

Student Take Home Guide

Money Smart

Your Own Home



FEDERAL CREDIT UNION

Table of Contents

Table of Contents	1
Money Smart	2
Your Own Home	3
Am I Ready to Buy a Home?	4
Components of a Mortgage Loan Payment	5
How Much Mortgage Can I Afford?.....	6
Mortgage Options	7
Mortgage Shopping Worksheet	8
Homebuyer Assistance Programs.....	10
Glossary	13
For Further Information.....	17
Acknowledgements	18
Course Evaluation – Your Own Home	19
What Do You Know – Your Own Home	20

Money Smart

The *Money Smart* curriculum is brought to you by the National Association of Federal Credit Unions (NAFCU). *Money Smart* is adapted from a curriculum developed by the Federal Deposit Insurance Corporation (FDIC). The *Money Smart* Program includes the following courses:

- **Credit Unions: Here To Serve You**
an introduction to consumer financial services
- **Borrowing Basics**
an introduction to credit
- **Check It Out**
how to choose and keep a checking account
- **Money Matters**
how to keep track of your money
- **Pay Yourself First**
why you should save, save, save
- **Keep It Safe**
your rights as a consumer
- **To Your Credit**
how your credit history will affect your credit future
- **Charge It Right**
how to make a credit card work for you
- **Loan to Own**
know what you're borrowing before you buy
- **Your Own Home**
what homeownership is all about

Your Own Home

Welcome to Your Own Home! Owning your home is a major step, and one that can lead to financial security. There are many benefits to owning your own home. There are also a number of challenges.

When you have completed this course you will know more about the process of getting homeownership financing.

Am I Ready to Buy a Home?

Use these questions to help you decide if you are ready to buy a home:

- Do I have a steady source of income?
- Have I been employed on a regular basis for 2-3 years?
- Is my income reliable?
- Do I have a credit history?
- Do I have a good record of paying bills?
- Am I able to pay my bills and other debts?
- Do I have the ability to make the mortgage payment every month plus handle additional costs for taxes, insurance, maintenance, and repairs?
- Do I have money saved for a downpayment and closing costs?

If you answer yes to these questions, you might be ready to buy a home. If you answer no to any of them, concentrate on strengthening those areas.

Components of a Mortgage Loan Payment

Your mortgage payment (PITI) will reflect the following costs:

- P = Principal. The amount applied to the outstanding balance of the loan.
- I = Interest. The amount of the charge for borrowing money.
- T = Taxes. $1/12^{\text{th}}$ of the estimated annual real estate taxes on the home.
- I = Insurance. $1/12^{\text{th}}$ of the annual homeowner's insurance premium. This figure will include flood insurance and private mortgage insurance (PMI) if required.

You will most likely pay the taxes and insurance along with the principal and interest to the lender every month. In some cases, however, the lender may allow you the option to pay the taxes and insurance separately.

If the lender requires you to pay the taxes and insurance as part of your mortgage payment, the lender will open an escrow account to hold this money until the payments are due. Many people consider this convenient because they don't have to make separate payments. If you live in certain states, the escrow account may also earn interest.

How Much Mortgage Can I Afford?

Keep in mind that just because you qualify for that amount, it does not mean you can afford or be comfortable with those monthly payments. You need to consider your particular circumstances and your future financial needs and goals.

As a rule of thumb, many people estimate they are able to afford a mortgage of 2 or 2 ½ time their household income. For example, if your annual income is \$30,000, you might be able to afford a mortgage of \$60,000 to \$75,000:

$$\mathbf{\$30,000 \times 2 = \$60,000}$$

$$\mathbf{\$30,000 \times 2.5 = \$75,000}$$

Lenders look at debt-to-income (DTI) ratios when they consider your application for a mortgage loan. A DTI ratio is your monthly expenses compared to your monthly gross income.

Lenders consider monthly housing expenses as a percentage of income and total monthly debt as a percentage of income. Both ratios are important factors in determining whether the lender will make the loan.

Lenders usually require the PITI (principal, interest, taxes, and insurance), or your housing expenses, to be less than or equal to 25% to 28% of monthly gross income is \$2,500, or \$30,000 annually, your mortgage payment should be \$700 or less:

$$\mathbf{\$2,500 \times 28\% = \$700 - \text{maximum monthly housing costs}}$$

Lenders usually require housing expenses plus long-term debt to be less than or equal to 33% to 36% of monthly gross income. Lenders call this the “back-end” ratio. In other words, if your monthly gross income is \$2,500, the combination of your mortgage, \$700, and other long-term debt should be no more than \$900:

$$\mathbf{\$2,500 \times 36\% = \$900 - \text{maximum total debt}}$$

If your debt-to-income exceeds these ratios, talk to your lender about your options.

Mortgage Options

15-Year Mortgage	30-Year Mortgage
Lower interest rate	Higher interest rate
Build equity faster	Build equity slower
Less interest to pay	Can deduct more interest from income tax
Larger monthly payment	Lower monthly payment

Fixed Rate	Variable Rate
Interest rate stays the same for the term of the loan	Interest rate can increase or decrease during the term of the loan
Interest rates could go down while you are locked into your mortgage at a higher than market rate	You might have a low rate for an initial period of one, three, five, seven, or ten years
	Monthly payments can be lower than fixed rate loans

Mortgage Shopping Worksheet

<i>Name of Lender</i> <i>Name of Contact</i> <i>Date of Contact</i> <i>Mortgage Amount</i>	Lender 1		Lender 2	
A. Basic Information about the loan	Mortgage 1	Mortgage 2	Mortgage 1	Mortgage 2
◆ Type of Loan: Fixed rate, variable rate, conventional, FHA, other?				
◆ Minimum down payment requirement				
◆ Loan term (length of loan)				
◆ Contract interest rate				
◆ Annual Percentage Rate (APR)				
◆ Points (may be called discount points)				
◆ Monthly PMI payments (mortgage insurance)				
◆ How long must you keep PMI?				
◆ Estimated monthly escrow for taxes and insurance				
◆ Estimated monthly payment (Principal, Interest, Taxes, Insurance, PMI)				
B. FEES – different lenders have different names for similar fees. Listed below are some of the typical fees you may see on loan documents				
◆ Application or loan processing fee				
◆ Origination or underwriting fee				
◆ Lender fee or funding fee				
◆ Appraisal fee				
◆ Attorney fees				
◆ Document preparation and recording fees				
◆ Broker fees (may be quoted as points, origination fees, or interest rate add-on)				
◆ Credit report fee				
◆ Other fees				
C. Other Costs at Closing/Settlement				
◆ Title Search/Title Insurance For Lender For You				
◆ Estimated prepaid amounts for interest, taxes, hazard insurance, payments for escrow				
◆ State and local taxes, stamp taxes, transfer taxes				
◆ Flood determination				
◆ Prepaid PMI				
◆ Surveys and home inspections				
D. Total Fees and other closing/settlement cost estimates				

	Lender 1		Lender 2	
<i>Name of Lender</i>				
E. Other Questions and Considerations about the loan	Mortgage 1	Mortgage 2	Mortgage 1	Mortgage2
❶ Can any of the fees or costs be waived?				
Prepayment Penalties				
❶ Is there a prepayment penalty?				
❶ If so, how much is it?				
❶ How long does the penalty period last? (3yrs? 5yrs?)				
❶ Are extra principal payments allowed?				
Lock-ins				
❶ Is the lock-in agreement in writing?				
❶ Is there a fee to lock-in?				
❶ When does the lock-in occur – at application, approval or another time?				
❶ How long will the lock-in last?				
❶ When the rate drops before closing, can you lock-in at a lower rate?				
If the loan is an adjustable rate mortgage:				
❶ What is the initial rate?				
❶ What is the maximum the rate could be next year?				
❶ What are the rate and payment caps each year and over the life of the loan?				
❶ What is the frequency of rate change and any changes to the monthly payment?				
❶ What is the index the lender will use?				
❶ What margin will the lender add to the index?				
Credit Life Insurance				
❶ Does the monthly amount quoted to you include a charge for credit life insurance?				
❶ If so, does the lender require credit life insurance as a condition of the loan?				
❶ How much does the credit life insurance cost?				
❶ How much lower would your monthly payment be without the credit life insurance?				
❶ If the lender does not require credit life insurance, and you still want to buy it, what rates can you get from other insurance providers?				

Homebuyer Assistance Programs

There are a number of different programs available for first-time homebuyers. Many people start the homebuying process with one of these programs or with a program offered by local community organizations.

Federal Housing Administration (FHA) Insured Loans

The 203(b) is the most common FHA loan featuring:

- Low downpayment
- Flexible qualifying guidelines
- Limited lender fees
- Maximum loan amounts

Department of Veterans Administration (VA) Insured Loans

Features of VA loans include:

- You must be an eligible veteran
- There are no downpayment requirements
- Competitive and negotiable fixed interest rates
- Limitations on closing costs
- Longer payment terms

Federal National Mortgage Association (FNMA) Loans

The FNMA Community Homebuyers Program features:

- 5% downpayment
- Expanded debt-to-income ratios (33% and 38%)
- You must attend homebuyer education
- You must earn no more than the median income for the area in which you live
- One family principal residence

The Fannie 97 features include:

- Fixed rate
- 3% downpayment
- Expanded debt-to-income ratios (33% and 38%)
- You must attend homebuyer education
- You must earn no more than the median income for the area in which you live
- You must have saved money for one month advance payment in an account at closing

The Flexible 97 features include:

- You must have very good credit
- 15-, 20-, 25-, 30-year terms
- 3% downpayment can be a gift or a grant from nonprofit or government agency
- No borrower income limits or property location restrictions
- Upfront mortgage insurance costs are lower than FHA loans

The Fannie 3/2 features include:

- Fixed rate
- 15- or 30-year term
- 5% downpayment—3% from your own resources, 2% from a government agency, nonprofit organization, employer, or private foundation
- Expanded debt-to-income ratios (33% and 38%)
- You must attend homebuyer education
- You must earn no more than the median income for the area in which you live

The 502 Rural Housing Direct Loan is offered only in rural areas. Features include:

- You must have low income—between 50% and 80% of the median income for the area in which you live
- The loan can be financed at 100%
- Payments are usually 22% to 26% of your income
- You must not be able to obtain financing elsewhere

502 Single Family Housing Loan Guarantee features:

- You can earn up to 115% of the median income for the area in which you live
- You must be without adequate housing
- You must be able to afford the payments
- You must not be able to obtain credit elsewhere
- 30-year term
- No downpayment

502 Mutual Self-Help Housing Loans:

- Primarily used to help low and very low income households construct their own homes
- Intended for families unable to buy clean, safe housing through conventional methods
- Families must perform at least 65% of construction labor on each other's homes under qualified supervision
- You must be able to make payments
- Payments are usually 22% to 26% of your income
- 33- or 38-year terms
- No downpayment

Glossary

Annual Percentage Rate (APR)

The APR is a measure of the cost of your loan expressed as a yearly percentage rate, such as 6% or 8%.

Asset

An asset is anything owned by a person or organization having monetary value.

Balloon Mortgage

A balloon mortgage is a large payment at the end of your loan term. This is often after a series of low monthly payments. A balloon mortgage generally offers very low rates for an initial period of time (usually 5, 7, or 10 years). After the period ends the entire balance is due. Many borrowers pay the balance by refinancing their mortgage.

Broker

A mortgage broker helps a prospective borrower shop around for the best rate and terms in obtaining mortgage financing.

Caps

Caps are provisions of an adjustable rate mortgage, which limit how much the interest rate can change at each adjustment period or over the life of the loan. A payment cap limits how much the payment due on the loan can increase or decrease.

Closing Costs

Closing costs are various charges associated with the transfer of property. The lender must disclose these costs to you.

Compensating Factors

Compensating factors are favorable factors that might outweigh the negative factors. For example, a borrower has high ratios, but he or she balances this with a good credit history and extra cash in a savings account.

Condominium

A condominium is an apartment building or multiple-unit housing area in which the living units are owned individually.

Conventional Loan

A conventional loan is a mortgage that is not guaranteed, insured, or made by the federal government.

Debt-to-Income Ratio (DTI)

DTI is the ration of monthly debt payments to monthly gross income. Lenders use DTI ratio to determine whether a borrower's income qualifies him or her for a mortgage.

Downpayment

The downpayment is the portion of the home's purchase price the buyer pays in cash.

Duplex

A duplex is a house divided into two living areas.

Finance Charge

The finance charge is the dollar amount the credit will cost you.

Fixed Rate Loan

A fixed rate loan has an interest rate and payment amount that stays the same throughout the term of the loan.

Good Faith Estimate of Settlement Costs (GFE)

When you apply for a loan, the Real Estate Settlement Procedures Act (RESPA) requires that the lender or mortgage broker give you a GFE of the settlement service charges you will likely have to pay.

Government Mortgages

A government mortgage is insured by HUD through the Federal Housing Administration (FHA) or guaranteed by the Department of Veteran's Affairs or the Rural Housing Service.

HUD-1 Settlement Statement

A HUD settlement statement is a summary of all the costs paid by the buyer and seller in a mortgage transaction.

Index

The index is a base interest rate used to calculate the interest rate that will be charged on a variable rate loan. The rate you will pay on a variable rate loan is usually a set percentage above the base rate, or the index.

Individual Development Account (IDA)

An IDA is a matched savings account. When an account is matched it means that another organization, such as a foundation, corporation, or government entity, agrees to add money to your account.

Interest

Interest is the charge for borrowing money.

Lien

A lien is a legal claim on the home that secures the promise to repay the debt.

Loan Origination Fees/Underwriting Fees

These are fees charged by the lender for processing or evaluating the loan application and are often expressed as a percentage of the loan amount.

Loan to Value (LTV)

LTV is the amount of money you borrow compared to the price of the property you are buying.

Mortgage

A mortgage is a legal document where the borrower pledges property to the lender to ensure payment of a loan.

Principal, Interest, Taxes, and Insurance (PITI)

PITI are the factors included in the standard mortgage payment.

Point

A point is the amount equal to one percent of the loan amount. It is a fee paid to the broker or lender for the loan, often linked to the interest rate.

Principal

The principal is the loan amount borrowed or still remaining on the loan.

Private Mortgage Insurance (PMI)

PMI is mortgage insurance issued by private insurers that protects the lender against loss in the event the borrower defaults on a mortgage with a downpayment of less than 20%.

Rate Lock

A rate lock is the time period, usually 30-60 days, that a mortgage lender agrees to hold the mortgage rate and points payable by the borrower to the rate quoted by the lender on a given day.

Real Estate Agent

A real estate professional who helps people buy and sell property.

Settlement Costs/Closing Costs

Fees associated with the transfer of property to a purchaser and recording the mortgage line on the property deed by the credit union or bank that is financing the transaction. These costs may include fees for application, title examination, abstract of title, title insurance, and property survey; fees for preparing deeds, mortgages, and settlement documents; attorney's fees; recording fees; and notary, appraisal, and credit report fees.

Title

The title indicates the right of ownership in the property.

Title Insurance

Title insurance protects the buyer and lender against losses arising from disputes over the ownership of the property.

Townhouse

A townhouse is one of a row of houses connected by common side walls.

Variable Rate Loan

A variable rate loan has an interest rate that might change during any period of the loan as written in the contract (loan agreement). Variable rate mortgages are often referred as adjustable rate mortgages (ARMs).

For Further Information

National Credit Union Administration

1775 Duke Street
Alexandria, VA 22314
1-703-518-6300

www.ncua.gov

Federal Deposit Insurance Corporation (FDIC)

Division of Compliance and Consumer Affairs
550 17th Street, NW

Washington, DC 20429
1-877-ASK-FDIC (877-275-3342)

Email: consumer@fdic.gov

www.fdic.gov

Department of Housing and Urban Development (HUD)

Office of Fair Housing and Equal Opportunity

451 Seventh Street, SW, Room 5100

Washington, DC 20410

202-708-4252

1-800-669-9777

www.hud.gov

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- *Consumer Action Handbook*, 2001, Federal Consumer Information Center, United States General Services Administration
- Fannie Mae
- *Gateway to a Better Life—Making Every Dollar Count*, 1998, Cooperative Extension, University of California
- *Helping People in Your Community Understand Basic Financial Services*, Financial Services Education Coalition
- Internal Revenue Service
- *Saving Fitness A Guide to Your Money and Your Financial Future*, U.S. Department of Labor, Pension, and Welfare Benefits Administration
- Social Security Administration
- United States Department of Agriculture, Rural Development, Rural Housing Service
- United States Department of Housing and Urban Development
- United States Veterans Administration, Department of Veterans Affairs Home Loan Program

Course Evaluation – Your Own Home

Instructor: _____ Date: _____

Thank you for your participation in this course. Your responses will help us improve the training for future participants. Please circle the number that shows how much you agree with each statement. Then answer the questions at the bottom of this form. If you have any questions, please feel free to ask your instructor.

	Strongly Disagree	Disagree	Agree	Strongly Agree
1. The course was interesting and kept my attention.	1	2	3	4
2. The examples in the course were clear and helpful.	1	2	3	4
3. The activities in the course helped me understand the information.	1	2	3	4
4. The slides were clear and easy to follow.	1	2	3	4
5. The take-home materials were easy to read and useful to me.	1	2	3	4
6. The instructor presented the information clearly and understandably.	1	2	3	4
7. The information/skill taught in the course is useful to me.	1	2	3	4
8. I am confident that I can use the information/skill on my own.	1	2	3	4
9. I am satisfied with what I learned from this course.	1	2	3	4

What was the most helpful part of this course?

What was the least helpful part of this course?

Would you recommend this course to others?

Any comments/suggestions?

What Do You Know – Your Own Home

Instructor: _____ Date: _____

This form will allow you and the instructors to see what you know about your rights and responsibilities as a consumer of financial products and services both before and after the class. Read each statement below. Please circle the number that shows how much you agree with each statement.

<i>I know:</i>	Before-the-Course				After-the-Course			
	Strongly Disagree	Disagree	Agree	Strongly Agree	Strongly Disagree	Disagree	Agree	Strongly Agree
1. The benefits and disadvantages of homeownership	1	2	3	4	1	2	3	4
2. Questions to determine my readiness to buy a home	1	2	3	4	1	2	3	4
3. Different mortgage programs	1	2	3	4	1	2	3	4
4. Basic terms used in a mortgage transaction	1	2	3	4	1	2	3	4