

# THE ABC'S of MORTGAGE

*A list of some common mortgage terminology*



# A

**Adjustable Rate Mortgage (ARM)**- An ARM, also known as a Variable Rate Mortgage, is a loan whose interest rate is periodically adjusted based on a pre-determined index.

**Annual Percentage Rate (APR)**- The APR is the cost of a mortgage stated as a yearly rate. Since the APR includes points and other credit costs, it is typically higher than the advertised note rate. An APR allows home buyers to compare different mortgages based on loans' annual costs.

**Appraisal** - An appraisal is a written analysis, prepared by a qualified appraiser, of a property's estimated value.

# B

**Buy-down** - A buy-down is when a lender or builder subsidizes a loan by lowering the interest rate during the initial years of a loan. Payments increase when the subsidy expires.

**Break even point** - The point at which total income equals total expenses. Also used in connection with decisions related to purchasing discount points on a mortgage. Calculating the break even point will identify how many months it will take to recoup the costs associated with paying for the discount point amount under consideration. In other words, if \$3,600 is paid toward discount points to reduce the interest rate and the reduced rate would decrease the monthly mortgage payment by \$100, it would take 3 years to break even on the choice to pay the discount point amount.

# C

**Cash to close** - The amount a homebuyer needs in cash at the closing of the loan. This typically, this includes down payment and closing costs.

**Closing Costs** - The fees charged for services performed, including but not limited to appraisal fees, loan origination, flood certificate, title insurance, and credit report fees. They are typically 2.5 - 3 percent of the loan amount and are typically paid at closing.

**Conventional loan** - A home loan that is not insured or guaranteed by the federal government. A conventional loan can be for conforming or non-conforming loan amounts.

# D

**Debt-to-Income Ratio** - Your total monthly debt payments (for example: loans, credit cards and court-ordered payments) divided by your gross monthly income before taxes and expressed as a percentage.

**Down Payment** - The part of a property's purchase price paid by the borrower (i.e., not financed by the mortgage). Down payments can be anywhere from 0-20 percent of the purchase price.

# E

**Earnest Money** - Earnest money is paid by the buyer to the seller as a sign of good faith. The deposit is typically made when the purchase agreement is signed.

**Equity** - The difference between the fair market value (appraised value) of your home and your outstanding mortgage balances and other liens.

**Escrow** - Escrow is the holding of funds or documents by a third party prior to closing; the funds are usually for payment of taxes and insurance on property

# F

**FHA home loan** - A mortgage that is insured by the Federal Housing Administration (FHA). Also known as a government loan. FHA mortgage insurance protects the lender (not the borrower) if a borrower defaults on the FHA loan. This insurance enables a lender to provide loan options and benefits often not available through conventional financing.

**Floating rate** - A loan rate for which the lender has not "locked" or committed to lend at a particular interest rate. The floating interest rate and any discount points are not guaranteed. Your actual interest rate and discount points will be based on the market price available for your loan product at the time your interest rate is locked.

# G

**Government loan** - A loan that is insured by the Federal Housing Administration (FHA), guaranteed by the Department of Veterans Affairs (VA) or guaranteed by the Rural Housing Service (RHS). The insurance protects the lender (not the borrower) if a borrower defaults on the loan. This insurance enables a lender to provide loan options and benefits often not available through conventional financing.

# H

**Homeowners Insurance** - Insurance to protect your home against damage from fire, hurricanes and other catastrophes. Usually, homeowners insurance also covers you against theft and vandalism, as well as personal liability in case someone is hurt or injured on your property. Also called hazard insurance.

**HUD-1 Settlement Statement** - Standard, government regulated settlement statement that itemizes the costs of transaction when purchasing a home. Commonly referred to as "HUDs" or "HUD-1s."

# I

**Insured Mortgage** - A mortgage that is protected by an insurer in case of default. The insurance protects the lender (not the borrower) if a borrower defaults on the loan.

**Interest Rate** - The annual cost of a loan to a borrower, usually expressed as a percentage. The interest rate does not include fees charged for the loan.

# J

**Jumbo Loan** - Also known as a nonconforming loan. The amount of the loan exceeds standards that would make it eligible for sale to Fannie Mae and Freddie Mac. Certain geographical areas have temporary conforming loan limits higher than typical conforming limits. Lenders may charge additional fees and place certain restrictions due to the large loan amounts. Also referred to as a "Nonconforming Loan"

# L

**Loan Estimate (LE)** - Disclosure to help consumers understand the key loan terms and estimated costs of a mortgage before they make a complete application. After a consumer submits 6 key elements: name, income, social security number, property address, estimated property value and desired loan amount, the lender is required to provide this form. All lenders are required to use the same standard loan estimate form to make it easier for consumers to compare and shop for a mortgage.

**Loan-to-value ratio (LTV)** - The ratio between the unpaid principal amount of your loan, or your credit limit in the case of a line of credit, and the appraised value of your collateral. Expressed as a percentage. For example, if you have an \$80,000 first mortgage on a property with an appraised value of \$100,000, the LTV is 80% ( $\$80,000 / \$100,000 = 80\%$ ).

# M

**Mortgage Insurance** - For conventional loans, insurance that protects the lender if you default on your loan. If your down payment is less than 20%, most lenders will require you to pay mortgage insurance. Also called private mortgage insurance (PMI).

# N

**Note** - A written agreement in which the signer promises to pay to a named person or company a specific sum of money at a specified date or on demand.

**Note Rate** - The interest rate stated in a mortgage note.

# O

**Origination Fee** - A fee imposed by a lender to cover certain processing expenses in connection with making a mortgage loan. Usually a percentage of the amount loaned (often 1%). The origination fee is stated in the form of points.

**Owner-Occupied** - A property that the owner occupies as a principal residence.

# P

**PITI** - A borrower's monthly mortgage payment: Principal, Interest, Taxes and Insurance

**Points** - Fee assessed by the lender, usually to permanently buy a below-market rate. One point equals 1 percent of the loan amount. For example, three points on a \$100,000 mortgage is \$3,000.

**Prepaid Expenses** - The expenses that are usually paid in advance, such as escrows for taxes and insurance (which are paid at closing).

**Prepaid Interest** - Interest collected at closing of a first mortgage, covering the period from the date of disbursement to the start of the next payment period.

**Prequalification** - The process of providing financial and other information (such as employment history and proposed collateral) by a prospective borrower in order for the lender to preliminarily estimate how much the borrower may obtain for the purchase of a home. A prequalification is not a commitment to lend.

**Q**

**Qualifying Ratios** - Calculations that are used to determine whether a borrower can qualify for a mortgage. They consist of 2 separate calculations: a housing expense as a percent of income and total debt obligations as a percent of income.

**R**

**Rate Lock** - A commitment issued by a lender to a borrower guaranteeing a specific interest rate for a specified period of time. Rate lock periods are for a fixed number of days, and rate lock expiration occurs when that period has passed, subjecting the interest rate on the loan to market fluctuations since the date of the initial rate lock. When a rate lock expires, you will need to contact your lending specialist to establish a new rate lock prior to closing your loan.

**Rescission** - The cancellation of a contract. In certain real estate-secured transactions that involve the refinance of a primary residence, applicants have 3 business days to cancel the transaction.

**S**

**Settlement/Closing** - Closing is the meeting between buyer, seller, and closing officer (a lawyer or title/escrow company representative depending on the state) where the property and funds legally change hands by signing all relevant documents.

**Subordinate Financing** - Any mortgage or other lien that has a priority lower than that of the first mortgage. The subordinate loan has a claim to payment in a foreclosure only after the first mortgage is paid. Example: HELOC or Home Equity Loan

**T**

**Third Party Fees** - Fees charged for services rendered by parties other than the borrower or the lender. Such fees may include appraisal, credit report, title and flood certifications.

**Title Insurance** - Insurance that protects an interested party, either the owner or the lender, against issues that would affect legal ownership of the property.

**U**

**Underwriting** - The lender's process of deciding whether to make a loan to a potential borrower based on credit, employment, assets and other factors, and the matching of this risk to an appropriate rate, term and loan amount.

**V**

**Variable Rate** - An interest rate that may fluctuate or change periodically, often in relation to an index such as the prime rate or other criteria. Payments may increase or decrease accordingly.

**W**

**Wire Transfer** - A transfer of money from one person's bank to another person's bank account, either domestically or internationally.