

Your Own Home



FDIC



FDIC Financial Education Curriculum

Welcome



1. **Agenda**
2. **Ground Rules**
3. **Introductions**



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Objectives



- **If you are a pre-homebuyer:**
 - Explain the advantages and disadvantages of renting versus owning a home
 - Identify questions to ask to determine your readiness to buy a home
 - Identify the steps required to buy a home
 - Identify basic terms and required disclosures used in a mortgage transaction



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Objectives



- **Pre-homebuyers:**
 - Describe the advantages and disadvantages of different mortgage options
 - Describe how interest rates affect the amount of house you can buy
 - Explain how taxes and insurance affect a monthly payment and the amount of house you can buy



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Objectives

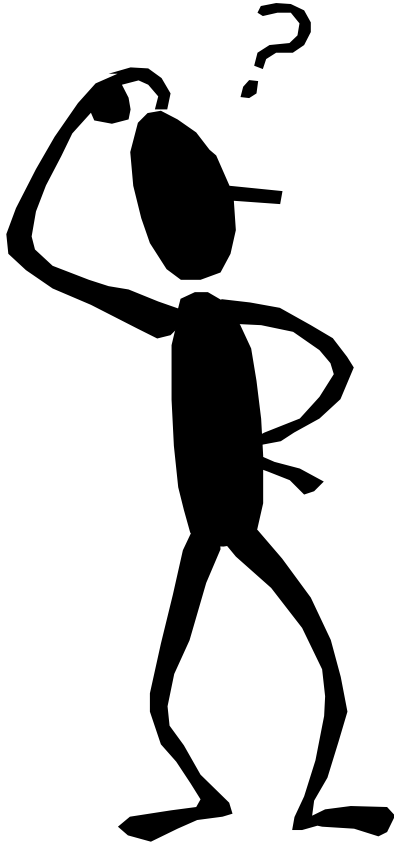


- **If you are a homeowner:**
 - Describe the advantages and disadvantages of borrowing against a home
 - Explain what to do if you are having trouble making payments
 - Describe different types of refinancing options
 - Explain the advantages and disadvantages of a reverse mortgage
 - Identify predatory lending practices and loan scams



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What Do You Know?



What do you know or want to learn about buying or owning a home?



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Renting a Home

- **Advantages:**

- No property maintenance
- Rental contract 1 year or less
- No homeowner associated costs

- **Disadvantages:**

- You are not the owner
- Your rent might increase
- You might not be able to renew your contract



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Owning a Home

- **Advantages:**
 - Building equity and borrowing against it
 - Good investment
 - Tax-deductible mortgage interest
 - Asset you can pass on to family members
- **Disadvantages:**
 - Property maintenance and upkeep
 - Not as easy to move as renting
 - Risk of losing your home



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Five Steps to Buying a Home

1. Determine your readiness to buy a house
2. Determine how much mortgage you can afford
3. Determine which mortgage option is best for you
4. Qualify for a loan
5. Go through settlement



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Meet Patricia



- **Patricia...**
 - Is a medical technologist
 - Makes \$49,200/year, or \$4,100/month
 - Is currently living with her parents
 - Wants to know more about home ownership



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Step 1: Readiness to Buy A House

- **Do you have:**
 - A steady source of income?
 - Good credit history?
 - Ability to pay debts, mortgage, and other additional costs?
 - Plans to move within 2 to 3 years?
 - Money for a down payment and closing costs?



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Down Payment and Other Expenses

- **Down payment:**
 - Typically 20% of the purchase price
 - Smaller down payment options may be available (e.g., 3% of purchase price)
- **Other expenses:**
 - Household emergencies, repairs, and other expenses
 - Private Mortgage Insurance (PMI)



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Mortgage Payments

- Include principal and interest
- May include PMI, property taxes, and homeowners insurance
- Should be no more than 28% of your income



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Other Questions to Ask Yourself


- **Where do you want to live?**
- **What kind of neighborhood do you want?**
- **If you have children, what types of schools should be in the neighborhood?**
- **How much space do you need?**



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Activity 1: Is Patricia Ready to Buy a House?

Complete Activity 1 in the Participant Guide.

- 
1. Read the scenario.
 2. Answer the question.
 3. Be prepared to explain your answer.



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Homebuyer Assistance Programs

- **For programs in your area, check with:**
 - Your lender, real estate agent, or local government about homebuyer assistance programs
 - A local Housing and Urban Development (HUD)-approved homeownership counseling agency



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Characteristics of Government Programs

- **Low down payment requirements**
- **Flexible underwriting standards**
- **Longer payment terms**
- **Homeowner education requirement**



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Fair Housing Act


- Prohibits discrimination in housing-related transactions on the basis of:
 - Race
 - Color
 - Religion
 - Sex
 - National origin
 - Family status
 - Handicap status



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Activity 2: Does Patricia Have Enough Money for a Down Payment?

Complete Activity 2 in the Participant Guide.

- 
1. Read the scenario.
 2. Answer the question provided.
 3. Be prepared to share your answer.



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Mortgage Terms

- **PITI:**
 - **P**rincipal
 - **I**nterest
 - **T**axes
 - **I**nsurance
- **PMI**



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How Taxes and Insurance are Paid

- **Through escrow account**
 - The Real Estate Settlement Procedures Act (RESPA) limits amount required to be held in escrow account.
- **Separately**
 - You are responsible for periodic payments.



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Four Cs of Loan Decision Making

Four factors lenders use to qualify you for a loan:

Capacity

Capital

Character

Collateral



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Step 2: Determine How Much Mortgage Can You Afford

- **Pre-qualification:**

- Lets you know how much mortgage you can afford

- **Pre-approval**

- Commitment from the lender to lend you money



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Patricia's Pre-Qualification

- Pre-qualified for \$165,000
- Rule of thumb estimate:
 - 2 to 3 times their household income:
 $\$49,200 \times 2 = \$ 98,400$
 $\$49,200 \times 2.5 = \$123,000$
 $\$49,200 \times 3 = \$147,600$
- Consider what you can afford if you qualify for more!



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Debt-to-Income (DTI) Ratios

- **Front-End Ratio:**
 - PITI or housing expenses should generally be less than 25–28% of your monthly gross income.
- **Back-End Ratio:**
 - Housing expenses + long-term debt should be less than 33–36% of your monthly gross income.



Activity 3: How Much Mortgage Can Patricia Afford?

Complete Activity 3 in the Participant Guide.

- 
1. Read the scenario.
 2. Answer the questions.
 3. Be prepared to share your answer.



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Mortgage Terms

15-Year Mortgage

- Borrow less money because of larger monthly payments
- Build equity faster
- Less interest to pay
- Lower interest rate

30-Year Mortgage

- Borrow more money because of lower monthly payments
- Build equity more slowly
- Can deduct more interest from income tax
- Higher interest rate



Mortgage Type

Fixed-Rate Mortgage

- Interest rate cannot increase
- Payments are predictable
- Interest rates could go below your set rate

Adjustable-Rate Mortgage

- Interest rate can increase or decrease
- Rates may be low for only an initial period
- Monthly payments may initially be lower than fixed-rate loans, but can increase significantly



Step 3: Which Mortgage Option Is Best for You

- **Fixed-rate mortgage**
- **Adjustable-rate mortgage (ARM)**
- **Interest-only mortgage**
- **Biweekly payment mortgage**



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Interest-Only Mortgages

- Pay only the interest, not the principal, for a fixed term (e.g., 5 to 7 years)
- **After the fixed term, you can:**
 - Refinance
 - Pay the balance in a lump sum
 - Start monthly mortgage payments toward the principal



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Benefits of Interest-Only Loans

- **A good choice if you:**
 - Do not plan to live in your home for more than the interest-only period
 - Have modest current income that will go up in the future
 - Are trying to resolve credit issues so that you can refinance into a lower fixed rate



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Pitfalls of Interest-Only Loans

- **Payments:**
 - May not cover all of the interest owed, prevents you from building equity
 - Can become unaffordable after the interest-only period
 - You may incur refinancing costs if you can no longer afford the payments.



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Biweekly Payment Mortgage

- A fixed-rate conventional mortgage with payment due every 2 weeks
- **Alternative: Add more money to your monthly payment**
 - Make sure your lender does not charge a prepayment penalty



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Shop, Compare, Negotiate

- **Check newspapers and the Internet for terms and rates**
- **Negotiate your best price**
- **Let lenders compete for your business**
- **Get costs in writing**
- **Use the APR and GFE to compare all costs**



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Good Faith Estimate

- Settlement services cost estimate
- Given to you when you apply for the loan
- **Keep your GFE to compare with the final settlement costs**
- **Ask the lender questions about any changes**



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Mortgage Shopping Worksheet

- **Federal law requires the lender or broker to:**
 - Disclose estimates of how much the loan will cost and the APR (Truth in Lending Disclosure)
 - Give you an estimate of closing cost fees and the money required at closing (GFE)



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Step 4: Qualify For a Loan


- Obtain pre-qualification and pre-approval
- Include homeowner's association dues when calculating your housing expenses



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Activity 4: Does Patricia Qualify for a Loan?

Complete Activity 4 in the Participant Guide.

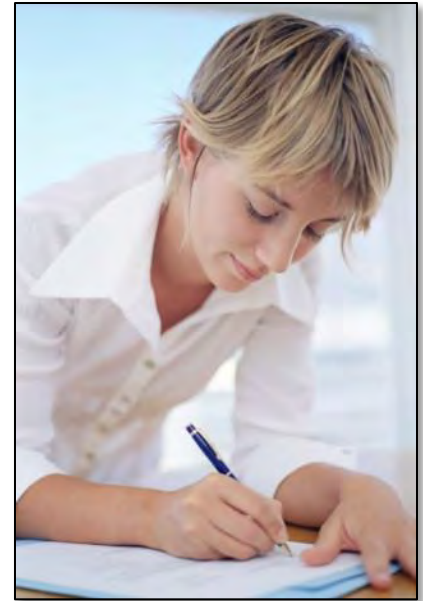
- 
1. Read the scenario.
 2. Answer the question provided.
 3. Be prepared to share your answer.



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Debt-to-Income (DTI) Exceeds Recommended Ratios

- **You might still qualify for a loan if you:**
 - Have ability to pay more toward housing expenses
 - Show evidence of sustained, good credit history
 - Make larger down payment
 - Have cash reserves

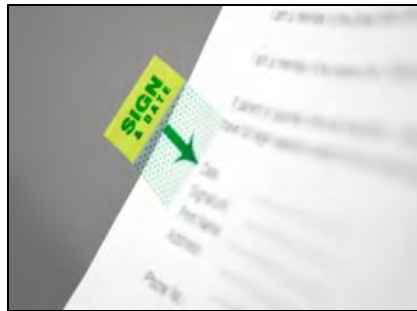


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Step 5: Go Through Settlement

- **Settlement:**

- Sign documents to finalize the sale of the house and any mortgage financing.
- Right to review the settlement statement at least 1 day before closing.



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Having Trouble Making Payments?

- **Contact your lender immediately**
- **Get help from a trained reputable housing counselor at no charge or for a small fee**



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Tapping Into Your Home's Equity

- Home equity loans
- Home equity lines of credit (HELOC)
- Refinancing and cash-out refinancing
- Reverse mortgages



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Home Equity Loans

- **One-time loan for a lump sum**
- **Typically at a fixed interest rate**
- **Equal monthly payments over a set period of time**



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Home Equity Lines of Credit



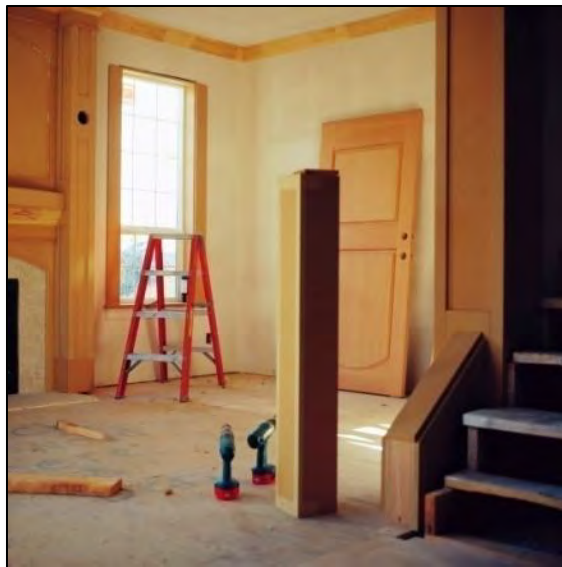
- **Works like a credit card:**
 - Draw from the line of credit as needed
 - Repay the principal and available credit goes up again
- **Interest rates are typically variable**



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Advantages of Home Equity Options

- **Flexibility to finance major expenses**
- **Lower interest rate than credit cards**
- **Tax-deductible interest**



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Home Equity Options Risks

- **Home is collateral**
- **Housing values can decrease**
- **Rates/payment may increase**
- **Temptation to use the money for unwise investments or purchases**
 - **Use caution and self-discipline**



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Your Rights Under Federal Law

- **You have 3 business days after signing loan papers to cancel the deal without penalty.**
 - Must cancel the deal in writing
 - Lender must return any fees or finance charges you paid
 - Does not apply if you are buying a home or refinancing without borrowing additional money



Refinancing Options

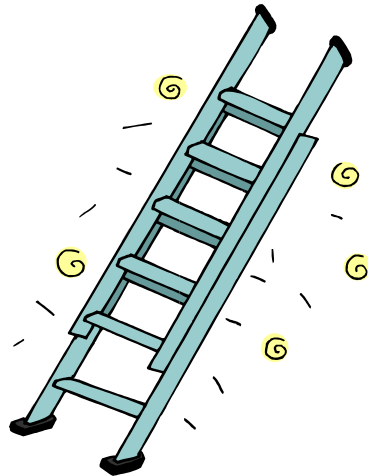
- ***Refinancing:*** pay off an existing home loan replace with a new loan.
- ***Cash out refinance loan:*** can borrow more money than owed on the loan to be replaced.



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Cash-Out Refinancing Example

- **Current Mortgage: \$100,000 at 9.95%**
- **Owe a total of \$87,000**
- **Monthly payment: \$873.88**
- **Want \$20,000 for improvements**



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Cash-Out Refinance Example

Option 1:

- Refinance \$107,000 ($\$87,000 + 20,000$)
- Interest rate: 6.02%
- Monthly payment: \$642.90 x 30 years
- Total = \$231,442.40

Option 2:

- Refinance \$87,000 at \$522.73 x 30 years
- Home equity loan: \$20,000 at 7.36% x 20 years
- Total = \$226,440.75



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Reverse Mortgage

- **Borrowing against home equity to receive cash:**
 - In a lump sum
 - Through monthly payments
 - As a line of credit you can tap when needed
- **Homeowners must be at least 62 years old.**
- **At least one owner must live in the house most of the year.**
- **Home type must be eligible.**



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Reverse Mortgage Considerations

- **Must repay loan + interest when you sell, move, or die.**
 - Amount owed increases over time.
- **Continue to pay property taxes, insurance, and repair costs.**
- **Heir must repay the loan to keep the house.**
- **Up-front costs make the first years of the loan relatively expensive.**



Predatory Lending Practices



**Marketing tactics,
collection practices, and
loan terms that deceive
and exploit borrowers**



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Department of Housing and Urban Development

- **Funds:**
 - Post-home ownership course
 - Housing counseling agencies
- **Contact HUD for a list of HUD-approved housing counseling agencies:**
 - 1-800-569-4287
 - www.hud.gov



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Summary

- **What final questions do you have?**
- **What have you learned?**
- **How would you evaluate the training?**



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Conclusion

- **You learned about:**

- Renting versus owning your home
- The steps required to buy a home
- Questions to determine if you are ready to buy a home
- The components of a mortgage
- Different mortgage options for buying a home
- Tapping into your home's equity
- Pitfalls and dangers of unwise mortgage refinancing



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