A Buyer's Guide to Financing a Home

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Buying a home can be frustrating, intimidating and extremely stressful. It's hard to know where to begin – especially for first-time home buyers. Much depends on the strategies you'll use in the current housing market condition and your knowledge of financing.

It's a constantly changing environment that you should know before venturing into the fray. You'll want to make the best deal you can on your home and make some wise financing decisions as well as knowing the lending requirements and tax repercussions.

You need to know how to research the housing market, how to become pre-approved for a loan and how to know what price home you can afford. You also want information on how to find a mortgage lender, what the job of a lender consists of and the intricacies of closing the sale, and more.

Before trying to head into it blindly, you need help navigating the daunting journey of home buying. You have to become at ease with the process and wipe out the confusion as you learn about the process in a step-by-step manner.

Research the Basics of Home Buying

Learning the basics of financing when it comes to real estate is like learning about a person before you marry them. The more you know, the better you can allay your fears and cut the confusion that often comes with a process you're unfamiliar with.

You need to know how to negotiate to get the best deal on a house and what it takes to get a low-down-payment mortgage contract. If you don't know how to improve your credit score, you should find out before beginning the home-buying process.

Lending standards change constantly and you need to get the latest information possible. Know what's happening in the current marketplace, what the mortgage rates are and find out about new or changing lending laws before beginning the search for your new home.

To begin the home-buying process, read as many newspapers, magazines (with real estate listings) and pour over websites to get an idea of what types of homes interest you, how long they've been on the market and observe changes which occurred in the asking prices.

This will give you a good idea of trends, what's available and for what prices. Pay attention to details when you're checking out the market. Drive around a neighborhood you're interested in to see if it really suits you and then price homes in that area.

Also, think about amenities you desire in a home. Will you be content with a balcony or small patio rather than a spacious yard – and how do you feel about custom countertops and cabinetry compared to stock items?

When you think you're ready, it's time to take the next step involved in financing a home. Based on your research, this is where you'll find out how much house you can afford and begin the paperwork so you can become pre-qualified and pre-approved for a loan.

Navigating the Process of Pre-Qualification and Pre-Approval

First-time buyers are easily confused and intimidated by the process of securing a mortgage. First, you must know how much you can truly spend on a home without breaking the bank and making it difficult to pay your other bills.

You can get a good idea about how much you can afford before going to the lender by using an online mortgage calculator. You'll enter some numbers based on your financial situation and the calculator will provide a figure based on that information.

A mortgage payment calculator is great to get an estimate of what your monthly payments might be. Just enter the price of home you can afford, the down payment you're planning to make and the interest rate you're looking for and you'll get a good idea of how much you're going to pay each month.

Lenders usually recommend that you should spend no more on the cost of a home than 3 to 5 times of your annual household income assuming you're making a 20% down payment and your other debts aren't overwhelming.

The pre-qualification process is performed by a mortgage lender and involves providing some basic information such as your income and assets such as investments and savings.

The lender then reviews the information you provided and lets you know how much they'll lend. You'll then be able to narrow down the homes you look at to only the ones you can afford.

The pre-approval process involves becoming pre-approved for credit. You'll then provide financial documents such as W-2 statements, bank account statements and paycheck stubs to the lender so they can verify the information you've provided.

Make sure you understand how to know if you're ready for a mortgage and avoid being disappointed because the lender turned you down. First, take a close look at your monthly budget and begin to save for a substantial down payment.

Look closely at the neighborhood and type of home you're considering. Are homes priced at a cost you can afford or are they beyond your means? Long before the pre-qualification and pre-approval process you should monitor your credit report carefully and take care of any issues.

Make sure you keep all monthly payments current and work to reduce your debt. Escrow can sometimes throw a wrench in the house-buying process because of hidden and unexpected costs.

Finally, educate yourself as much as possible about financing a home so you're up-to-date on the changes and nuances that occur on a constant basis. Preparation is the key to helping the finance portion of buying a home go smoothly.

Know Your Home Financing Options

There is an abundance of competitively-priced loan options and lenders with good customer service reputations. Knowing your home financing options before you get too far in the home-buying process can cut down on the stress when it gets down to the final steps.

You can choose a financing option from several criteria – keeping your monthly payments low might be a priority for you. Others may be more interested in making sure there is never an increase in the monthly payments.

Among the most popular and well-regarded type of loans for home-buyers are FHA loans. Established in 1934 by the federal government, they're able to offer better interest rates than most commercial mortgage lenders.

The amounts of FHA loans you can apply for depends on the area in which you live. For example, in areas where home prices are comparably low, you may only be able to borrow up to $300,000 – whereas in high-cost real estate areas such as New York and Los Angeles, the amount of a loan may reach as high as $750,000.

Some benefits of securing an FHA loan include the fact that you only need to have a 3% down payment to get financing. It's easy to qualify because FHA doesn't use the same strict criteria as other mortgage lenders to determine eligibility, credit worthiness or interest rate.

You'll have more security with an FHA loan than even some established financial institutions, but you still shouldn't expect an easy ride. They do have strict rules about lending to those with histories of foreclosures and bankruptcy.

A fixed rate mortgage loan is another option. The interest rate stays the same for the entire time of repayment, so your monthly payment will remain fixed for the duration of the loan. You can even choose a long-term option for as many as 30 years.

An adjustable rate mortgage loan (ARM) provides you with a rate that will periodically change – usually every year after a set time of staying fixed. Typically referred to as a "hybrid" type of loan, the adjustable rate mortgage begins with an interest rate that doesn't change for five years and then starts adjusting the rate each year thereafter.

You may benefit more from a fixed type of loan because you'll know exactly what your interest rate and monthly payment will be for the entire duration of the loan. The benefit of an ARM is that the beginning interest rate is significantly lower.

Government loans such as FHA, VA and USDA/RHS loans are insured by the government and each has its pros and cons. An FHA loan lets you make a low down payment, but you'll have to secure mortgage insurance which increases the amount of your monthly payments.

The VA (U.S. Department of Veterans Affairs) is exclusively for the military and their families. The mortgage is guaranteed by the government and they will pay for any losses that result from a default. This type of loan requires no down payment.

The United States Department of Agriculture (USDA) allows rural residents who may have a low income and can't find financing elsewhere to secure a home loan if they meet specific income requirements. The Rural Housing Service (RHS) manages the USDA loan process.

A conventional home loan is set apart from FHA, VA and USDA loans because it isn't guaranteed or insured by the government. Other types of loans include Jumbo and Conforming which involve programs such as Fannie Mae and Freddie Mac.

Your realtor and mortgage lender should be able to guide you to the loan that suits your situation best, but take the time to really educate yourself so you can make the best decision.

Choosing a Mortgage Lender

Buying a home usually ties you to a mortgage lender for up to 30 years – so you'll want to shop around for the best one you can get. And it's not all about getting a great interest rate.

It's important to find a lender who can guide you through the maze of decisions you'll have to make in your home-buying journey. Don't go with the first lender that accepts your application, but consider your needs and choose the lender that can best deal with them.

You can choose from two methods to find a lender. One is to research, interview and choose the lender yourself and the other is to go through a mortgage broker who will negotiate the deal between a lender and you.

The mortgage broker can save you much time and angst by taking care of much of the work it takes to find the right lender. But know that brokers do earn money when they arrange the contract between you and the lender.

A broker who doesn't necessarily have your best interests in mind could arrange the contract with a lender that offers the best profit to them – but it's not always the best mortgage deal for you.

That's why it's important to research before you choose. Be sure to ask for references from other homeowners who have dealt with the broker and can tell you about their experience.

If a broker declines to give references from clients they've worked with you should decline to work with them. Before you begin to search for a lender, decide if you prefer a smaller lender who will know your name and provide excellent customer service.

A large lender might be able to secure the best interest rate for you. Research the difference before you decide. If possible, get as much information as you can from a friend or family member who has used a broker or lender.

You can also browse online reviews. Knowing as much as possible about the reputation of the lender you're dealing with can save you much stress later in the home-buying process.

One of the most daunting decisions you'll make when buying a home is deciding which lender to choose. Don't take the first one who accepts your application, but shop around, interview references and ask questions. Read the fine print of the deal.

Your Lender's Tasks – What Should You Expect?

The amount of paperwork involved in purchasing a home is staggering. Fortunately, part of your lender's job is to coordinate with a title company to make sure that everything is in order and that the seller is definitely the owner of the home you're purchasing.

Basically, a lender is a licensed professional who provides money to fund your home loan through a third party or directly to you. Lenders can have a variety of jobs depending on what they specialize in.

For example, a mortgage broker will assess your financial information and then attempt to match you with a lender offering the best terms and rates for your situation. Out of many lenders, the broker will choose one that matches and you'll then work with that lender exclusively.

A lender can be a financial institution, public or private group or even an individual who transfers funds, expecting them to be paid back according to the contract. There may be fees and interest that you can pay through the mortgage payment or in a lump sum.

Some lenders are considered wholesale types which mean they get mortgages through brokers outside of their own company and agree to fund them. Brokers take the loan applications in the beginning and then sell them to the wholesale lenders.

Retail lenders (also called direct lenders) such as some banks have loan officers that perform all loan functions. You can work through a retail lender directly through the loan officer to acquire the loan.

Correspondent lenders combine the roles of a broker and retail lender by funding mortgage loans with their own money, but can lock in rates with another lender and then sell the loan.

This reduces their risk of loaning the funds. Your lender – whatever the type – will review your credit report and determine if you have the means to pay back the loan. The lender will also evaluate your income and employment history, new and old debt and may use the FICO (Fair Isaac Corporation) score to help them make a decision about giving you the loan.

The lender will want to know how much capital you have in case you lose your job. This may include investments, savings accounts and other assets you might use if you lose your source of income.

Mortgage lenders can take much of the drudge work out of purchasing a home. It's overwhelming for most of us to navigate the process. A good lender will keep you informed of everything that's going on in the process of purchasing a home and if you choose the lender well, it can be a smooth experience.

Beware of mortgage loan fraud. Some predatory lending practices exist that don't have your best interest at heart. For example, a fraudulent lender might remove you from a fixed rate loan you've been approved for and give you an adjustable rate mortgage that has a low "teaser" rate.

To avoid this scam, check the good faith estimate that's required on all mortgage transactions to check out the APR that's being offered. You can quickly figure out the full price of the loan.

Find the Home – Make an Offer

Now comes the fun part – looking for your dream home. Before you begin to drive around looking for open houses, identify your needs and wishes for the home. You know what you can afford because you've been pre-approved for a loan – but if you don't know what you're really looking for the dream can evaporate before you begin.

If you tell your real estate agent that you're looking for a large home, she doesn't really know your definition of large and can't help you until you narrow it down to approximate square feet.

Wanting an older home to you might mean pre-1900s, but to your realtor it might mean a 1950s ranch style. Write down your wants and needs and prioritize them. For example, you may want a certain finish in the kitchen, but if it's not a deal breaker, keep your mind open to other options.

You'll likely have to make compromises as you move along in your home search and you'll soon find out which is a deal breaker to you – and which are not. You might divide your feature list into the 'have to have', 'It would be nice to have' and those features that you don't care one way or the other about.

The real estate agent you've chosen can help you through the steps of finding a home making an offer and then help you with closing and other tasks. You should familiarize yourself with what's available in the neighborhood you want to be in and then trust your realtor to inform you about homes and information that you may not have access to.

The agent works for you – but the seller compensates her by paying a commission at closing. You'll likely see a lot of homes and you may not remember every detail, so it's a good idea that you make pictures or take a video of those homes you're truly interested in.

When you've finally found the home that's best for you, your realtor will help you in the negotiation process to get you a fair price. She'll check out the prices of comparable homes in the neighborhood your home is in and present your offer to the seller.

After you've reached an agreement on the price and the seller has accepted your offer, the home will go into escrow – meaning there are other tasks to complete before the sale is final.

A Home Inspection Can Save You Money

A thorough home inspection by a licensed home inspector can save you money, but the peace of mind you gain is also very valuable and could set the tone for living in the home for the next few years.

Usually, an offer on a home is contingent on the inspection of the property. The inspector will look for such things as structural damage and things that need repair. The contingency protects you against getting stuck with a money pit of a home if the inspection reveals nightmares getting ready to happen.

The home inspector will send a report on his assessment of the home to both you and the seller. You may then ask the seller to fix any problems and on the final walk-through of the home, you can check to see if contingent repairs have been made.

Although inspections are optional, they're almost essential in the world of home-buying so you can assess the problems that already exist and those that might happen soon. If there are too many problems you don't want to deal with, you then have the option of finding another home that suits you better.

Some banks require a home inspection before they will approve a loan, but you, the buyer are responsible for and will pay for the inspection. Be sure and accompany the inspector on the home's inspection and ask any questions you might have.

The inspector works for you rather than the seller and you can rest assured he will report any potential problems directly to you. The seller will also receive a copy of the report.

Your realtor can be a good source of information about certified home inspectors or check out the professionals online. Make sure they're certified and have completed continuing education courses if necessary.

Generally, the home inspector will provide you with a report that covers such things as interior plumbing and electrical systems, heating and cooling, window, door and door frame conditions, foundation, basement and other structural areas, floors, wall and ceiling and insulation (if visible).

The inspection doesn't cover all the components in your home - such as septic tank, inside walls, chimney and roof and any wells or other structures other than the main house.

After you receive the inspection report, ask any and all questions you may have and don't hesitate to seek further inspection (for example a plumber or A/C and heating specialist) if you have serious doubts.

Get an Appraisal

An appraisal is performed by an experienced appraiser who will assess what the home is worth based on the fair market value. Lenders will arrange for the appraisal, but the appraiser will not be connected to the lender in any way.

The process is to simply let everyone know that you're paying the fair market value for the home. Among the criteria in a home appraisal are gathering the most recent sales in the area for similar homes, the property's condition, location and overall assessment of the neighborhood.

Licensed or certified professional appraisers are very highly trained to objectively assess the home without bias and provide you with his opinion about the home. Appraisers are highly regulated and there are dire consequences for providing misleading reports.

Your appraiser won't be looking at anything except the home and what is permanently attached to it. Characteristics such as number of bedrooms, baths, square footage, age, size of lot, view and location will all factor in to the final appraisal.

If you're in love with the home you've chosen and don't feel as if you've received fair appraisal, you can challenge the content by stating what you think is particularly valuable about the home that the appraiser didn't take into consideration.

Keep in mind that most appraisals are also based on the other sales in your neighborhood for similar properties, but if you can provide the lender more information about the property's value, it may help.

Closing the Sale

You're almost finished and that dream home is in the final stages of becoming yours. The closing of purchasing a home between you and the seller isn't done by shaking hands or committing verbally to the deal.

When you close, you're agreeing (and signing papers) that all agreements have been met. The seller will transfer the property and any existing mortgages on the home will be paid, ensuring the house is free and clear and the title can be yours.

Essentially, closing is all about documents and money, transfer of ownership and taking possession of the home. All repairs should have already been made to the home that the seller agreed to and everyone who assisted in the home buying process is paid.

A settlement agent (or escrowee) will likely be the person or company that finalizes the sale. The agent will be a disinterested third party and make sure all money is transferred, people are paid, the title is clear and that all agents are paid.

The closing will likely occur in the escrowee's office – usually the title company that ensures the title to the property for the buyer. It can, however take place in a lender or realtor's office. A notary should be present at the closing to validate the paperwork.

You should always have the escrowee explain the documents for you. Much of it is "legalese" and you may want to ask questions along the way. In some states, the closing may take a few days or even weeks.

The seller should always attend the closing but the seller may or may not be compelled to attend because they can transfer documents and pre-sign the deed over to the seller before the closing takes place.

The closing process on your home will end when the seller's lender is paid by the escrowee or agent, all service providers and lien holders (if any) are paid and the seller receives the proceeds from the sale of the home.

The deed (including the mortgage) will then be transferred to you (including the loan documents) and within a couple of days your loan is funded. After the check is delivered to the seller – you can finally move into your dream home.

Some Final Thoughts about Financing a Home

If you've never financed a home, the entire process can seem complicated, overwhelming and intimidating. Hang in there. If you're patient and do the research, you'll soon be experiencing one of the most exciting times of your life – home ownership.

There are some dos and don'ts you should think about before you choose that dream home and find a real estate agent, lender, inspector or neighborhood. The lending marketplace has drastically changed over the past few years – so know the good, the bad and the ugly before taking the leap.

For example, don't think of purchasing real estate as a short-term investment and you can make lots of money by fixing and flipping. It usually takes a while for your home investment to materialize into a great investment.

When you're shopping, think about the resale value of your future home. It's doubtful that you'll live in the same house for the rest of your life, so don't make expensive or funky remodels without giving it some thought about how it will look to someone else

Before you shop – write down and prioritize your preferences in a home – and then set a budget that won't make you miserable and sorry you made the decision. Even if you qualify for a higher-priced home, use common sense (and some time on the calculator) to face reality.

And make sure you get pre-approved for a loan before you begin your home search. Then you're not blindsided by finding out you can't buy a home you've really grown to love. You'll know your price range and the sellers will know you mean business.

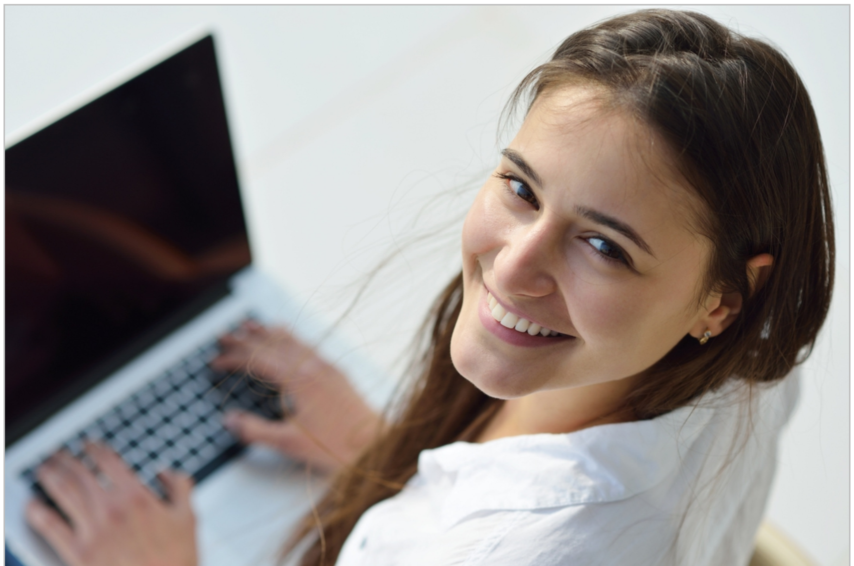
Don't be a stranger at closing. Help schedule a good time to close, know a close estimate of costs before you meet with the lender and take a look at the contract and other paperwork before you meet.

Don't be blindsided by hidden costs at closing. There may be maintenance and insurance costs, plus property taxes and much more that you may not have known about. Make sure you know what your hidden costs might be.

When the excitement and butterflies over owning your new home begin to dissipate, be sure to manage your finances well. Never miss a mortgage payment date and make sure you notice how your payments are divided each month.

Paying off your mortgage as soon as you can may also be a good idea. Since the beginning of time, land and property have been badges of honor and coveted for the protection they give and are showcases for your hard work and good credit.

Finding and financing a home is one of the most costly and important moves you'll ever make, so make good decisions by first finding out all you can about the process. You'll love the feeling of home ownership and finally understand the old saying, "There's no place like home."



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