



# Homebuyer Guide

Presented by:



*Real People ★ Real Service ★ Real Simple*

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# The basics

## What is a mortgage?

A mortgage is a loan secured by real estate. You borrow money to buy a home and promise to pay it back over a specified period, for a specified cost. Repayment typically happens through monthly mortgage payments. If you stop repaying the loan, your lender may take ownership of the property.

## What does my mortgage payment include?

A mortgage payment consists of principal and interest. If you make less than a 20% down payment, your mortgage payment will include principal, interest and mortgage insurance if applicable. In addition, you will be required to make payments of your homeowners insurance, property taxes and association dues to your lender on a monthly basis to be placed in an escrow account, in addition to other required expenses that may apply. Your lender will then pay those third parties from the escrow account funds.

- The principal part of your payment reduces the original amount you borrowed.
- The interest part covers the fee to borrow the amount you still owe.
- The taxes and homeowners insurance parts are collected and held in an escrow account to pay your property tax and homeowners insurance on your behalf as they come due. If mortgage insurance is applicable to your loan, that part of your payment is forwarded to the agency that is providing the insurance.

**Note:** Use of an escrow account to pay for taxes and insurance is an option, as long as you have at least 20% for down payment. If you choose this option, or you have less than a 20% down payment, your monthly payment to your lender will include property tax and homeowners insurance.

## What does “amortize” mean?

Amortize means the process of paying off a debt by regularly scheduled payments that include both principal and interest. In the early stages of your mortgage term, your mortgage payment is mostly interest and only a small portion pays down your principal. As you continue making payments through the years, and because the principal balance is reduced, a smaller portion of each payment is interest and a larger portion of your payment goes toward reducing principal until your entire loan is repaid.

## What is homeowners insurance?

Homeowners insurance provides financial protection in the event of losses that are the result of fire, wind, natural disasters or other hazards. Most mortgage lenders require you to have a homeowners insurance policy.

## What is mortgage insurance?

Mortgage insurance (MI) protects the lender against financial loss if a customer fails to repay the loan. It is usually required when your down payment is less than 20% of the home’s purchase price.

- FHA-insured loans require a mortgage insurance premium (MIP)
- VA loans require a funding fee
- Conventional loans can be insured with private mortgage insurance (PMI)

## What are closing costs?

In addition to the sales price of the home, you’ll need to pay for the services of various real estate and lending related professionals who are required to complete a purchase transaction. Depending on your lender, the mortgage you chose, and the location of the home, these “closing costs” can add up to several thousands of dollars. You’ll get a better idea of the amount soon after you apply.

### What is Annual Percentage Rate (APR)?

The APR shows the costs of your mortgage loan as a yearly rate. The APR includes up-front fees (such as points) as well as interest and is intended to show you the true cost of your loan. When comparing one loan to another, be sure to compare APR's to get a true picture of what each one will cost you.

### What is Debt-to-income (DTI) Ratio?

There are two debt-to-income ratios that are used to determine your maximum loan amount:

- **Housing Ratio (or front-end ratio)** is the percentage of your gross monthly income that is dedicated to paying your monthly mortgage-related expenses (principal and interest, property taxes, homeowner's insurance, mortgage insurance.)
- **Total Debt Ratio (or back-end ratio)** determines the percentage of your gross monthly income that is used to pay your combined monthly debts (mortgage-related expenses, credit cards, car loans, student loans, child support, etc.) Generally, this ratio should be 48% or lower.

### What is Equity?

Equity is the portion of the property that you actually own through your payments, versus the portion that you still owe the mortgage lender. The longer you stay in your house, the more equity you will have.

### What is Escrow?

An account set up on your behalf in which a portion of your monthly payment is held to pay property taxes and insurance.

### What is Gross Income?

Amount earned before taxes or types of payroll deductions. Gross income includes overtime, commissions, dividends and any other sources for which a steady history can be shown.

### What is Loan-to-value (LTV) Ratio?

The ratio of a loan to the value of the asset purchased. If you have a higher down payment, you would have a lower LTV ratio. This factors into whether or not a lender will require someone to get mortgage insurance.

### What are points?

Percentage points of the loan amount. Often in order to get a lower interest rate, lenders will allow borrowers to lower the rate by paying points upfront.

### What is "Locking In" a Rate?

Interest rates fluctuate everyday. Locking In a rate guarantees you will receive that interest rate for the duration of the lock period.

## What other costs should be considered?

While homeowners don't have to pay rent, they do have to manage expenses — beyond mortgage payments — that renters never face.

- **Maintenance:** It can be costly to keep a property in top condition. This is particularly true of older homes, where system and appliance warranties may have expired. Home warranty plans provide repair or replacement coverage for certain built-in appliances and major home systems for a specific length of time. They cost a few hundred dollars a year, depending on the size of your mortgage and where you live.
- **Taxes:** Most communities finance schools and other services through property taxes. Tax rates vary from town to town, so ask your real estate agent about taxes in your area. The good news is: whether you pay them directly, or through the tax portion of your mortgage payment, property taxes are usually fully deductible at income tax time. Consult your tax advisor for details.
- **Association dues:** Condominiums and planned unit developments (PUDs) often have homeowners associations that can charge fees as high as several hundred dollars a month. These may be included as part of your mortgage payment. If not, you'll need to budget for them.

## How do I know how much money I can borrow to buy a home?

Your lender can help you get a preapproval that states the maximum loan amount you can borrow. Add your preapproved maximum loan amount to the amount you plan to use for your down payment, and you will know your home purchase price range.

## How do lenders determine if a customer qualifies for a mortgage?

Lenders look at your credit score, the cash you have available for a down payment and closing costs, your income, and your existing debt and financial obligations.

## Two ratio guidelines are used.

- **The housing expense-to-income ratio (or front-end ratio)** compares your anticipated monthly mortgage payment to your total household gross monthly income (pre-taxed).
- **The debt-to-income ratio (or back-end ratio)** compares your anticipated monthly mortgage payment to your gross (pre-taxed) monthly earnings and your monthly debt requirements. Monthly debt includes credit cards, car loans, student loans, consumer loans plus other financial obligations such as child support and alimony.

## What is a credit score?

The three credit reporting agencies — Experian, TransUnion and Equifax are clearinghouses for information on the credit rating of individuals and firms. Credit score is a term often used to refer to credit bureau risk scores. It broadly refers to a number generated by a statistical model which is used to objectively evaluate information that pertains to making a credit decision (i.e. credit cards, car loans, student loans, etc.) that includes:

- Your payment history
- The total amount you owe
- The amount of time you've had available credit
- Whether you have any judgments entered against you
- Whether you filed bankruptcy
- The number of times potential lenders have reviewed your credit

Information in the agencies' reports is evaluated and interpreted into a "credit score," which help lenders make loan decisions. Credit scores range from 350 to 850, and yours may determine whether you are approved for a loan, the terms of the loan, and the interest rate.

**Note:** Making large purchases with a consumer loan or credit card just before applying for a mortgage may impact your ability to qualify. So consider your needs and priorities carefully.

## What can I do to manage my credit score?

Lenders look at your credit score, the cash you have available for a down payment and closing costs, your income, and your existing debt and financial obligations.

- **Pay down revolving debt.** Don't move debt around between credit cards.
- **Make bill paying automatic.** Set up electronic withdrawals from your checking or savings accounts to help you make timely bill payments.
- **Don't open a lot of new accounts.** Instead, hang on to and maintain your older accounts.
- **Contact your creditors if you are having trouble.** Most creditors are willing to work out a payment schedule rather than see you fall delinquent and not pay at all.

## What is the difference between a government loan and a conventional loan?

- A government loan is a mortgage product whose requirements are established by a government agency such as the Federal Housing Administration (FHA) or U.S. Department of Veteran's Affairs (VA). Government loans typically have lower down payment requirements than conventional loans. Be certain to ask your home mortgage consultant to help you compare the overall costs of all products, including the monthly and long-term costs and conditions of any required mortgage insurance. In many instances, you may find FHA to be a more expensive financing option and should only be considered after thoroughly evaluating all other product options that meet your credit qualifying and financial needs.
- A conventional loan is a non-government loan and is the most common kind of mortgage product. There are "conforming" and "non-conforming" categories, and conventional loans usually require a down payment.

## What is the difference between a conforming mortgage and a non-conforming mortgage?

- A conventional conforming mortgage has a loan amount and underwriting guidelines that follow standards set by the Federal National Mortgage Association (FNMA) and Federal Home Loan Mortgage Corporation (FHLMC).
- A conventional nonconforming mortgage has a higher "jumbo" loan amount or underwriting guidelines that differ from standards set by FNMA and FHLMC.



### **What if I am not able to make a 20% down payment?**

There are mortgage products and programs that may help qualified first-time homebuyers achieve their goals with less available cash. Just remember, if you make less than a 20% down payment, you will likely be required to purchase mortgage insurance (MI) or similar fees, which adds to the cost of your loan and may increase your monthly payment. If you know you want to become a homeowner some day, it's never too early to start building up your personal savings.

### **Can I use gifted money to help me make my down payment?**

Some loan program guidelines may allow you to use monetary gifts from family or friends as part of your down payment. Keep in mind:

- You will most likely be required to provide written proof that the funds were truly a gift and not a personal loan.
- There are limits on how much gift money you can receive per year without increasing your tax obligations.

Speak with a financial advisor, tax accountant, and a mortgage professional to learn more about how these options can impact your overall home financing plans and future goals.

### **Are there any other down payment sources I may be able to use?**

Not-for-profit downpayment assistance programs (DAPs) provide funds to qualified homebuyers to help with down payments and closing costs. Many DAPs don't require repayment, if you meet their guidelines. Groups like Habitat for Humanity and Homeownership Alliance of Nonprofit Downpayment Providers (HAND) can also be sources of help. Your mortgage professional can help you find out which programs are available in your area, explain their details and see if you qualify.



# Who's Who in the Mortgage Process

## Appraiser

An individual who is licensed to estimate the worth (fair market value) of the property you are purchasing.

## Closing or Settlement Agent

The party who conducts the closing meeting. This role may be filled by an attorney, title company, or real estate agent depending upon the state where the property is located.

## Loan Officer

A Loan Officer represents one lending institution and their loan programs. They help you choose the best mortgage loan based upon your situation and will help you complete the loan application.

## Loan Analyst

A Loan Analyst is one who gathers, administers, and processes your loan application before it gets the approval of a loan underwriter. This individual is essential to getting your mortgage loan request to the final close.

## Loan Servicer

The entity that collects mortgage payments (it may or may not be the lender) and pays taxes and insurance and mortgage insurance, if required, on your behalf.

## Mortgage Insurer

By compensating the lender for losses should a borrower be unable to make payments, Mortgage Insurance allows a borrower to get into a home without having to come up with a 20% down payment. Many Mortgage Insurers, such as Enact Mortgage Insurance, can assist borrowers if they become behind in their mortgage payments.

## Mortgage Lender

A financial institution that issues loans. Unlike brokers, lenders control the whole process, from underwriting to funding.

## Property Inspector

An individual certified to conduct an examination of the home. An inspector will look for issues that may affect the value of the property and can assess the condition of a property's roof, foundation, heating and cooling systems, plumbing, electrical work, water and sewage, and some safety issues.

## Real Estate Agent

A real estate agent is a person who acts as an intermediary between sellers and buyers of real estate/real property and attempts to find sellers who wish to sell and buyers who wish to buy. They can often provide helpful and specific community information such as shopping, transportation, and schools.

## Real Estate Broker

A broker is a licensed real estate professional who represents the sellers or buyers of a property, and can typically help determine the market values of properties. While a broker may work independently and has the ability to manage their own firm, an agent usually works under a licensed broker to represent clients.

## Underwriter

A worker who evaluates and determines the risk for potential clients when applying for a mortgage. They may decide whether and under what terms to provide the mortgage.

## Do's and Don'ts During the Home Loan Process



**DO** keep all existing credit card accounts open



**DON'T** MAX OUT or overcharge existing credit cards



**DO** maintain your current employment (if a job change is unavoidable, contact us)



**DON'T** make any large deposits into any of your bank accounts



**DO** continue to make your rent or mortgage payments



**DON'T** make any large purchases, such as a car, appliances, etc.



**DO** pay off collections, tax liens, or judgements



**DON'T** co-sign for a loan or credit with another borrower



**DO** stay current on your existing credit or loan accounts



**DON'T** apply for new credit or loans of any kind



**DO** contact us if you are considering any decisions that may impact your financial picture

# When you're ready to shop for your home

## Effective house hunting begins with a mortgage preapproval

A preapproval will let you know how much you may qualify for, so you and your real estate agent can make the most of time spent looking at homes. Also, with your application, credit check and first loan decision phase already complete, you are seen as a serious homebuyer.

## Choosing your real estate agent

A good real estate agent should have a working knowledge of the area where you're thinking of buying and can help you:

- Decide what you want in a home. Ask your mortgage professional for a "House Wish List" to help you communicate your needs and preferences.
- Search the Multiple Listing Service (MLS) and other resources for homes in your price range that match your needs and show you potential homes, listed by any agency.
- Find valuable information on communities, comparable values of neighboring homes, tax rates and building code regulations.
- Make an appropriate bid on a home you want to buy and act as an intermediary between you and the seller, during the negotiating process.

Note the names of agents on "For Sale" signs as you drive through neighborhoods of interest. Ask friends and family members and your mortgage professional for referrals. Check the websites of local realty companies, too. When you've got a list of potential agents, interview at least two or three of them. In addition to experience, the real estate agent you choose should be trustworthy and easy to talk to.

## Choosing your neighborhood

Location is a very important factor when choosing your new home. Here are a few things to think about and discuss with your real estate agent:

- Do the schools meet my needs?
- Is the commute time acceptable?
- Are there good public recreation areas nearby?
- Do nearby stores and services meet my needs?
- Are most of the homes in the neighborhood owner-occupied?
- What population, development and economic trends are occurring in neighboring areas?

**Start looking online:** There are several excellent websites that showcase homes for sale. Searching your price range is a good way to narrow down the field of neighborhoods you'll have to choose from, and those you'd like to explore further. Write down the MLS numbers of listings that get your attention so you can give them to your real estate agent.

**Check school reports:** If you'll need to send kids to school, now or in the future, the quality of area schools is very important. Ask your real estate agent to give you school reports for any neighborhoods you're interested in.

**Visit local websites:** Go online and research town, city, visitor's bureau, and area newspaper websites.

## Choosing your mortgage lender

We are trained to pay attention to your goals, help you understand your options, and clearly explain how different loan programs work, so you can make informed decisions.

Count on us to provide help and information every step of the way. Let's get started today!

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