | | | | |
| Noise level | | | | | |
| Other: | | | | | |
| Other: | | | | | |
| Other: | | | | | |
| Other: | | | | | |

Click here to schedule your Personal Financial Checkup today for helpful guidance and more tips!

Or contact us directly via email:
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