

UNRAVELING THE MYSTERY OF CLOSING FEES

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You have found the perfect house, your offer has been accepted and you have sailed through the property inspections – so, now you can just wait around for the closing and plan your decorating, right? Well, maybe. In the time between final acceptance of the offer and the closing, a lot of people, bankers, insurance agents, attorneys and even you, the buyer, will be involved in requesting, gathering and verifying information and in preparing for the closing. To the first-time buyer, a real estate closing may seem mysterious and chaotic, but, if done right, all of the various interests are choreographed to come together peacefully in one final event. Furthermore, despite any horror stories you may have heard, most residential closings are routine affairs, with little or no nail biting or bloodletting, successfully completed in about one hour.

Buyers always want to know “the numbers” before the closing. The reality is that it is hard to determine the final numbers with any certainty too far in advance as the various charges to the buyer and seller are continually being calculated, adjusted, checked and rechecked. For a better understanding of closing costs, read on.

Getting and Paying For The Money

While many buyers save up enough money for a healthy down payment on a home, most buyers do not have stacks of cash to plunk down on the closing table for the full purchase price of a home; therefore, nearly everyone finances a home with a loan. If you are a buyer in need of financing, it will be your responsibility to secure a mortgage commitment. How do you do that? Simple. Meet with a lender or meet with many lenders - it can be to your advantage to shop around for the best rate and terms. Meeting with a lender (could be a mortgage broker or the local banker) can be full of curious new terminology like “loan to value” and “income to debt” ratios, “mortgage qualification” and “mortgage commitment”. But, Mr. Buyer, take heart, because aside from learning some new words, a lender will carefully explain, explore and present the different possibilities under which you may borrow. When you receive loan commitment, the lender sets in motion various processes that subsequently oblige the lender to charge what may seem to you as way too many fees, but which are really very standard fees in the industry. Some typical fees include: an application fee, an appraisal fee, a credit report fee, an origination fee, a mortgage insurance application fee (if the mortgage amount exceeds 80% of the fair market value of the property), a commitment fee, a processing fee and a document preparation fee.

Another cost linked to borrowing funds is prepaid interest. Huh?, you say. To explain, you first need to understand that mortgage interest is collected in arrears, or, put another way, the interest included in the mortgage payment you pay towards next month’s mortgage payment actually covers last month’s interest. So, as the first mortgage payment typically is not due until the first day of the *second* month following the closing, the prepaid interest is interest on the money you are borrowing from the date of the closing until your first mortgage payment.

Everyday Expenses - Adjustments

Everyday expenses, the routine costs, other than the cost of borrowing money attendant to owning a home, are adjusted as of the closing date, and apportion the payments fairly and accurately between the buyer and the seller. Such expenses include city or town taxes, fire district taxes, water assessment, sewer assessment, heating fuel, tenant rental payments, if any, and common expense assessments for dwellings in common interest communities. Some of these are pay-as-you-go expenses, some are paid ahead and some are paid in arrears. For example, if the seller paid in June for property taxes for July

through December and the closing is August 1, the seller would have paid ahead for property tax on property he no longer owns (August 2 – December 31). The settlement statement, then, would reflect a credit to the seller for that August 2 through December 31 period.

Insurance

Before a lender will consent to close a homebuyer's loan, it will need assurance that its investment (the loan) is protected. This assurance comes in the form of two types of insurance – homeowner's insurance and title insurance. The buyer/borrower provides proof of the homeowner's insurance by either a certificate of insurance or a binder and is available upon payment of the insurance premium. At closing, the homeowner's insurance policy premium may be listed as "POC" on the settlement sheet, signifying that the premium for the policy was Paid Outside of Closing and, therefore, not listed as a charge to the buyer. The buyer/borrower also must provide proof of title insurance with either a lender's policy, known as the Mortgagee Policy, or an Owner Policy. At closing, the fee for the title insurance is reflected on the settlement statement as a debit to the buyer.

Escrows – Taxes and Insurance

Where a buyer's mortgage payment includes principal, interest, taxes and insurance ("PITI"), lenders apply the appropriate amounts to the outstanding principal and interest and escrow accounts to fund the periodic tax and insurance payments. While the Buyer may be accustomed to paying for these items separately, many lenders prefer to collect, hold and disburse the taxes and insurance payments, thereby guaranteeing payment and protecting their investment. The amount of escrow at closing for hazard insurance is usually equal to two month's premiums as the buyer will make only ten monthly insurance contributions before the next yearly premium is due. (Remember, the first mortgage payment is typically not due until the first day of the second month following the closing). The amount of escrow for taxes is normally 1/12 of the year's total taxes, taking into account when the next tax payment is due, how many months of taxes are to be included in the next tax payment, how many months of reserve are needed to make that payment, how many mortgage payments will be made between closing and the next tax payment date, and, how many contributions will be needed to make the payment.

Attorney's Fees

Legal representation is another fee related to the closing of title on the settlement statement. There may be several attorneys involved in the closing with the number of attorneys dependent upon how many interests choose to be represented. A seller may require an attorney to prepare the deed and the other necessary closing documentation and a lender will require an attorney to prepare and/or review the gazillions of loan documents required for the buyer to sign. It is important to note that a lender's attorney represents only the lender's interests and not necessarily those of the buyer/borrower; therefore, a buyer may choose to have an attorney represent its interests, apart from those of the lender.

Recording Fees

The buyer will want to record the deed it receives on the land records in the town in which the property is located to provide notice that the buyer is the owner of that particular piece of property. Recording fees are set by statute and are \$10.00 for the first page of a document, \$5.00 for each subsequent page, plus \$3.00 for restoration, preservation and management of historical documents. The seller must pay conveyance taxes (based on the purchase price) to the municipality and to the state as well as a release of any mortgage satisfied at closing.

Miscellaneous Fees

Lastly, there may be miscellaneous fees incurred on behalf of the buyer and seller such as overnight mail or courier service incurred in preparation for the closing that have nothing to do with the financing or the adjustment of closing costs, but which have everything to do with pulling together a successful transaction.

Real estate closings mean different things to different people. For a buyer, it means owning a home; for a seller, it means moving on; for a lender, it means making money on generating and providing a loan; for the insurance companies, it means creating revenue by insuring against reasonable risks; and for the broker(s), it means a paycheck. Sure, a buyer can expect to jump through some hoops and pay routine closing fees, but the payoff is huge - home ownership. For the new homeowner, a real estate closing should not be a mysterious and scary thing. Not knowing what to expect with respect to closing charges and fees could leave a buyer feeling as if he had been nibbled to death by ducks. A basic understanding of the closing costs before arriving at the closing table goes a long way to allaying fears and trepidation. So, if a buyer has questions along the way, there are plenty of people – real estate agents, attorneys and lenders - who will gladly provide answers, explanations and guidance. Just ask.