

Buyers' Basics

By Judith Johannsen

Sellers know it, do you? It's a *buyers'* market and that means there are more sellers trying to sell than buyers looking, willing and/or able to buy. So, if you're a buyer, you're in luck and looking for two things – a house to buy and a mortgage loan to buy it with – but, you also probably have questions.

Typically, buyers want to know what the smallest amount of money is they can put down as a deposit, how the amount of their deposit affects their mortgage payment, and if they choose a fixed rate mortgage, will their mortgage payment really remain fixed.

As a matter of common sense, the more money a buyer puts toward a house as a down payment, the lower the amount of mortgage loan he/she will need, so to know how much down payment is appropriate for him/her, a buyer will need to speak with a lender to see how much he/she can and wants to afford to borrow.

There are different types of home loan lenders – there are big banks, small banks, credit unions and mortgage brokers - and each can offer different loan programs, interest rates, fees and closing costs. Interest rates can vary based on the buyer's credit score, the loan to property value ratio, the type of property being bought, the loan's term, and any secondary financing.

The good thing about a home loan is that it is typically repaid over many years, but it is not made up of just the total amount of the loan divided by the number of months. A mortgage loan has four components to it and is described as PITI. First, there is the **p**incipal, which is the amount of money the buyer borrows, and second, there is the **i**nterest, which is the amount of money the lender charges the buyer for the privilege of borrowing the money. The third and fourth parts are the property taxes and the homeowner's insurance, but the amount paid each month is 1/12 of the yearly amount due.

The reason a pro rata portion of taxes and insurance is included in a mortgage payment is so the lender is assured the taxes and insurance are paid on time. A lender has a financial stake in the property and wants to protect its interest and not leave payment of taxes and insurance to a homeowner's whim.

With a fixed rate loan, the amount of each principal and interest payment is constant throughout the life of the loan, with the early payments consisting of mostly interest and the last payments mostly principal. However, because taxes and insurance amounts may change (usually increase), they can cause the PITI mortgage payment to rise slightly each year to reflect those adjustments.

Additionally, if a borrower is making a down payment of less than 20%, a lender may also require mortgage insurance. This is not homeowner's insurance, rather it is insurance to protect the lender's investment in the event the property is foreclosed on and the lender sells it at a loss. The mortgage insurance payments are in addition to the loan's principal, interest, taxes and insurance payments.

Another really good question for a buyer to ask a lender is if the buyer is penalized if he/she chooses to pay off the loan early. If there is a penalty, it is stated in the mortgage document (two examples are 1% of the loan and 6 months' interest) and exists because the lender expects steady repayment of the loan, plus interest, over a period of time, and if a borrower repays the loan earlier than expected, the lender is then deprived of the income it would have received over the life of the loan.

To say that the real estate market has changed and lending policies tightened over the past year is an understatement, but knowing where to go for a home mortgage loan and some basic questions to ask a lender can make the home buying and mortgage loan process easier and friendlier.

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