A Better Transaction with Hudson United

HUDSON UNITED

MORTGAGE ▪ TITLE ▪ INSURANCE

Welcome to Hudson United Home Services

We want to thank you for giving Hudson United the opportunity to work with you to help address your mortgage, insurance, and title needs. We look forward to providing you with the kind of home buying experience that have made our family of companies one of the most successful home service firms in the country.

This is our starting point for the delivery of services to you throughout the process. You're probably already familiar with the Buyer Orientation Guide provided by your Better Homes and Gardens Rand Realty agent, which takes you through the three stages of the home buying experience and explains how you can prepare for the long process of purchasing a home. This Orientation Guide for Hudson United has the same purpose, but with particular attention to the even more complicated parts of the home buying experience: mortgage, title, and home insurance. We'll give you an overview of the industries, with particular attention to how you can get engaged in your transactional process with the goal of having a better overall experience.

The Guide is divided into three parts:

- **Part One:** Getting a Mortgage, with ten chapters that explain the fundamentals of the mortgage process and guide you through your application all the way until you get your "clear to close."
- **Part Two:** Getting Title Insurance, with an explanation of what title insurance is, and a helpful guide to avoiding title report pitfalls that can delay your closing.
- **Part Three:** Getting Home Insurance, with a comprehensive overview of your coverage choices, along with some tips on how you can save money.

The Rand Family
Matt, Dan, Marsha, Joseph

Finally, at the end of the Orientation Guide, you'll get some advice to prepare you for the closing costs you'll need to cover at the end of your home buying process.

We hope you find the Guide helpful, and we encourage you to work with the professionals at Hudson United for your mortgage, title, and insurance needs. As the owners of Better Homes and Gardens Rand Realty, we've applied the same commitment to excellence to these companies that we used when building a great real estate company. And just like with Rand Realty, you get a local, family run company, dedicated to the people and the communities in our area.

A Better Transaction with Hudson United Home Services

Real estate transactions are complicated, with a lot of moving parts: real estate brokerage, mortgage lending, engineering inspection, legal representation, title insurance, and home insurance. Unfortunately, those parts don't always work so well together. And when they don't, what we often think of as the "American Dream" becomes more like a nightmare.

Indeed, as the owners of Better Homes and Gardens Rand Realty, it has long been frustrating to see clients who otherwise had a wonderful service experience working with their Rand agent ultimately come out of the process miserable and unhappy – not because of anything their agent did, but because the rest of their transaction was so mishandled. The clients might have been thrilled by the work performed by their agent, but walked away from the deal with a sour taste because of transactional delays associated with mortgage processing or title work.

That's one of the reasons we are delighted to be affiliated with the Hudson United family of home service companies, which provide mortgage lending, title insurance, and home insurance to many of our real estate clients. Perhaps we are "control freaks," but we are passionate about providing our clients with an outstanding service experience, and we have found that we cannot ensure that experience without taking greater control over those moving parts of the transaction.

So we're happy to recommend the Hudson United family of home service companies:

- **Hudson United Mortgage.** Our full-service mortgage brokerage has access to any financial product you might need, and our mortgage officers are available to help guide you through the financing process right from the initial pre-qualification.
- **Hudson Abstract Services.** Our title insurance operation is one of the leading abstract companies in the region, closing almost 1,000 transactions every year without a meaningful adverse claim from its inception over 10 years ago.
- **Hudson United Insurance Group.** Our insurance company can provide you not only with the homeowner's insurance that you'll need at your closing, but with any policies you need, including auto coverage.

Most importantly, by putting all the moving parts of the transaction (literally) under one roof, we're able to provide you with an integrated and seamless one-stop shopping experience that had long eluded our real estate clients.

Part 1:
Everything You Need to Know About Getting a Mortgage with Hudson United

The hardest part about buying a home is getting a mortgage. For the most part, you will actually enjoy the home buying process: looking at homes is like "shopping," and most people enjoy shopping. Looking at homes online, going on showings with your agent, getting to know the different areas and neighborhoods – those are all the fun parts about buying a home.

But getting a mortgage is the hard part. It's messy, complicated, and often intimidating. You'll have to maneuver your way through all the different mortgage products, and then once you actually start your application process you'll have to endure a detailed examination of your financial profile and spend a lot of time tracking down documents to complete your file. Even in the best of situations, the mortgage process is difficult and often frustrating.

That's why we want you to be prepared. As you'll see, that usually means getting engaged in the process, and immediately starting to gather the information you'll ultimately need for your mortgage application. Another part, of course, is being fully educated and informed about the entire process, from your first consultation, to your application, to getting a "clear to close" on your file. That's why we've put together this guide to getting a mortgage, with a comprehensive overview of everything you need to know about the process:

Chapter 1: Getting Prepared For Your Mortgage Process

Chapter 2: Your Initial Consultation: How to Get Prequalified

Chapter 3. An Overview of Mortgage Products

Chapter 4. An Overview of Mortgage Features

Chapter 5. Qualifying for a Loan

Chapter 6. Understanding Interest Rates

Chapter 7. Your Loan Application

Chapter 8. Commitment Issues

Chapter 9. Dealing with Appraisals

Chapter 10. Conclusion

We hope that you are able to review this *Orientation Guide*, and that it helps you navigate your way through the mortgage process.

Overview of the Mortgage Process

Initial Consultation.
You'll meet briefly with your loan officer and get a pre-qualification letter to advise you of your general price range.

Application.
Once you find a home to purchase, you'll complete a formal mortgage application to your lender.

Processing.
Your loan processor, working with your mortgage officer, will review your file and probably contact you about supplementing it with some supporting documentation.

Underwriting.
Your processor will submit the file to an underwriter, who could deny or approve the application, but will more likely issue a "conditional commitment" required more documentation or clarification.

Clear to Close.
Once you have satisfied all the conditions, your bank will issue a commitment letter and you will be "clear to close" your transaction.

Getting Prepared for Your Mortgage Process.

Be engaged. Be proactive. Be responsive. If you've read our Better Homes and Gardens Rand Realty Buyer Orientation Guide, you know how important we think it is for you to be deeply invested and involved in your home buyer experience. And while that's true throughout your transaction, it's particularly important for your mortgage process. If you're actively involved throughout that process, and if you start planning ahead now, you'll have a much better experience getting a mortgage.

How can you be more engaged, so that you are better prepared for the mortgage process? Here are a few suggestions::

Consult with a loan officer right from the start.
At Hudson United Mortgage, we encourage our clients to meet with a loan officer right at the beginning of their home search, because even a short consultation can answer your questions about the current rate environment, assuage some of your concerns about the process, and also help you get a better sense of your buying power. Too many buyers start looking for a home without a clear idea of how much they can afford, and they waste a lot of time looking at homes that are above, or below, their actual price range.

Get a prequalification letter from your loan officer.
A prequalification letter is a statement from your loan officer indicating your buying power – how much home you can afford. Not only is the process of getting the letter important, because it allows you to sit down with the loan officer to go over your financial profile, but a prequalification letter is also crucial for establishing credibility with sellers.

Start collecting and saving your financial documents.
As your loan officer will probably explain, your lender will ultimately require you to produce several months' worth of pay stubs and bank statements as part of your initial loan application. You can save yourself a lot of time and stress by starting the process of collecting those documents immediately. As they come in the mail, put them aside in a special file so that you can easily pull them together for your loan officer when you need them. And if they are available online, make sure to print them – every single page (even the blank ones!)– every month and store them.

Don't do anything to dramatically change your financial profile.
When you do your initial consultation with your loan officer, your prequalification letter will be based on the financial profile you present: your assets, income, credit, and debts. Any changes in that profile are likely to impact your buying power, and can often send up "red flags" during your mortgage application process: things like new credit card accounts, major purchases on credit, large deposits or withdrawals from your bank accounts, or changes in your employment. Now, you still have to live your life, so sometimes these things are unavoidable, but at least be aware that any sort of modification to your finances could change your buying power and will likely complicate your application process.

Stay in touch.
Don't have that initial consultation with your loan officer at the beginning of your home buying process, and then disappear until you've reached an accepted offer and now want to file a loan application. It can take a long time to find the right home, and much about the financing environment can change in the meantime. Keep in touch with your loan officer: get an update on what's going on in the lending market, find out what's happening with rates, and keep him or her appraised of where you are in the process. Your loan officer is a great resource for you during your home search, so don't be reluctant to take advantage of what he or she can offer.

Your Initial Consultation: How to Get Pre-Qualified

Getting prequalified is an important first step in your overall home buying experience. Not only will it help you narrow down your price range, but it will also give you credibility in the eyes of sellers and listing agents.

Maintaining Your Financial Profile

Here are five ways to keep your financial profile consistent and prepare for the loan application you'll ultimately be submitting to get your mortgage.

Store your bank statements and pay stubs.

You'll need those for your loan application, and it takes forever to get new statements and stubs from your bank or employer if you misplace them.

Keep your credit clean.

Don't buy anything big on credit, because any major purchase can completely change your credit profile and impact your rate and buying power.

Maintain steady account balances.

Don't move too much money around. Any major deposits or withdrawals are going to send up "red flags" to your lender. You want to show consistent account balances over time.

Stay at your job.

You'd be amazed at how many people quit or change jobs while they're in the middle of applying for a loan. Any changes to your employment situation are going to complicate your loan process, and set you back months until you build up a new income record.

File your taxes.

Your bank is going to want to see recent tax returns, and it will slow you down if you still have to prepare and file your old returns.

At your initial consultation with your loan officer, you should be prepared to discuss in some detail your financial situation. Remember that loan officers, at least the ones with Hudson United, are under strict licensing requirements to protect the privacy of your information and keep your confidences, so you should feel free to discuss your personal situation without holding anything back.

Here are some of the issues your loan officer can address with you at your initial consultation:

- **Price Range.** By going over your financial profile, your loan officer can give you a much better sense of your price range. The loan officer will review your income, savings, recurring debts obligations, and your credit score, and will probably have some other questions for you, but at the end of a very short consultation you'll understand how much home you can afford.

- **Interest Rates.** Your loan officer can tell you about the current interest rate environment: where rates are, and even where the industry expects rates to go. You will not be able to "lock in" a rate until you are much further along in the process, when you are actually applying for a loan after you have found a home to buy. But at least you'll be able to get a sense of your buying power in the current and foreseeable rate environments.

- **Mortgage Products.** You can get an overview of the mortgage products that are available to you, not just standard mortgage loans but any special programs for which you might be eligible. By reviewing your financial profile and your long-term plans and goals, your loan officer will have some good suggestions about the types of loans that would be best for you.

Most importantly, by having that initial consultation with your loan officer, you'll be able to get a pre-qualification letter: a statement on the bank's letterhead indicating that you have been "qualified" for a particular price range. Now, you should be aware that a pre-qualification letter is not a firm commitment from the bank – you won't get anything like that until you complete and submit a formal loan application, which you cannot do until you actually find a home to buy. Rather, the pre-qualification letter is really just a general indication of your buying power.

But the pre-qualification letter is still important for two major reasons. First, it will allow you to go through the process of discussing your financial situation with your loan officer, which will ensure that you have a good sense of your true price range before you go out and start looking at properties. Second, and perhaps more importantly, a pre-qualification letter from a reputable lender like Hudson United is almost a "stamp of approval" for sellers and listing agents. In a competitive environment for buyers, a pre-qualification letter indicates that you are credible and serious, and that you have the general financial wherewithal to back up your purchase offers. Indeed, many

sellers demand a pre-qualification letter before they will even consider your offers!

An Overview of Mortgage Products

What's the difference between a conforming and non-conforming loan? What are FHA loans? What's a jumbo? In this chapter, we break down all the different loan types, and explain what you need to know about the different products available to you.

Although you will not be selecting a particular type of mortgage loan until you are much further along in the process, it's helpful to get a general sense of the products that are available and the choices you'll have to make when you find a home and get ready to apply for your loan. We're not going to delve into the full range of all the esoteric and exotic loan products that are available. Rather, we just want to introduce you to the basic loan types that are appropriate for most buyers.

Conventional Loans: Conforming, Conforming-Plus, and Jumbo

Most people have a basic misunderstanding about the lending industry. Specifically, they usually believe that loans come from banks, which take in money from deposits, pay a small bit of interest to the depositors, and then loan that money out to borrowers for a slightly higher rate of interest. Like in the old movie It's a Wonderful Life, where Jimmy Stewart explains to a customer trying to close his account that the "old Building and Loan" doesn't actually have his money on deposit: "You're thinking of this place all wrong. As if I had the money back in the safe. The money's not here. Your money's in Joe's house...right next to yours."

It's a lovely thought, and at one point in our history it was actually true, but it's no longer how the system really works. As many of us discovered during the financial crisis of 2008, most lenders don't actually hold onto mortgages once they make the loans to borrowers. Rather, they take those loans and sell them to investors, who pay the lender a premium for the right to collect the interest payments on those loans for the remainder of their term. Those investors make up what's called the "secondary market," which provides the demand for mortgage loans throughout the industry. Regardless of where you get your financing – whether it's a nationally charted bank or a local mortgage broker -- your loan will probably end up being owned by one of the investors on this secondary market.

The most important secondary market investors are the government-sponsored entities known as "Fannie Mae" and "Freddie Mac," which ultimately buy most of the home loans made in this country. These agencies are designed to promote liquidity in the market by creating sufficient demand for home loans, thereby incentivizing lenders to give mortgages. They also set certain guidelines for the loans that they will accept, which have ultimately shaped how the mortgage industry fashions its underwriting standards – the banks want to be able to sell their loans to Fannie and Freddie, so they adhere to the guidelines in setting their own internal standards.

Most importantly, Fannie and Freddie are restricted in the size of the loans that they can purchase, which has created the general categories of loans known as conforming, conforming-plus, and jumbo:

Conforming. Conforming loans are those that follow agency guidelines and are made below the

Servicing Your Loan

Most secondary market investors don't "service" their own loans. That is, they don't collect monthly payment checks or send out notices to the borrowers. Rather, the investors hire third-party service companies to manage their loan portfolios. So regardless of who owns your loan, your main relationship will be with the "servicer" to your loan – the company that sends you payment notices, and to whom your write your monthly mortgage payment check.

loan limit, which is currently set at $417,000 for single-family homes. Because conforming loans are "backed" by Fannie and Freddie, the secondary market demand is high, and they generally carry the lowest available interest rate. Conforming loans are also sometimes called "agency loans" or "conventional loans."

Conforming-Plus. In 2007, in response to some weakness in the secondary market, the government raised the conforming loan limit in certain high priced areas, including many of the markets in the New York City area. This "conforming-plus" loan limit is now set as high as $625,500, depending on the location. Loans made between the conforming loan limit and the higher conforming-plus limit are known as "conforming-plus loans," and might also be called "conforming jumbo," "agency jumbo", or "conventional-plus" loans. Even though conforming-plus loans are backed by Fannie and Freddie, they generally carry slightly higher interest rates than what is available for traditional conforming loans below the $417,000 limit.

Jumbo. Loans above the conforming loan limit, or even the conforming-plus limit in higher-priced markets, are called "jumbo" loans, and they are generally available only at higher interest rates. Because Fannie and Freddie don't purchase loans above the conforming loan limit, the secondary market for those "jumbo" loans is much smaller, which reduces demand for those loans. And since demand is lower, investors on the secondary market require a higher rate of return to purchase those loans. Accordingly, borrowers getting a non-conforming or jumbo loan generally have to pay higher interest rates than if they were getting a conforming or conforming-plus loan.

FHA Loans

In addition to the conventional financing options described above, borrowers can also take advantage of an increasingly popular product offered by the Federal Housing Administration ("FHA"). FHA loans are directly insured by the federal government, which reassures lenders that they will be made whole even in the event that the borrower defaults on the loan. Accordingly, the loans, while slightly more expensive than conventional financing, are available to a wider pool of buyers, and are often appealing options for first-time home-buyers, borrowers with weak credit histories, or people with a relatively small down payment.

For these types of borrowers, the FHA loan can have some distinct advantages:

- **Lower down payments.** Conventional loans require at least a 5% down payment, and usually demand significantly more than that, but FHA loans are available with as little as 3.5% down.
- **Broader qualifying guidelines.** The FHA qualification guidelines are a bit more flexible than the standards required by Fannie and Freddie, so some borrowers who would not qualify for conventional financing (i.e., because of their income-to-debt ratio) can obtain FHA loans.
- **More forgiving credit requirements.** FHA loans also have more flexible credit standards, allowing borrowers with weaker credit to still qualify for a loan.

All this flexibility, though, comes at a price. FHA loan interest rates are generally a bit higher than for conventional financing, so your loan will be a little more expensive. More significantly, the government insurance that makes these loans possible comes at a fairly high cost. Borrowers getting an FHA loan have to pay a "mortgage insurance premium (MIP)" up front when they get the loan, and then in their monthly payments for at least several years.

And the MIP is not cheap. The up front MIP can be as high as 1.75% of the value of the loan, although it does not have to get paid when you take out the loan – it gets added to the loan balance. Additionally, you'll need to pay a monthly insurance fee along with your regular mortgage payment, which can be as high as 1.25% of your loan amount. You'll generally pay that MIP until enough time has passed and you have built up sufficient equity in your home.

Accordingly, most people who qualify for conventional financing, or who can afford a relatively high down payment, will opt to get a conforming, conforming-plus, or jumbo loan. Generally, the extra cost of the MIP, and the higher

interest rate, makes the FHA a less appealing choice if you have the option. But if you can't qualify for conventional financing, or you only have enough for that 3.5% down payment, an FHA loan can make the difference between renting and buying.

VA Loans

If you are a veteran of the armed forces, you might also qualify for a VA loan, which is a variation of the FHA loan that eliminates some of the more costly requirements like the MIP. The VA loan is a terrific program, so be sure to ask your Hudson United loan officer if you think you might qualify.

An Overview of Mortgage Features

Should you get a 15- or 30-year mortgage? What about a fixed- or –adjustable rate? How much down payment do I need? All these questions get answered in this overview of mortgage features.

Regardless of your loan type, you still have a number of choices in fashioning your particular product: the term of your loan, whether to get a fixed or adjustable interest rate, your down payment, and more.

The 15- and 30-Year Mortgage Terms

One of the most important decisions you'll make is the term of your loan – whether you want to set the amortization schedule for 15 or for 30 years, which are the two standard terms offered by most lenders. The choice of loan term is really an intensely personal decision, depending on your short-term cash flow needs and your long-term plans. But to give you a general sense of your options, we'll review the major differences between the 15- and 30-year loan, and some of their relative advantages and disadvantages.

Here are some of the advantages of the 15-year loan:

- **Lower interest rate.** 15-year mortgages generally carry a lower interest rate than a comparable 30-year mortgage, because lenders are willing to take a reduced return over the shorter amortization period. The difference is generally about a half-point.

- **Faster Principal Repayment.** Because you're paying the loan off over a shorter period of time, you will pay back your principal and build equity more quickly. For example, over the first five years of a $100,000 loan with a 4% interest rate, you'll pay back about 27% of your principal on a 15-year loan, and only about 10% of your principal on a 30-year loan.

- **Lower Overall Cost.** The 15-year mortgage will have a lower overall cost for the life of the loan, because you will be paying interest for a shorter period of time. For instance, for a $100,000 loan at 4.0%, a borrower with a 15-year amortization will pay out about $133,000 over the life of the loan, while the 30-year borrower will end up paying over $170,000 over the longer period. Now, very few people live in the same home and keep the same loan for the full 15- or 30-year period, but even if you sell or refinance in that time you'll still have lower costs with a 15-year loan.

So the 15-year note will generally confer a lower interest rate, help you build equity more quickly, and lower the overall cost of the loan. But the 30-year mortgage also has certain advantages:

- **Lower Monthly Payments.** The monthly payments for a 30-year mortgage are going to be lower, because the loan amortizes over a longer period of time. The payments are lower even if the 30-year loan is at a higher interest rate. For example, on a $100,000 loan, the payment for a 30-year loan at 4.0% is $477/month, compared to a $715/month payment for a 15-year loan at 3.5%.

- **Higher tax deduction.** For many borrowers, the faster principal repayment of the 15-year mortgage is actually a negative, because a greater proportion of every mortgage payment will be principal rather than interest. Because the home mortgage deduction only applies to the interest on the mortgage, not the principal repayment, the 30-year note provides a larger tax benefit. Indeed, for the first few years of a 30-year mortgage, the monthly payments consist almost entirely of tax-deductible interest.

- **More flexibility.** Some borrowers like the flexibility of the 30-year amortization schedule, because it keeps their monthly obligations lower while still allowing them to make "extra" payments against the principal of the loan. Some financial advisers say that getting a 30-year amortization, but making one extra payment against principal every year when possible, provides better long-term benefits than the 15-year note.

As you can see, the 15- and 30-year mortgage terms both have benefits and drawbacks. Again, the choice is really up to you, based on your own situation: your own risk preferences, your long-term goals, and your short-term cash-flow needs.

Fixed or Adjustable-Rate Mortgages

Another decision you'll be making with regard to your mortgage is whether to get a fixed- or adjustable-rate loan. Very simply, a fixed-rate loan is one in which the interest rate is guaranteed to remain the same for the life of the loan. You take out the loan at 4.0% interest, and you'll pay that 4.0% interest rate for as long as you have the mortgage.

The advantages of the fixed-rate mortgage are obvious. You get the certainty of knowing exactly what your mortgage payment will be as long as you own that home, and you completely eliminate any interest rate risk during the entire term of your loan. From a financial perspective, a fixed-rate mortgage is also a nice hedge against inflation, which will make your locked-in payments look even more affordable over time. And having a fixed interest rate is particularly attractive in a historically low-rate environment like the one we have been enjoying for the past decade, especially with the anticipation that rates are likely to rise in the coming years. It's certainly tempting to lock that rate in for 30 years and be done with it.

Alternatively, many borrowers opt instead for an adjustable-rate mortgage (ARM), where the rate can change over time. An ARM is fixed for a certain period of time -- typically for one, three, five, or seven years – but can then rise according to the terms of your loan agreement, usually based on the movement of a particular benchmark index. Adjustable-rate mortgages are significantly more complicated than fixed rate loans, with terms that can vary widely. Some can adjust every year, others more infrequently. Some can go up indefinitely, and others are capped for each change.

The advantage of the ARM is simple: you will get a much lower interest rate than you could get for a fixed-rate product. Lenders prefer adjustable rate mortgages, because it reduces their own interest rate risk, and they're willing to extend much lower rates for those initial terms. The rate difference will depend on your fixed term -- the longer you fix the rate, the narrower the difference between the ARM and a fixed-rate loan. And because your rate will be lower, your payments will be lower. Indeed, in many cases, buyer who would not qualify for a fixed-rate financing can get a mortgage on an adjustable-rate basis.

The disadvantage of the AMR, though, is obvious: you're exposed to interest rate changes over the life of the loan. If you're not planning on living in that home for longer than the fixed-rate period, then a ARM can be a great way to lower your monthly payments and your overall cost of ownership. But if you think that this might be the home for the long-term, you're probably better off with a fixed-rate mortgage, particularly when you can take advantage of the historically low interest rates available right now. After all, over time, you'll find it enormously satisfying to have a really low interest rate on your home mortgage when everyone else is getting loans at two or three points higher than yours.

Down Payment and PMI

All loan types require borrowers to invest some of their own money in the home in the form of a down payment. Banks like to know that you have some "skin in the game," and that you won't walk away from your loan obligation without giving up some of your investment. Moreover, the down payment allows the bank to loan you less than the full value of the home, which provides a buffer for the bank's collateral and some protection against a decline in the market.

Generally speaking, the ideal down payment amount is 20% of the purchase price. If you can pay 20% down, you'll probably get the best rate and terms available for that mortgage product.

But you still have options even if you can't afford that 20%. FHA loans require as little as 3.5% down, and conforming loans are available with as little as a 5%. It's only really the jumbo loans that absolutely require at least 20% down.

If you do put less down, though, you're going to absorb some added costs in your loan. First, you'll have to pay a higher interest rate. Low down payment loans come at a rate premium. If you put down 20%, you get the best rate. If you put down less, your rate goes up. Second, you'll need stronger qualification for the loan: the less you put down, the more qualified you have to be. Banks really do like to see that 20% down as a standard buffer for protecting their collateral, and they will demand a stronger financial profile to issue the loan.

Third, and most importantly, if you put less than 20% down, you'll have to pay for private mortgage insurance (or PMI). PMI is similar to the MIP insurance collected by the government for FHA loans – it's insurance designed to protect the bank in the event of a default. Unlike the FHA loan, though, there's no upfront payment added to the value of the loan. Rather, the "PMI Factor" is simply added to your monthly payment. Generally, PMI costs run to about .5% to 1.0% of the value of the loan, calculated for the year and then paid monthly. So if you take out a $360,000 loan and have a 1.0% PMI Factor, you'll pay $3,600 a year, broken out into an additional $300 added to each month's payment. That money does not go to pay your interest or principal – it's simply an insurance payment requirement by the bank to protect against the possibility you might default on your loan. That's why it's so much better to pull together a full 20% down payment, because you avoid making insurance payments that don't help build equity.

Discount Points

Finally, the last major loan feature that you need to understand is the concept of "discount points." You've probably seen mortgage advertisements offering a loan at, say, "4.0% with 1 point." What's that point? It's basically pre-paid interest -- a fee equal to 1% of the loan amount designed to reduce the rate that you will pay over the life of the loan. So if you're taking out a loan for $400,000 at a particular interest rate with one point, that one point will cost you $4,000 (1% of the loan amount). And if you're paying two points, you'll pay $8,000 (2% of the loan amount), and so on. Because those points are prepaid interest on the loan, they're immediately deductible on your federal income tax.

Why would a borrower want to pay these discount points? Because they want to lower their interest rate over the life of the loan, especially in situations where they plan on staying in the home for a long time. A point might save you as much as .25% on the interest rate, which might be to your advantage if you want to get some immediate tax savings and lock in a lower rate for the long term. On the other hand, if you're trying to keep your closing costs low, or if you don't think you're going to be staying in your home for a particularly long period, you're probably better off with a zero-point loan product that carries a slightly higher interest rate.

We should distinguish prepaid points from the other origination fees that you'll pay when applying for your loan. Lenders might charge you other fees when you take out the loan, but those are generally not tax deductible and do not impact your interest rate – they're just fees associated with the services provided by the lender.

Qualifying for a Loan

Banks will only loan money they believe will be repaid. So how do they figure out how much you can afford? This chapter reviews the fundamental calculations that go into qualifying you for a loan.

Even though you'll be meeting with your loan officer to get a general sense of your price range, it's also important for you to understand the fundamentals of how you qualify for a loan. Not only will you get a better understanding of the process overall, but you'll be able to identify issues that you can address if you want to improve your financial profile and extend your price range.

The qualification calculation is grounded in a simple concept: banks will only loan money if they believe they will be repaid. Everything they do – every number they examine, every document

they request, every form they require – is aimed at reassuring the bank that you are a good candidate for a loan, and that you will not default, leaving them holding the bag. That's why they want to see every aspect of your financial profile, including all of the following:

Income. The starting point for any determination of qualification is your monthly gross income: the amount of money you make every month before taxes. Under standard lending guidelines, banks presume that borrowers can only spend about 28% of their income for their housing expenses – not just their mortgage payment, but property taxes and insurance. For example, if you earn $60,000 a year, which breaks down to $5,000 per month, banks will project that you can only afford to spend $1,400 (28% of $5,000) of that monthly income for your housing expenses. That's called the "front-end ratio."

Debt. Banks also want to know whether you're going to have other significant financial obligations other than your mortgage and housing expenses, so they will take note of your outstanding debts, such as car payments, student loans, or any other long-term obligations. Again, under the standard guidelines, banks presume that borrowers can only dedicate a certain percentage of their monthly income toward paying debts: this is called the "back-end ratio," and is generally set at 36%. So, for example, if you earn $5,000 a month, your back-end ratio is $1,800 (36% of $5,000), which is the maximum amount that banks will allow you to devote to long-term debt. Essentially, then, banks presume that you can afford 36% of your income to cover all your debts, with up to 28% of your income dedicated just to your housing expenses.

Assets. The bank is going to look at your assets in order to determine whether you have sufficient funds to pay a down payment and associated closing costs when you buy your home. Your assets include your bank accounts, investments, life insurance cash value – anything that substantiates your overall financial health. The more liquid assets you have, the greater a down payment you can make, the lower the monthly payments you'll need to cover, and the more home you can qualify for.

Credit Score. The bank will examine your credit score and credit report as a indication of the likelihood that you will pay back the debt. Your credit is crucial for both deciding whether you can get a loan at all, and for determining the interest rate that banks will offer you. For example, the interest rates you see quoted in advertising or the media are always the rates that apply to borrowers with good credit – no one with a poor credit score or a checkered credit report is going to be able to get those rates. So even if your weak credit is good enough to qualify you for a loan, your resulting interest rate might be so high that you'll end up with a much lower price range than your income would justify.

Now that you understand how those four factors -- income, debts, assets, and credit – impact your qualifications for a mortgage, let's just go over one example to illustrate the process. Assume that our borrower earns $120,000 a year, has outstanding student and auto loans of $600 per month, holds assets of about $50,000 that could be put toward a down payment and closing costs, and has good credit. Here's how the qualifying factors play out:

- **Front-end ratio (Income):** At $120,000 a year, our borrower earns $10,000 per month before taxes. A 28% front-end ratio would result in a targeted housing expense of $2,800. That amount is what the bank will presume that she can spend on her housing expenses (mortgage, property taxes, insurance).

- **Back-end ratio (Debt):** A 36% back-end ratio would result in a target for total monthly debt to be about $3,600 – the amount that the bank will estimate that she can spend for her housing expenses and other monthly outstanding debts. Because her monthly debts are only $600, and her front-end ratio allows her to spend up to $2,800 on housing expenses, her back-end ratio is high enough that her debt obligations will not lower her loan qualifications.

- **Down Payment (Assets):** The $50,000 our borrower can afford for a down payment would represent 20% of a loan for $250,000, and 10% of a loan for $500,000.

- **Credit.** Assuming she does have good credit, our borrower will be able to obtain a loan at the best prevailing interest rate. Let's say that the current

interest rate for a 30-year fixed-rate loan in her price range is 4.0%.

So under these conditions, what could she qualify for? Well, let's start with her monthly payment. Although can afford to spend about $2,800 a month for her total housing expenses, we can't just apply that full amount to her mortgage payment because that amount also has to cover her insurance and taxes. So let's assume that in our area, insurance and property taxes would come to about 25% of her monthly housing expenses. So in this case, 25% of her $2,800 would come to about $700 a month for taxes and insurance, leaving her with $2,100 to spend on her monthly mortgage payment.

Now that we know her monthly payment, we need a mortgage calculator to see the loan amount supported by that payment. You can find mortgage calculators at www.hudsonunited.com that allow you to do all sorts of things, including the "How Much Can I Afford" calculator that asks you to input your monthly payment, interest rate, and term. If you do that for the $2,100 monthly payment, a 4.0% interest rate, and a 30-year term, the result is a loan value of $439,868.60. That is, a loan of about $440,000 at 4.0% for thirty years generates a monthly payment of $2,100.

Okay, so now we know how much loan she can afford given her income and debts. We also know that she can put up to $50,000 down out of her assets. Accordingly, if we add her loan amount to her down payment amount, we come to a top line qualification of about $490,000.

Now, all that said, this is all just in theory, and we kept things simple for illustrative purpose. We should set out a few caveats about how our example might play out in the real world:

- **Her low down payment will increase her loan cost.** Although our borrower's income qualifies her for a loan of up to $377,030, she doesn't have enough for a full 20% down payment to put on top of that loan amount. Accordingly, she would have to pay for private mortgage insurance (PMI) on her loan, which would raise the cost of her loan and slightly reduce her borrowing power from what we calculated based on her income and expenses. If the PMI, for example, were 1% of the loan size, that would be about $5,000 per year, or about $450/month, which would be added to her monthly payments and thereby reduce the amount she could borrow.

- **A weak credit score will reduce her borrowing power.** We assumed perfect credit in our example, but if our borrower had a mediocre or poor credit score, her interest rate would be higher, which would make her loan more expensive and reduce her borrowing power.

- **Higher property taxes will increase her housing expenses** Without knowing the actual property she is buying, we can't know precisely what her property taxes will be. We assumed that taxes and insurance would make up 25% of her housing expenses, but taxes in her area and price range might be higher. If so, she will have less to spend on her mortgage payment, which will again reduce her borrowing power. When she goes through the actual qualification process as part of her loan application, she'll have a property to buy and can make a more precise determination of her housing expenses.

- **Some loans allow for a higher back-end ratio.** On the positive side, we assumed that the bank would be following a 36% back-end ratio, which was the total percentage of her income that she could pay for her monthly debt load. But many banks and loan products will extend the back-end ratio to 40% or even higher, which would put her in a position to borrow more on her loan and increase her price range.

In other words, and long-story short, qualifying for a mortgage is complicated. You not only have to figure out your qualifying ratios based on income and debt, but you also have to factor in the impact of changing down payment amounts, credit scores, property taxes, and other factors.

Price Change Shortcuts

Here are some simple rules of thumb to help you figure out your general price range:

1. The 3.5x Income Rule

Take your income and multiply it by 3.5 – that's how much home you can afford, assuming that you can also make a reasonable down payment and have decent credit. (This used to be the "3x" rule, but when interest rates are in the 3-5% range, it's 3.5x).

2. One-Quarter of Income Rule

On the other side, to figure out how much of a monthly payment you can afford, take one-quarter of your monthly income. Assuming decent credit, that's how much you can reasonably spend on your mortgage payment.

If you do want a shorthand way of figuring out your borrowing power, one common shortcut is to simply take your income and multiply it by 3.5 to figure out the approximate range of the loan you can afford. This is really a blunt instrument, and it's no substitute for a thorough examination of your financial profile by a loan professional, but it can be helpful just as a "back-of-the-envelope" way to calculate your borrowing power. Assuming that you have good credit, a low level of debt obligations, and sufficient money for a down payment, it does give you a general idea of your price range. (The multiplier used to be 3x rather than 3.5x, but with interest rates below the 5% range borrowers can afford more based on their income.) For example, if we use that shortcut with our theoretical borrower making $120,000 a year, we come up with a total loan amount of $420,000, which is reasonably close to the $440,000 calculation we made by going through all the complicated ratios.

Ultimately, of course, you should talk about any major issues related to your qualifications with your loan officer. It's particularly helpful to have that discussion early in the process, while you're still looking for a home, because you might be able to take steps to improve your financial profile and strengthen your qualifying position. For example, you might be able to start liquidating assets to raise the amount you have for a down payment, or clear up issues on your credit report to improve your score.

Understanding Interest Rates

Nothing will impact your purchasing power more than the prevailing interest rate. That's why it's so important for you to understand how rates can change your price range, and what you can do to change the interest rate you'll be able to get for your loan.

During your home buying process, you're going to want to pay particular attention to what's happening with interest rates, because nothing will affect your ability to buy a home more than changes in the prevailing rates. Simply put, as rates go up, your monthly payment goes up, and your buying power goes down.

Before we begin, though, it's crucial for you to understand how you are exposed to interest rate risk while you are on the market. When you first sit down with your loan officer, you will get qualified for a certain loan amount based on your financial profile (income, debt, assets, credit) and on the prevailing rate environment. That is, you'll be qualified based on where rates are at that very moment. But that quoted rate has absolutely NOTHING to do with the rate that you will actually be able to get when you apply for your loan. You don't get to "lock in" that rate based on your first meeting with your loan officer, or your prequalification letter. Rather, you will not be able to lock in a rate until you actually apply for a loan, which you cannot do until you are close to getting into contract on your new home.

In other words, you will be exposed to interest rate changes during the entire time that you're looking for a home. And there's really nothing you can do about it. Indeed, any loan officer who quotes you a "guaranteed" rate during your home shopping process is almost certainly misleading you, because no reputable lender can lock in a rate prospectively before an application is filed. That's why you need to be so careful of those advertisements from lenders who quote

you outrageously low rates – what they're doing is seducing you into working with them based on that promised rate, only to pull a "bait and switch" after you actually file an application.

When you file your loan application, you'll be able to lock in your best prevailing rate for a period of time, and can often pay some additional fees to lock in that rate for longer if you feel you need more time. That's something you can discuss with your loan officer, but generally we do not advise clients to pay for an extended lock-in unless rates are extremely volatile and they are dependent on that particular rate to qualify for that loan.

Ultimately, this is something you should discuss with your loan officer. But just remember that you will be exposed to rate changes during the entire time you look for a home, and that an increase in rates could significantly impact your appropriate price range.

How Rates Impact Affordability

We've prepared some tables to show the impact of rates on home affordability. The first measures how changes in rates can impact your buying power – that is, given a particular monthly payment, how much an increase in rates can reduce the loan amount you can get for that payment. The second measures reverses the calculation, showing how increases in rates will raise your monthly payment for a fixed loan amount.

On Table 1, you can see how a change in the rate can impact your buying power. For example, let's say that your qualification calculation indicates that you can afford a monthly payment of about $3,000. At a $3,000/month payment, you can afford to borrow up to $668,085 on a 30-year fixed-rate loan when the prevailing interest rate is 3.5% (you can do your own calculations on the loan calculators at hudsonunited.com). But if rates rose to just 4.0%, your purchasing power for that $3,000 monthly payment would go down to $628,383, a reduction in about $60,000. The rule of thumb is that for every half-point rise in interest rates, your buying power is reduced by about 5-6%. That's why we always caution buyers not to wait to purchase a home on the speculation that home prices might go down – because all it takes is a small increase in interest rates to wipe out the savings you would realize from a decline in the average sales price.

Table 1:

How rate increases affect your buying power: (Based on rates and payments for a 30-year fixed rate mortgage)

Interest Rate	Buying Power For Every $1,000 in Monthly	Buying Power for Every $3,000 in Monthly	Change in Buying Power for each .5% Increase in Interest Rates	Total Change in Buying Power from 3.0%
3.0%	$237,189	$711,567	n/a	n/a
3.5%	$222,695	$668,085	-6.1%	-6.1%
4.0%	$209,461	$628,383	-5.9%	-11.7%
4.5%	$197,361	$592,083	-5.8%	-16.8%
5.0%	$186,282	$558,846	-5.6%	-21.5%
5.5%	$176,122	$528,366	-5.5%	-25.7%
6.0%	$166,792	$500,376	-5.3%	-29.7%
6.5%	$158,211	$474,633	-5.1%	-33.3%
7.0%	$150,308	$450,924	-5.0%	-36.6%
7.5%	$143,018	$429,054	-4.9%	-39.7%

Similarly, Table 2 takes the same analysis from the other direction, measuring the monthly payment you would have to make to borrow $100,000 or $500,000 at half-point increments in interest rates. As you can see, the monthly payment required goes up significantly as rates increase – meaning that you'll pay more for a home when rates rise, even if prices go down a little. For example, to borrow $500,000 would cost you $2,245/month in mortgage payments at 3.5%, but $2,533 a month if rates rose a point to 4.5%. That's a difference of almost $90/month, or almost $1,100 a year. Again, the rule of thumb is that for every half-point increase in interest rates, you'll end up paying about 5-6% more in your monthly payment to borrow the same amount of money.

Table 2:

How interest rate increase affect your monthly payment (Based on rates and payments for a 30-year fixed rate mortgage)				
Interest Rate	Monthly Payment for each $100,000	Monthly Payment for Each $500,000	Payment Increase Percentage for Each .5% Increase from Previous Rate	Total Change in Payment from 3.0%
3.0%	$422	$2,108	n/a	n/a
3.5%	$449	$2,245	6.5%	6.5%
4.0%	$477	$2,387	6.3%	13.2%
4.5%	$507	$2,533	6.1%	20.2%
5.0%	$537	$2,684	5.9%	27.3%
5.5%	$568	$2,839	5.8%	34.7%
6.0%	$600	$2,998	5.6%	42.2%
6.5%	$632	$3,160	5.4%	49.9%
7.0%	$665	$3,327	5.3%	57.8%
7.5%	$699	$3,496	5.1%	65.8%

So given how important interest rates are to your ability to qualify for a loan, it's important for you to understand what affects both your personal interest rate and the rate environment overall.

What Causes Changes in Interest Rates?

So what could spur a change in interest rates while you're actively on the market? Technically speaking, interest rates are determined by the movement of the ten-year United States Treasury bond: when bond yields go up, interest rates go up; when bond yields go down, interest rates go down. But on a more practical level, and as a simpler rule of thumb, the easier way to think about it is that mortgage interest rates tend to rise as overall economic growth picks up – so if the economy starts to strengthen while you're engaged in your home search, you might see rates rise. Here are some of the reasons why economic changes can impact mortgage rates:

- **Government Intervention.** As we write this in mid-2013, the Federal Reserve has been actively working to keep mortgage rates low by investing heavily in securitized mortgage loans. But if the economy strengthens, the Fed would likely feel that it no longer needs to subsidize mortgage rates and would stop buying mortgage loans, which would drive rates up.

- **Inflation.** Interest rates tend to be lower when inflation is low. But as the economy improves, the risk of inflation tends to increase. The rate of inflation has been low over the past few years, at least by historical standards. But if inflation starts to pick up, investors would demand higher rates of return for loaning money, and rates would likely go up.

- **Stock Market.** Generally, the stock market and the bond market compete for investment dollars, so when the outlook for the stock market is weak, investors tend to put money into the bond market, which keeps rates low. But if the economy strengthens, the stock market rallies, and investors will be tempted to take money out of bonds. Again, that would tend to drive rates up.

- **Demand for Financing.** On a practical level, we have seen interest rates go up simply because of an increase in demand from mortgage lenders. When lenders get busy, they sometimes raise their rates (i.e., what is essentially their "price") to both make more money on a particular loan and to reduce their transactional load so their service does not suffer.

Essentially, what it comes down to is that interest rates stay low so long as the economy does not "overheat." But if we start to see significant economic growth, that would tend to reduce government support for low interest rates, drive up inflation, and create a stock market rally – all of which would be associated with higher rates.

Even if you're exposed to interest rates, though, remember that you always have the option to get an adjustable rate mortgage rather than a fixed-rate mortgage. Let's say, for example, that you plan your home search around rates being set at 3.5%, and then once you've gotten into contract rates pop up to 4.0%. You might not be able to afford a 30-year fixed-rate mortgage at that higher interest rate, but you could take the option of an adjustable mortgage that would stay fixed for a number of years at a rate you could afford, particularly if that fixed period would likely cover you through the years you'd be living in that home.

What Affects Your Personal Interest Rate?

Whenever lenders advertise a particular interest rate, they're not talking about a rate that they will offer to every borrower. They're stating the rate that applies to a perfect borrower getting a 30-year fixed-rate mortgage under ideal circumstances. But that's not how the real world works. As you can probably tell from the discussion we've had so far, the interest rate that you can get for your own loan is going to depend on your particular situation, specifically the following factors:

- **Your credit score.** The better the credit score, the lower the rate. Lenders reward you for being a good credit risk.
- **The loan product.** Some loan products carry inherently higher interest rates. For example, conforming-plus, jumbo, and FHA loans all have higher rates than the conforming loan.
- **The type of home you are buying.** The rates for single-family homes are generally lower than for condos, coops, or multi-family homes.
- **The term.** The longer the term, the higher the rate, so the rate on a 15-year mortgage will be lower than a 30-year mortgage.
- **Your down payment.** If you can't afford to put at least 20% down, you'll pay a higher rate. But you generally don't get any rate benefit for putting down more than 20%.
- **Fixed or adjustable rates.** Adjustable-rate mortgages obviously will have a lower starting rate, although they can go up significantly once they start adjusting.
- **If you pay points.** If you pay discount points, you'll reduce the interest rate that you'll have to pay over the life of the loan. This can be a smart idea if you're going to be staying in the home for a long time, taking advantage of that lower rate.

You'll notice that most of those factors are within your control. They either relate to the type of loan you're getting or to your own financial profile. But there's one last factor that will impact your rate but is entirely out of your control – namely, the bank's appetite for loans. Generally speaking, at any given time, most lenders will be offering roughly the same interest rates for similar loan products. Sometimes, though, a lender might decide that it's gotten "too busy," and that a flood of loans is putting too much pressure on its back office. Or the lender might simply decide to try to make more money on each loan, and raise the rates to generate more profit, taking the risk of losing some business.

You'll never know whether the lender you're meeting with is in the position of juicing its rate to reduce its workflow or increase its profits. That's why it's a good idea to work with a broker like Hudson United that has access to multiple banking sources with a wide variety of products and rates. When one bank is raising its price to generate fewer loans at a higher profit margin, a broker can switch you to a bank that is cutting its price to create more demand for its loans.

Your Loan Application

The loan application process is the most difficult and time-consuming part of the home buying experience. It's never going to be easy, but it will be easier if you go into the process prepared for what's coming and fully engaged in working to get your file closed.

Okay, this is where we need you to take a deep breath and relax, because now we're coming to the hardest part of your home buying experience: filing your mortgage application, and dealing with underwriting issues. Right from the start, we warned you that going through the mortgage application and review process will be frustrating and difficult. After all, a mortgage loan is a complex financial transaction that generates a tremendous amount of paperwork, involves numerous service and transactional professionals, and takes a good deal of time.

That's why you need to be relaxed. Even in the best of circumstances -- when you have impeccable credit, sufficient funds in your bank accounts, and all your documentation in order – the mortgage process will be challenging. Even if you've gotten a mortgage before, you'll be surprised at how exacting the banks have become since the financial crisis of 2008. Documentation will be

checked, then double-checked, then scrutinized one last time right before your closing. Your credit history, bank accounts, employment, tax returns – all of them will be reviewed for any discrepancies that might send off a "red flag" to the bank.

So what can you do to make it easier? First, you just need to be prepared for what's going to come. Ultimately, our goal is to highlight the steps you can take to facilitate your process, to make it as easy as possible. Second, we want to emphasize yet again the importance of being engaged and proactive in your home buying process. Indeed, your active involvement in the loan process is crucial for ensuring that you have a smooth transaction. Although you'll have a whole team of professionals to help you along, you're the only one who can do some of the work that will need to be completed to get you to a closing. So the more engaged you are throughout your loan process, the better.

Your Loan Application

Once you have an accepted offer, you'll be able to fill out a formal loan application. Your loan officer will take you through the process and help you gather the necessary documentation to substantiate your file. Although every bank is different, here is an overview of the basic information required in most loan applications:

- **Bank accounts.** You'll need the account numbers for all your bank accounts, including your checking, savings, cd's, money market, and IRA accounts. You'll also need the complete statements for the last three months (even blank pages), and the current balances on those accounts.

- **Loans and credit cards.** For any outstanding loans, you'll need the names and addresses of your creditors, the monthly payments and balances, and the type of loan. This includes loans for your cars, any current real estate mortgages, student loans, and any other type of debt obligations. You'll also need to list all your current credit cards with account numbers and any outstanding balances.

- **Credit History and Current Loans.** You will want to review your credit report carefully, line by line, for accurate balances, monthly payments, account numbers, your past addresses, former and maiden names, etc. Your loan officer should give you a copy of your credit report. The lender will use the info on your credit report to identify your outstanding debt obligtations, so you certainly want that information to be accurate.

- **Employment.** You'll need the names and addresses of all employers for the past two years. You'll also need complete tax returns for the past two years, and two current paystubs. If you're self-employed, you'll probably need your corporate tax returns for the past two years, and a year-to-date profit-and-loss statement.

- **Real Estate.** If you own any real estate, you'll need to list the properties, their value, their lease terms (if leased), and the carrying costs for the property, including mortgage payments, taxes, insurance, HOA fees, etc.

Obviously, pulling all that information together can take time. That's why we recommend you start gathering the necessary documents as soon as possible, to avoid any unnecessary delays in submitting your application. And be sure to keep all this information in a central file folder at the ready.

Your Loan Processor

Once you have completed your application, your loan officer will submit it to your loan processor. The processor is the person responsible for performing a rigorous review of the application to prepare it for underwriting, and will ultimately be responsible for shepherding you through the rest of the underwriting process. You will become very familiar with your processor, who will be your key point of contact as you go through underwriting, and who will be regularly communicating with you to give you updates on what is happening with your file. You should absolutely take down the name, number, email address, and phone number for your processor and add it to your phone list, because you'll need to be in regular contact.

When your processor gets your application, he or she will review it to see whether you need any additional documentation or information. If so, the processor will contact you to get what's needed. Then, once the application is finalized and complete, the processor will submit it to the bank's underwriter for review. Most likely, you won't meet or ever speak directly with the

CORE Client Connect

One of the real advantages to working with Hudson United Mortgage is our CORE Client Contact system, which sends you email alerts throughout your mortgage process to let you know what's happening with your file. These alerts can help reassure you that progress is being made, tell you what is still needed, and eliminate the feeling that you don't know what's happening with your file.

underwriter, because your processor, and to some extent your loan officer, will act as your intermediary. But it's the underwriter who reviews the file, follows the lender's guidelines for extending financing, and makes a determination on whether to grant you a "loan commitment" -- the lender's promise to give you the financing that you have requested.

Getting a Commitment

From this point, three things could happen. The lender could either: (1) deny your application, giving you a reason why the lender will not extend you an offer to finance; (2) grant your application and issue you a loan commitment, or (3) give you what's called a "conditional commitment," listing a series of requests for further information needed in order to make a full and final financing commitment:

- **Denial.** Most likely, unless your file is completely outside the lender's guidelines, you won't get an immediate denial. If it does happen, though, then your loan officer and processor will probably work with you to make an application to a different lender, so long as the reason for your denial has something to do with the inherent underwriting practices at that specific lender. Different lenders have different standards and products, so often an application rejected by one bank might be acceptable to another. So a denial doesn't mean that you cannot get financing at all, just that this particular application did not go through.

- **Commitment.** Similarly, you're also unlikely to get a formal loan commitment right off the bat, simply because it's unusual to make an application that is so "clean" that the bank will not have some type of follow-up requests. Most of the time, even if the lender is well-disposed to your application, you will still have at least a few conditions that you have to meet in order to get a final commitment.

- **Conditional Commitment.** That's why most borrowers who file applications get what's called that "conditional commitment," which is a letter from the lender spelling out additional requests for information or documentation, or requesting clarification of an issue that popped up during the review of the file.

The key to satisfying the conditions of the commitment and getting you to the closing table on time is simple: it's all up to you. You're the one who has the information that the lender wants, so it's really in your hands to move the process forward quickly and efficiently. Your processor will guide you through it, and will take the lead in getting whatever's needed from third parties, but in many cases you're the only person who can move the process along.

Finally, once you have satisfied all those conditions, you will get an updated commitment letter with no conditions, which is the lender's promise to give you financing on the specified terms. This is commonly called "clear to close." At this point, your mortgage process is complete, and your attorney can set a closing. But note that even with the commitment letter, the bank still has the authority to do final checks of your credit, employment, and other terms of your application before closing, so issues could still pop up at the last minute.

Commitment Issues

When transactions are delayed going into contract, you'll almost always find that the buyer is dealing with conditional commitment issues that were raised by the underwriter about the application. How you deal with those commitment issues can make the difference in making your closing on time.

Why does it take so long to get from contract to closing? Generally speaking, it comes down to two issues: (1) the seller clearing issues on the title; and (2) the buyer clearing conditions on the mortgage. And while the seller is busy fixing

problems that come up on the title report, you'll be dedicating most of your time to tracking down the documentation you need to satisfy the conditions placed on your bank commitment. That's why it's so important to be engaged and proactive in resolving those commitment issues: they may be, and often are, the biggest obstacles to getting to the closing table.

Basically, the commitment conditions usually come down to clarifications about your financial status. The bank wants to make sure that you're using your own saved money for the down payment on the home, and that you're a good credit risk. And to make that determination, the bank will be tying down any loose ends that come up in the review of your initial application: any questions about your bank accounts, credit history, source of funds, and other aspects of your financial profile.

General Guidelines

Here are some guidelines to keep in mind if you want to move through the process more quickly.

- **First, respond quickly to requests from your processor.** If the underwriter wants to see a particular document, then you need to produce it. The request isn't going to go away on its own. The quicker you are in tracking down the items needed, the faster you'll get a clear-to-close.

- **Second, be careful about making any changes involving your financial profile.** The bank's decision to extend you financing depends on the state of your finances when you make the application, and if you do anything that impacts your employment, bank statements, or credit history, you're going to send up red flags and set yourself back weeks or even months.

- **Third, keep updating your file, particularly your bank statements and pay stubs.** Processing your mortgage application may take months, but lender guidelines require fresh statements and stubs. So you'll need to keep updating your file. Keep a separate file folder for all your financial-related mail, and be ready to send it to your processor upon request. And when you submit your paperwork, provide ALL PAGES of the statements and stubs – not just the cover page. The bank wants to see it all.

Ten Common Commitment Issues

More specifically, we've identified below 10 common issues that come up during the commitment process that can delay your ability to get to a quick closing. We'll describe each of the problem areas, and try to explain how you can either avoid the issue or fix it when it crops up.

1. Changes in Your Bank Statements

You want to be careful making any major deposits or withdrawals from your checking and savings accounts in the months leading up to your mortgage application. Any major withdrawals, other than the money you take out to make a down payment, are going to require follow-up documentation and clarification as to the purpose for the withdrawal. Similarly, if you make a large deposit into your account that's not from your normal salary or other income, you'll raise an issue of whether that money is a gift or a loan that you will have to pay back. That's a big red flag to the lender, who doesn't want you to have additional debt obligations to some third party to pay back the down payment when you're already trying to pay your monthly mortgage payment. So try not to make any large withdrawals or deposits, and be prepared for follow up requests if you do.

2. Changes to Your Credit

Right from the beginning of your home search process, we have warned you not to do anything that would impact your credit while you prepare to buy a home. Well, that's even more important now. Don't take out any new credit cards. Don't buy anything major on credit (like a new car!). Don't fall behind on any of your payments. Don't even close existing accounts. Anything you do on credit will impact your credit profile and could slow down your loan process.

3. Credit Issues

You might have credit issues that you need to resolve for the lender. For example, if you are disputing a credit card balance the bank will want you to settle that dispute before you close, so you're going to need to clean those up. You might also have to explain issues like late payments in your credit history with an explanatory letter.

4. Changes to Your Employment
Don't quit your job. We know that seems like very obvious advice, but you'd be amazed by how many people quit their jobs while they're trying to get a mortgage. Obviously, quitting your job is going to put a major obstacle in your mortgage process, and might result in you getting denied. But even just changing jobs in the middle of your application can cause you months of delays, because the bank is going to want to see updated pay stubs from your new employer. We know that you have to live your life, and your mortgage is not the only thing you have going on, but do try to avoid major job changes while you're trying to get your loan approved.

5. Proof of Self-Employment
If you are self-employed, you can expect to see certain conditions regarding proof of your personal income. The bank will want to know that your self-reported income is legitimate, so you might have to provide your business tax returns or even a profit and loss statement. This can seriously delay your application if you have not yet filed the returns, or if you don't have statements already prepared by your accountant.

Co-op or Condo Approvals

If you're buying a condominium or cooperative apartment, you are likely to have additional commitment issues come up regarding approvals for the building. Not only will you need the bank to investigate to ensure that the condo or the coop is eligible for financing (not every building is), but you will also need to show the bank your condo or coop board approval. Often, condo and coop buyers will have everything else completed, but will wait impatiently for the building's board to meet to approve their application. So, as always, start that process as early as possible.

6. Verification of Employment
Another employment issue that comes up a great deal is the verification of employment (VOE) that banks will conduct on every file. You would think this would be a simple matter, but we often find it difficult to get client employers to return phone calls and provide documentary proof if needed to show that you actually work there. You can make it easier if you provide your processor with a name, phone number, and email address of someone at your company with the authority to confirm your employment and salary. If you work for a large employer, it's best to get a live contact in the human resources department; for small employers, the owner or manager would be best.

7. Tax Returns.
Again, this is a simple thing, but you'd be amazed at how many borrowers do not have copies of their most recent tax returns, or who haven't filed for a recent tax year. The bank is going to want to see those returns, so you will need to track them down or get your previous year returns filed.

8. Sourcing of Gifts
If you are getting part of your down payment as a gift, you will need to provide documentation to prove that the money is not really a loan. You can usually accomplish this with a form letter from the giver attesting that you do not need to pay the money back. The bank needs to see this for fear that you will be taking on too heavy a debt burden, and will have problems paying back both the "gift" and the mortgage loan.

9. Home or Title Repairs
Sometimes, the inspection or title report will turn up problems that have to be resolved for the bank to finalize the loan. Usually, you really can't do much about these problems, since you don't own the home, so your only recourse is to badger the seller through your attorney into fixing the problem. Ideally, you will get the title report quickly so that the seller can work on clearing the title while you're resolving the other outstanding conditions on your loan. That's why it's so important to order title early in the process.

10. Investment Property
If you already own investment property, you will have to reassure the bank that you can afford to buy a new home while still maintaining that investment. Usually, you will need to provide extensive documentation regarding your investment, including mortgage paperwork and rental leases. If you do own investment real

estate, you should keep that documentation handy, because you will certainly need it during the process.

Conclusion

It's very likely that you will have "commitment issues" on your file. The important thing is to respond to documentation requests from your processor as quickly as possible, so you can address and resolve those issues as soon as possible.

Dealing with Appraisals

Appraisals can be one of the most frustrating aspects of your home buying experience, not only because they can "make-or-break" your deal but because the results of an appraisal are mostly outside your control. As always, though, it helps to be prepared for what might happen.

Once you have submitted your application, the bank will order an independent appraisal of the home to determine whether the value of the property justifies the loan amount. The licensed appraiser will visit the home, look through recent sold data, and render an opinion as to the home's value. Your real estate agent will often try to help the appraisers along by providing them with information on recent comparable home sales that justified the price you're paying for the home. But neither your agent nor your lender are allowed to try to "influence" the appraisal, so they have to walk a fine line between providing helpful information and advocating for a particular appraisal value.

The appraisal is a crucial step in securing final approval for your mortgage. If the appraisal comes in at or above your purchase price then the bank will be reassured that it has sufficient collateral for the loan. But if the appraisal comes in low, you're going to have a problem getting bank approval..

Of course, if the appraisal comes in low, your first reaction might be to wonder whether you're overpaying for the home. That's a normal response, but we want to caution you that an appraisal is simply one person's opinion. Basically, appraisers do the same thing you do when they're valuing a home: they look at recent sold comparable properties, and make adjustments for differences in condition or amenities. So don't start to question the price you agreed to pay just because the appraisal comes in low. After all, you just completed an arms-length negotiation with a seller on the open market – your price reflects true market value. Unless you made your offer without regard to what was happening in the market, it's most likely that your price is accurate and the appraisal is coming in too low.

So why do appraisals come in low? Here are some of the reasons:

- **Bad appraisers.** Unfortunately, some banks, particularly lenders from outside the area, also have appraisers from outside the area. And you can imagine what happens when you bring in an appraiser who doesn't really have a feel for local market conditions. (That's another reason why you should use a local lender for your mortgage needs.)

- **Distressed properties.** It might be that a number of distressed sales make up the comparable properties used by the appraiser to determine value. A home in foreclosure, for example, usually sells at a significant market discount, and too many such sales can skew the appraiser's analysis of local home values. It's difficult for appraisers to factor in the reduced value of a distressed home, since the appraiser doesn't do onsite inspections of recent sales to see how the condition of the recent comps affected the sale price.

- **Fast-changing market conditions.** If you are buying a home in a rising market, even six-month old comparable sales might be significantly out-of-date. That is, market conditions might have dictated the price you agreed to pay for the home, particularly in a bidding war situation, but the recent sales don't yet justify the price.

Unfortunately, if you get a low appraisal, there's not much your loan officer or agent can do. Federal and state regulations make it difficult for lenders or real estate agents to have direct contact with appraisers. The rules are designed to prevent collusion, but they mostly have the effect of preventing your agent or loan officer from protesting a low appraisal value.

Your best course of action, in fact, might be to request that the bank order another appraisal. Not every bank will do that, and some loan types don't allow it. But if the bank will order another appraisal, it gives you another bite at the apple, and you can be sure that your loan officer and agent will bury the new appraiser in good comps that justify the sales price.

Otherwise, you might be forced to re-start your loan process with another bank. This is always a last-resort option, because you'll be starting from the beginning with a new application. But at the very least, you will have already gathered all the documentation likely to come up in the conditional commitment process, so you'll be better-prepared for other issues that might come up. As a result, your second turn at the wheel might go more quickly.

So if you do get a low appraisal, what do you do? Obviously, one of your options is to simply walk away. Assuming that your contract has a "mortgage contingency" that gives you the right to cancel the deal if you cannot get a mortgage, you might want to withdraw your offer. Again, we caution you not to get cold feet just because you got a light appraisal, particularly in a rising market where appraisers can often be well behind true market value, but if you feel that the valuation has now raised a serious question in your mind about whether you're actually overpaying, you can certainly walk away.

In our experience, though, buyers usually find low appraisals to be an impediment to closing their deal, rather than a justification for canceling their contract. Usually, they want to buy the home, even if the appraisal is a little light, and their goal is to find some way to still get the deal done. If that's your goal, you have several options:

First, you can try to re-negotiate the price of the home. Again, assuming that you have the right to cancel the deal if you cannot get a mortgage, you can approach the seller about reducing the sales price closer to the appraisal price. Now, many sellers won't agree to this, but some recognize that a low appraisal is likely to be an issue with anyone else trying to buy the home — they might be willing to take a slightly lower price to ensure that the sale goes through, rather than put the home back on the market and risk the same problem coming up with the next buyer. It may not work, but it's worth a try.

Second, you can challenge the appraisal with the lender. Many of our borrowers have had success in disputing the results of the appraisal directly with the bank and requesting a second appraisal. Often, a second set of eyes will come up with a different valuation, which will reassure the bank and allow the loan to go through. Your agent and loan officer will help you through the process of making that request, and will likely work aggressively to make sure that the second appraiser has access to accurate and helpful comps. The banks will not always order that second appraisal, and there's no guarantee that a second opinion will be any more helpful than the first one, but it's one possible option.

Third, you can change lenders. If the bank will not order a second appraisal, you can always start the mortgage process fresh with a new lender who will order its own appraisal from presumably a different appraiser. That's always a last-resort option, because you'd be starting from the very beginning with a new application. At the very least, though, you will have already gathered all your documentation, so you'll have a head start in getting through the process a little quicker. Be mindful, though, of your contractual obligations — if you have a mortgage contingency and you're starting a new application, you should talk to your attorney about extending that contingency to cover the additional time you'll need to get through a new mortgage application process.

Finally, you can also just put more money down. The greater the down payment, the more leeway the bank has to approve a loan with an appraised value lower than the purchase price. So if you put more money down, you might get the bank to approve the loan even with the appraisal coming in light. Of course, this might not be something you want to do, or can do given your financial circumstances.

As always, your Rand Realty agent and your Hudson United loan team will be instrumental in guiding you through this process, and will be available to help you work through any challenges that come up in the appraisal.

Conclusion

Ultimately, no matter how well-prepared you are, the loan application process is going to be a trial. You're going to generate a lot of paperwork, you'll have myriad forms to sign, and you're likely to have to dig up and track down documents you haven't seen in months, if not years. And on top of all that, you have to be careful with everything you do, so you don't upset the delicate fabric of your financial profile.

The best we can say is what we always say: be engaged. Be proactive. Be responsive. Be involved. More than ever before, the more engaged you are in the process, the better your experience will be.

We've covered a lot throughout this Guide about getting a mortgage, everything from your initial consultation with a loan officer, to the different type of loan products and features that are available, to the potential challenges you'll face in closing your loan. To sum it all up, here's a simple checklist of "do's and don't's" you should follow throughout your loan process.

Do:

- Meet with a loan officer at the beginning of your home buying process to have a simple consultation.
- Get a pre-qualification letter and keep copies handy for your agent and sellers.
- Create a financial file to keep all your mortgage application documents.
- Start keeping your pay stubs and bank statements in your financial file.
- File your taxes for the most recent tax year, and keep copies in your financial file.
- Stay in touch with your loan officer to keep him or her appraised of your home shopping progress.
- Follow the news on interest rate changes, and contact your loan officer if those changes might meaningfully impact your purchasing power.
- When you start your application, add your processor's name and contact information to your "Contacts" list.
- Follow up on any requests from your processor promptly.

Don't:

- Make any major withdrawals or deposits to your bank accounts if possible.
- Don't take out any new credit cards.
- Don't close any outstanding credit accounts.
- Don't make any major purchases, particularly on credit.
- Don't change jobs.
- Don't quit your job.

Part 2:
Everything You Need to Know About Title Insurance and Your Title Report

One of the major sources of delay for your transaction could come from issues in the title reports created when you order title insurance. Although it's mostly the seller's responsibility to resolve those issues, you should be prepared for the kinds of problems that title reports can turn up.

Once your transaction has gone into contract, you'll find two major congestion points that can keep you from getting to your closing table quickly. The first is on your side of the deal, from the mortgage process: the lender conditions you need to resolve to get an unconditional mortgage commitment. The second is on the seller's side of the deal, because the seller will have the obligation to clear any title problems that turn up on the report generated by your abstract company. This part of the *Hudson Orientation Guide* will explain the fundamentals of both title insurance and the issues that can come out of the title report produced on your potential new home.

Understanding Title Insurance

As part of your purchase, you will almost certainly be required to get title insurance. Not only is this type of insurance necessary to protect your own interest in your property, but your lender will require it if you are getting financing.

What does Title Insurance cost?

Title insurance rates are set by law, so the fees do not vary according to the title company you use. The fee depends on the purchase price and the amount that will be financed, but as a general rule of thumb you can expect to pay about ½ of one percent of the value of your purchase for your title insurance. Remember, though, that once you buy title insurance, you have it for the entire time you own the property. You don't need to keep paying it every year.

Most of our buyers are unfamiliar with title insurance. That's understandable, because title insurance is very different from other types of insurance that you might have, such as health, auto, or home. For one thing, you only have to pay for title insurance when you purchase (or refinance) your home – it's not something that you have to continually renew every year the way that you have to keep paying monthly or yearly for the insurance policies that most of our clients are more familiar with.

Moreover, most clients have difficulty understanding why they need title insurance, mainly because we so rarely hear of cases where people actually made claims on their title insurance policies. After all, we're all pretty familiar with the reasons we need health, auto, or home insurance, because we can all imagine the risks of getting sick, having an accident, or experiencing a house fire. But it's tough to visualize a situation where people would actually have to make a claim on their title insurance policy.

So what is title insurance? Basically, it's protection against other claims of ownership of your property. When you purchase your home, you're going to get what's called "clear title" to the property, which means that you own it free and clear against anyone else's ownership claim. That's very important, because you don't want to commit to spending hundreds of thousands of dollars to buy something only to find that someone else is challenging your rights to it and could theoretically take it away from you. So rather than take the risk that there's an undiscovered cloud on your clear title, you get title insurance to protect you just in case someone else could pop up with an ownership claim on your home.

Today, the risks posed by adverse claims of ownership are very low, mainly because modern title search methods have become much more reliable. But this wasn't always the case.

Historically, the title insurance industry developed because public land records were generally unreliable, and it was difficult to establish an unbroken "chain of title" from one owner to the next in order to prove that the current owners had clear title of ownership. And if the current owners could not establish that chain of title, buyers would be foolish to purchase the home without some form of insurance to protect their ownership rights.

In the modern era, though, public records have become much more reliable, and as homes change hands over time, title companies have established clear chains of title to most properties in our area. Accordingly, these days we rarely see adverse claims of ownership that would trigger a claim on a title insurance policy. Nevertheless, because of the stakes involved, mortgage lenders absolutely require title insurance protection, and virtually all buyers get it. Like a lot of insurance situations, the risk of loss is very low, but the cost if you did have a claim would be enormously high: potentially, the uncompensated loss of the home that you purchased. That's why you need title insurance.

Understanding the Title Reports

In order to get title insurance, you or your attorney will order a series of reports and searches from your abstract company designed to identify any problems with the seller's title to the property. Those searches will trace the chain of title, reveal any liens, disclose any boundary line issues or possible encroachments, and identify any easements, covenants, or restrictions on the property.

As we have said, those reports are unlikely to turn up problems in the chain of title, so they are unlikely to actually kill the deal by revealing that the putative owner does not actually have good title to the property. But those reports often raise some questions and issues about the seller's title that will have to be cleared, because you will not be able to get title insurance if there are even minor outstanding defects on the seller's title.

In most situations, the title defects are simple issues that can be cleared up in a matter of days. But sometimes, the problems can be serious, take a lot of time to resolve, and can delay your transaction. So it's a good idea to be prepared in advance for the kinds of title problems that can turn up in these reports.

Open Liens. Usually, the biggest title problem you'll come across will be unresolved liens on the home. Most titles have a primary lien that comes from the mortgage that the lender put on the property when the current owner purchased it. Indeed, if you get financing to purchase the property, you will be agreeing to your lender's placing a lien on your own title right at the closing table.
But sometimes a title report will find items like tax liens, judgment liens, mechanic's liens, or other types of blemishes on the title that will have to be cleared up to allow for the seller to transfer ownership to you. Those issues need to be resolved, because theoretically those liens stay with the property, and the last thing you want is to buy a home that comes with its own set of new debts. Moreover, a lender will never let you close on a property with outstanding liens, because those obligations, however small, would have priority in time over the lender's mortgage on the property, and few lenders will ever allow any other lienholder to have priority over them.

Open liens can be a real challenge in getting to closing, but there's not much that you can do other than push the seller to clean them up. It's really up to the seller and seller's attorney to clear up the liens, either by negotiating them down, challenging them so that they are removed from the title, or paying them off out of the proceeds of the sale. Don't worry about being stuck with the debts. Neither your abstract company nor your attorney will allow you to take possession of a property that has outstanding liens against it. But waiting for the seller to resolve the issues could cause a major delay in your transaction.

In the worst-case scenario, substantial open liens on the property could terminate your transaction. This does not happen very often, and usually only in situations where the sellers have been terribly delinquent in paying their bills to the point that they cannot get the outstanding liens released in order to sell you the property. The only time we ever really see deals fall apart over liens is

where the owner has major tax deficiencies on the property that cannot be resolved with the government.

Short Sales. A short sale is a transaction in which the sellers owe more to the bank than the property is worth, and have to get bank approval for the sale in order to close with you. In most cases, you will know up front whether the home you're buying is going to subject to a short sale, because listing agents are supposed to identify short sale situations up front when they market the home. But sometimes sellers were not aware they were going to have to sell short, either because they've not been attentive to their mortgage or because they originally tried to sell the home for more than the mortgage amount and only discovered that they were short after they ran the numbers on your final offer. So it might be that you'll discover from the title report on the property that you're purchasing a home subject to short sale approval after you're already in contract. If it turns out you're involved in a short sale, you should be prepared for a significant delay in your closing. Sellers involved in a short sale have to prepare a lengthy set of documents to secure bank approval for the sale, and banks can sometimes take weeks or months to decide whether to allow the sale. Sometimes, of course, the bank will not approve the short sale, something that was more common a few years ago. More recently, banks have come to realize that allowing a defaulting owner to sell short is a better option that taking the property through the longer foreclosure process.

Documentation Errors. Sometimes, your abstract company's title examination will reveal a superficial defect that is not an actual break in the chain of title, but rather just an obvious mistake in the documentation. The most common error is a failure to record mortgage satisfactions – that is, the seller paid off a mortgage on the property, but the lender failed to properly file a discharge of the mortgage and the lien is still showing up on the title. These problems are usually pretty obvious to the abstract company, and they're not serious, but they do take time to resolve and can delay your closing.

Property Taxes. Your abstract company's title report will identify the accurate property taxes for the home, which will be used at the closing to apportion the year's taxes between you and the seller. The problem that comes up is when the actual taxes are different from the amount the seller listed in the multiple listing system. Unfortunately, sellers who misidentify the property taxes almost always err on the low side, which can often be an unpleasant surprise for a home buyer who discovers very late in the process that the property taxes are a lot higher than she thought. This does not mean the seller was being deliberately misleading – calculating property taxes can be a little complicated, and the mistake usually comes from a seller who listed only the town taxes but not the village taxes, or who listed the taxes that he actually pays without realizing that he has some sort of exemption that will not be transferable to the buyer. Usually, the differences are marginal, and you'll probably just shrug them off. But if the true taxes are significantly higher than what you expected, you might try to negotiate with the seller to cover part of the difference. If this comes up, discuss the issue with your attorney.

Survey Inspections. You will need an accurate survey of the property in order to secure title insurance. Your abstract company will try to locate a copy of the survey to the property if one is available. If not, you'll have to get a new survey, which will cost a few hundred dollars and can take a few days or weeks to complete. Once the abstract company has a survey in hand, it will

CORE Client Contact from Hudson United

One of the biggest complaints buyers have during their transaction is that they say they never know what's going on with their title report. To help address that as part of our Client-Oriented Real Estate ("CORE") program, Hudson Abstract created "CORE Client Contact" as a way of keeping your attorney and your agent in the loop at every step of the title process. Once you order title from Hudson Abstract, they'll get email alerts every time we complete a major task in the title generation process, so you'll always know where things stand.

conduct a "survey inspection" of the property to ensure that the property lines are consistent with what's going to be transferred to you in the deed. And sometimes, that inspection will reveal discrepancies that will have to be resolved by the seller: property additions like pools or decks that are not on the survey or the certificate of occupancy, encroachments onto the property by neighbors, or even encroachments by the seller onto a neighbor's property. In those cases, the seller will need to spend time resolving the issues, which can often require exchanging contractual releases with the neighbors or obtaining after-the-fact building permits from the municipality. Again, this is not something that you can control, but is really in the hands of the seller.

Municipal Violations. In addition to the title report, your abstract company will also order a municipal report on your new home. This report does not involve actual title to the property, but examines whether the seller has any unresolved issues with the local municipality. Some of the issues that can crop up in a municipal report are outstanding building code violations, open building permits, or inaccuracies in the certificate of occupancy. Usually, these problems are not that serious, and the seller can resolve them with the municipality. And your attorney will not let you purchase a home that has these types of outstanding problems. But, again, when they do turn up, they can seriously delay your closing.

Conclusion – What Can YOU Do?

Generally speaking, most title reports turn up minor issues that can be resolved quickly and easily, and will not significantly delay your closing. The disconcerting part, though, is that you really can't do much to prepare for these kinds of issues. You're not going to know about the problems until you get the title reports back from your abstract company, and in most of the cases it's really up to the seller to resolve them.

Indeed, one of the advantages in working with Hudson Abstract, one of our affiliated Hudson United home service companies, is that if you agree to get title insurance through us when you purchase your home, we will provide you with preliminary lien searches during your home search process. Thus, when you are preparing an offer, or have reached an accepted offer and are drafting contracts, you can get a better sense of whether the title reports are going to turn up problems that could delay your transaction. The preliminary lien searches can identify situations with open liens on the property, reveal undisclosed short sales, and also identify the correct taxes so that you know what you're getting into BEFORE you sign the contract. It's a great way to be prepared in advance for title-related problems that could delay your closing. So make sure to ask your agent about getting preliminary lien searches from Hudson Abstract.

Part 3: Everything You Need to Know About Getting Home Insurance

Most people don't spend a lot of time thinking about their home insurance, particularly when they're in the process of buying a home. As always, we believe that great service requires full and complete information, so we've provided an overview of home insurance, including the types of coverage you can get and some tips on how to save money.

Before you can close on the purchase of your home, you will need to have a homeowner's insurance policy in place. Most of our clients forget about their insurance needs when they're busy trying to get everything else done before their closing, and end up scurrying around to get coverage at the last minute. Not only could that delay your closing, but it also adds stress that you don't need at that point in the transaction.

Accordingly, we recommend that you take a little time at some point prior to closing to investigate your home insurance options. And we've provided this basic overview to give you an idea of what to expect, what to look for in your coverage options, and how to save money in the process.

An Overview of Homeowner's Insurance

Homeowner's insurance is a policy that protects against losses to your home, its contents, and its use, or the personal possessions that you have within your home. Homeowner insurance also provides liability insurance for accidents that might happen at the home, as well as outside the home if the incident is covered within the overall terms of your policy.

Applying for home insurance is a simple process. You can just call your insurance agent, who will need to get basic information from you like your current occupation, employment history, marital status, previous addresses, date-of-birth, and social security number. Your insurance agent will also ask you questions about the home you're buying, particularly the home's age, building materials, location, square footage, and even the distance from the nearest fire hydrant. Finally, you should also discuss the nature of the coverage you're going to want for the home, and go through the various available options.

Following the call, your insurance agent is going to perform some underwriting due diligence, checking your credit, criminal, and insurance history, as well as your "loss history" to see what kinds of insurance claims you've made in the past. Finally, he or she will also investigate your coverage options, to try to find the best pricing for the policy you requested.

Ultimately, the insurance agent will provide you with a written "quote" identifying the cost for the policy type you requested, which typically breaks down your coverage into five different classifications. For example, Classification A usually explains the coverage for the dwelling, and Classification C the coverage for your personal property. Those classifications can be a little confusing at first, but they're actually very helpful if you decide to get other quotes, because you'll be able to compare policies side-by-side to see the differences in prices and coverage. The pricing of your insurance quote is good for 30 days, and you can get as many quotes as you wish as you narrow your choices down.

If you approve the quote, your insurance agent will prepare and send an insurance application setting out the terms of the policy, which you'll need to sign and return with a check or credit card information. Once your application and payment are received, you'll get a "paid in full" receipt and "proof of insurance," also called the "binder," which you will need for your lender in order to close on the loan. Indeed, some lenders require the binder's proof of insurance to even schedule the closing.

Once you get the binder, your work is done, and you will have insurance coverage that will activate on your expected closing date. It's important,

though, to let your insurance agent know if your closing date is delayed, because otherwise the policy will go into effect before you even own the home. In that case, even though you'll be paying for the insurance, you won't actually get any coverage, since you can't get insurance on a home that you don't own yet. So to avoid paying for insurance that doesn't actually apply to you, let your insurance agent know if your closing is rescheduled.

Understanding Insurance Policy Forms

Given how much advertising you see about home insurance generally, you'd probably be surprised to find out that virtually all insurers offer very similar types of policies. Insurance contracts from different carriers may vary slightly, and you can get particular "endorsements" that will expand your protection, but state regulation sets the fundamental coverages provided by each policy.

The standard policy forms are all known by the acronym "HO" for "Homeowner" and a number delineating the type of coverage extended by the policy form. These standard policy forms can be confusing, so we'll try to break it down a little. Basically, when you get an insurance policy, you're getting a contract guaranteeing that the insurance carrier will reimburse you for damage to your home or your personal possessions from certain hazards, and will provide liability protection for accidents inside or outside the home. But when you're choosing a policy, you have a number of options that carefully delineate the contours of the property and liability protection you want.

For most homeowners, the choice of policies comes down to two common forms for single-family homes, and a standard form for condominiums and coops:

- **HO-3 ("Special Form" or "Broad Form").** The HO-3 is the typical policy in place for most single-family homeowners, because it provides basic protection against common hazards with moderate levels of reimbursement. In the modern era, the HO-3 is the "vanilla" form of insurance coverage that most homeowners get because it provides good coverage at a reasonable price.

- **HO-5 ("Premier Form").** The HO-5 covers everything on the HO-3, but provides more expansive personal property coverage and a higher level of reimbursement for losses. The HO-5 is designed for higher-end single-family homeowners that might have more expensive personal possessions, or who want the more extensive coverage and are willing to pay more for it.

- **HO-6 ("Condos and Coops").** The HO-6 is the standard form coverage for condominiums and coops. Unlike the single-family policies, it won't cover the structure of the home, which should be insured by the building. But it will cover the contents of the home, and can be customized to provide either standard protection at an affordable price or more expansive coverage at some additional cost.

This is not to say that these are the only policy forms available, but the vast majority of our clients end up getting a policy under one of these forms. The other forms tend to be designed for unusual properties or coverages. If you do have an unusual situation, you should discuss it with your insurance agent.

Choosing Coverage

How do you choose from among the policy forms available to you? Basically, any decision about your home insurance coverage comes down to five distinct choices that you have to make about the type of coverage you want:

1. **Named or All-Risk:** Whether to get protection against only named hazards, or get full coverage for all un-excluded risks.

2. **Dwelling:** the kind of replacement coverage you want for losses to your home.

3. **Contents:** the kind of replacement coverage your want for your personal property, and whether to get additional coverage for particularly valuable items.

4. **Liability:** how much liability coverage you will need for accidents.

5. **Deductible:** the amount you pay before your insurance coverage kicks in.

Let's go over each of these decisions in turn:

1. Named Risk or All Risk

When you're choosing a policy type, make sure you understand what your policy covers, what it explicitly does not cover, and what it might cover. Both the HO-3 and the HO-5 provide for standard coverage and specific exclusions, but they differ in how they treat risks that are not explicitly identified in the policies:

- **What's specifically covered?** Standard policy forms will cover what's called the "16 named perils," which are specifically identified and enumerated on the policy. For example, these common hazards include fire, explosions, windstorms, and damage from weight of ice or snow. If you incur damage from the specifically named perils in the policy, you'll be covered under either the HO-3 or the HO-5 form.

- **What's specifically excluded?** The policy forms also specifically exclude certain types of hazards, which will most definitely NOT be covered. The standard exclusions include water damage from floods, earthquakes, homeowner negligence, or power failure. So if you incur damage caused by one of the excluded hazards, you won't have coverage under either the HO-3 or HO-5 form.

- **What MIGHT be covered?** So what happens if you suffer property damage caused by an event that is not covered as a "named peril," but is also not explicitly excluded? In those cases, you might or might not have coverage for what are called "open perils" – hazards that are not specifically named, and not specifically excluded. This is where you see a major difference between the HO-3 and HO-5 forms. The HO-5 is known as an "all-risk" policy because it will cover damage from open perils to BOTH your dwelling and your personal possession, so if you have an HO-5 policy you'll be fully covered for any hazard that is not specifically excluded in the policy. The HO-3 form, though, only covers open peril losses to the dwelling, NOT the contents of your home.

Basically, when it comes to the type of overall coverage you can get, both the HO-3 and the HO-5 over the named perils, and generally have the same named exclusions. The difference is that for hazards that are not specifically named or excluded, the HO-5 will cover damage to both your dwelling and your contents, while the HO-3 will only protect against damages to your dwelling.

Note that you can get coverage for some of the specific exclusions either through an "endorsement" (i.e., an addition to the formal policy) or with an additional insurance coverage policy. For example, because flooding is a specific exclusion to both the HO-3 and the HO-5 list of perils, many homeowners get flood insurance separately as part of a federal program. Indeed, depending on where your home is located, you might be required to get that flood insurance by your lender.

2. Dwelling

When you get home insurance, you'll obviously be getting protection against a major loss to your home – i.e., your dwelling. But you will have an important choice to make about how you will be reimbursed in the event that you actually suffer such a loss. Essentially, the difference comes down to this: if you want to be absolutely sure that you can rebuild the home exactly the way it was before the loss, then you'll have to pay a little extra for what's called "guaranteed replacement cost coverage."

Let's say, for example, that you lose your home from a fire or one of the other named perils, so that coverage is not an issue. Now, you're going to want the insurance company to rebuild your home. This

Insurance Coverage for "Market Value"

When you get coverage for your home, you're not covered up to the "market value" of the property. After all, the market value includes the cost of the land, which is not part of the "dwelling." So the insurance company doesn't simply look to see how much the home is worth on the open market, and write you a check for that amount – the company isn't "buying your house." Rather, you get reimbursed for the cost of rebuilding the home, either up to the policy limits or with a guarantee to pay the full costs.

policy, the insurance company will only pay up to that amount to rebuild your home, even if it turns out that the construction costs more than that. If it costs $500,000 to rebuild your home, but you're only covered for up to $400,000, you're going to be responsible for that extra $100,000 out of your own pocket.

That's why if you get the replacement cost coverage offered by the HO-3 form, you'll want to set that limit at a level that will provide for fair compensation in the event of a loss. That can be a bit of a challenge, so be sure to gather as much information as you can about the home you are insuring, in order to get accurate valuations for your coverage. You don't want to set the policy limit too high, or you'll be paying for coverage you don't need and won't be able to collect. And you don't want to set it too low, because then you'll be out-of-pocket for the additional cost of rebuilding your home. In particular, make sure you tell your insurance agent if the home has high-end materials that would raise the cost of rebuilding. A good insurance agent will ask those questions, to determine, for example, if the home has remodeled kitchens or bathrooms, marble floors, granite countertops, and the like. Even then, remember that you'll still be exposed in the event that you miscalculate the cost of rebuilding the home, or if rebuilding costs go up. This could happen, for instance, in the event of a major storm, which could increase demand for construction and drive up the cost of labor and materials beyond the limits of your replacement cost coverage – even in a situation where you had sufficient coverage before construction costs shot up.

In contrast, HO-5 forms provide for "Guaranteed Replacement Cost" coverage for your home, which guarantees that your carrier will pay whatever it takes to rebuild the home exactly the way it was. Policies with guaranteed replacement cost coverage have no stated reimbursement limits, so you will be fully compensated for your loss. That's another reason why HO-5 policies are more expensive – because the carrier takes the risk of covering all the costs of rebuilding your home. When you get the policy, you'll provide your carrier with an estimate of that cost, but the carrier will probably conduct an inspection of the home to make sure that you're paying a fair price for the insurance that you're getting. For example, if you set the policy for a guaranteed replacement value estimated at $750,000, and the carrier determines that rebuilding the home will cost significantly more, you're going to end up having to pay a bit more for your policy.

The guaranteed replacement cost coverage comes automatically with the HO-5 policy, but you can also get it with the HO-3 by a specific endorsement. In some cases, it might be less expensive to do it that way rather than getting the full HO-5 coverage.

3. Personal Property

When you suffer a catastrophic loss, you not only lose your home but all the personal possessions you kept in the home. So you're going to want to examine your policy choices to see how you will be reimbursed, and whether you want to specifically add protections for particular valuables.

Both the HO-3 and HO-5 policy forms automatically provide for personal property coverage up to a certain percentage of the amount of insurance that you have on the home itself – generally from 40% to 70% of your overall coverage, depending on the carrier. So if you are covered up to $300,000 on the value of your home, you might have up to $120,000 (40% of $300,000) of coverage for your possessions. This doesn't mean, though, that in the event of a catastrophic loss you'll just get a check for $120,000 for the loss of all your things. Rather, when you file a claim for loss of personal possessions, you'll itemize everything that you've lost and identify the value of each item. Your carrier will reimburse you for your losses, up to that $120,000 cap.

Again, though, the HO-3 and the HO-5 provide different methods of reimbursing you. HO-3 policies typically pay personal property claims on an "Actual Cash Value" basis, which is determined by taking the price you paid for an item and factoring in the depreciation. That is, if you bought a television for $1,000 four years ago, your policy would compensate you, but not for the value of a new television. Rather, you would get reimbursed for the carrier's calculation of the value of a four-year old used television, which might not be enough to actually replace what you lost. In contrast, the HO-5

policy provides for "Replacement Cost Coverage" for your personal possessions, which will replace your lost items with new items, without regard to the depreciation. So instead of getting a check for the value of a four-year old television, you get enough compensation to buy a new television. You get the replacement cost coverage automatically if you obtain an HO-5 policy, but you can also do it through endorsement to the HO-3.

Getting a Home Warranty

Another type of insurance you can get when you purchase your home is a home warranty, which protects against certain types of defects that you might discover once you move in. For example, let's say that you move into your new home, and a week later you find that the outlet in your bedroom doesn't work. It's not something you would have known about when you looked at the house, but the kind of thing you discover as soon as you move in. It's very disappointing, and a real pain to have to pay an electrician to fix the problem. But if you obtain a home warranty it's something that you won't have to pay for. For that reason, we highly recommend that you get a home warranty when you buy your home. It costs about $400, but it protects you from all sorts of hidden physical problems in your home, and can save you a lot of time and energy. It's nice to simply make a call to an 800 number to fix all those little things.

Also, you might also consider getting additional coverage for particularly valuable items. Most homeowner's policies offer limited coverage amounts of $500 to $2,500 for individual personal articles such as jewelry, watches, furs, firearms, silverware, cameras, golf equipment, computer equipment, collectibles, or fine art. If you have these kinds of valuable items, you might want to get additional endorsements that will fully cover their value, or a "personal article floater," which is a separate policy specifically for that item.

To get an idea of the coverage you need, take an inventory of all your personal possessions. Some suggestions for your inventory:

- If possible, list each item, its value, and its serial number (if available).
- Photograph and videotape each room, including your closets, open drawers, storage areas, and your garage.
- Safeguard the receipts of your major items, which will help you prove their value.

That inventory is not only necessary for ensuring full coverage of your personal possessions, but it can be critical in proving the extent of your damages in the event of a loss. Indeed, if you're in the process of moving, your inventory might do double-duty in giving you a basis for itemizing your insurance and for cataloguing your possessions in order to get an accurate estimate of the cost of your move.

To ensure that these types of items are properly protected, discuss with your insurance agent how to cover them on a scheduled basis.

4. Liability

Most people think of their home insurance as protection against property damage from catastrophic events, but your policy will also provide liability protection against accidents in your home. So, for example, if someone slips and falls in your living room and is badly injured, you'd be covered under your homeowner's policy. Your policy even extends off-premise liability, which protects you if you're involved in certain kinds of accidents outside the home.

The main choice you have with regard to your liability coverage is the amount of protection you want. Most of our clients get at least $300,000 in coverage, but you might find that's not nearly enough to protect your assets in the event of a major accident. You can discuss the level of coverage you need with your agent, but just think of it this way: if someone suffered a serious injury in your home, she could theoretically sue you for everything that you own, so to be fully covered you should make sure you have coverage up to that full value. You can simply add up the value of your savings, the equity in your home, your investments, your personal possessions, and

your business. Whatever that number is, that's how much protection you probably need, and it helps that generally speaking the insurance gets cheaper dollar-for-dollar as you extend the limits.

You also might consider getting an umbrella policy that would provide additional protection beyond the limits of your other liability policies. An umbrella policy sits on top of your homeowner's and auto policies, augmenting their liability coverage. Many homeowners take a moderate amount of liability insurance on their home and auto policies, and supplement that with an umbrella policy, because it can be a much cheaper way of getting high limit coverage.

5. The Deductible

When you set up your insurance policy, you'll likely have a choice as to the level of the deductible that you want. The deductible is the amount of money you'll have to pay out-of-pocket before your insurance coverage kicks in. Generally speaking, the higher the deductible, the lower your premium, so you can save money if you set a higher deductible.

The deductible amount only really comes into play when you incur a small loss. For example, the difference between a $500 and $2,500 deductible is negligible if you ultimately have a fire that costs you $250,000 of damages. But if the loss is only for $3,000, then you would have been able to claim a $2,500 reimbursement after the smaller deductible, but wouldn't even bother to file a claim at the larger deductible – it probably wouldn't make long-term sense to put a claim on your record with the insurance company to collect just $500.

Where you set the deductible is up to you, and your personal risk preferences. Some clients like to set high deductibles, particularly if they figure they're never going to make a claim on the policy except for a catastrophic loss. They'd rather save money on the yearly premium and take the risk that they'll suffer some small losses for which they won't be reimbursed. Others are more risk-averse, and would rather ensure that they have coverage for any material damages they suffer.

One word of caution: if possible, you should set your deductible for a flat rate rather than a percentage rate. Traditionally, a deductible is a flat rate, such as $1,000. But many insurers are introducing percentage deductibles around the country, particularly in high-risk areas such as homes built on the coast (indeed, for some areas, you might only be able to get a percentage deductible). These policies make you liable for 1%-5% percent of your home's insured value before the insurance coverage comes into play. So, if you have a 2% deductible and your home's insured value is $500,000 (remember, that's the cost to rebuild, not your home's market value), you'd have to pay the first $10,000 in damages. Some homeowners are switched from flat-rate to percentage deductibles at renewal time and may not be aware of the change. Make sure to read special notices sent by your home insurer and your "declarations page" at renewal time, or call your agent to check on what kind of deductible you have.

Getting Additional Coverage

In addition to the coverage provided by the standard homeowner policy forms, you can get all sorts of additional protection. For example, many homeowners get coverage for flood damage, since flooding is one of the specific exclusions to both the HO-3 and HO-5 policies. If you want that protection, you can get it from the National Flood Insurance Program (NFIP), a government-subsidized program that offers flood insurance through home insurance companies nationwide. Moreover, if your home is in a special flood hazard area, your lender will almost certainly require you to purchase flood insurance. Your insurance agent can arrange a separate quote for flood insurance if you want it or need it for your mortgage.

Moreover, as we've discussed, you can supplement your HO-3 policy to upgrade your reimbursement coverage, and add endorsements to protect particularly valuable items. Here are some common endorsements that many homeowners get:

- Water back up and Sump Pump Discharge Overflow. Water can enter your home in ways other than actual flooding, such as when water backs up

through sewers, drains, or sump pumps. You can get sewer and drain backup coverage by adding an endorsement to your homeowner policy.

- Additional Replacement Cost Protection. If you get the HO-3 policy form, this endorsement will provide an additional amount of insurance, up to 50% of the primary dwelling coverage limit. This is an excellent safeguard against inflation and sudden increases in reconstruction costs that can come after major catastrophes. In this situation, the Additional Replacement Cost Endorsement would increase your primary dwelling coverage limit and protect your home from being under insured.

Insurance companies offer any number of other options that you can discuss with your agent.

Conclusion: HO-3 or HO-5?

Although insurance policy forms can be confusing at first glance, you should take the time to make sure you understand the fundamental nature of the coverage you are getting, and the way in which you'll be reimbursed. Both the HO-3 and HO-5 policy forms provide good insurance protection, but homeowners who are risk-averse, and who have particularly expensive personal possessions, might opt for the HO-5 coverage to ensure that they can get full replacement value for that personal property in the event of any named or open peril.
Others, though, might opt for the reduced coverage of HO-3 to keep their insurance rates lower, and take on the small added risks. Indeed, one option many homeowners take is to choose the HO-3 policy form, but supplement it with the endorsements that enhance its coverage to provide for guaranteed replacement cost coverage of the home or replacement coverage for the contents. In some cases, supplementing the HO-3 with endorsements might be less expensive than buying a HO-5 policy, but provide much of the same protection. Indeed, HO-5 policies might not be available from some insurers at lower price points, so taking out an HO-3 policy and supplementing it with endorsements might be the only way to get the added protections.

How to Save Money on Your Home Insurance

Finally, we want to address some ways that you can save money when getting your home insurance. We've all seen the glut of insurance advertising from companies claiming they have the best rates, or that they saved money for customers who switched. They all say the same things, and they can't all be right.

Now, sometimes, the ads are just misleading. For example, a company might advertise that it has low rates, but those rates might only be available to people with particular risk profiles, in specific locations, getting a stripped down policy that doesn't provide them nearly enough protection. Moreover, when companies claim that they saved money for people who switched, remember that they're only counting the people who switched – they don't count the ones who decided to stay put! In other words, people who switch insurance companies usually make the change precisely because of the rates, so virtually everyone who does switch did so because they saved money.

For the most part, though, the incessant insurance advertising makes a reasonable point: insurance rates do vary among carriers. But that doesn't mean that a particular company always has the best rate for a particular individual. Rather, insurance rates really depend on three things: (1) the policy, (2) the carrier, and (3) the insured (i.e., you!).
The Policy. We've already seen how your policy choices can affect your rates. If you choose the HO-5 premium policy, you'll pay more than you would for the more limited HO-3 coverage. If you want to insure particularly valuable items, it will cost you. If you want to add endorsements, your payments will go up. So when you evaluate rates across companies, make sure that you're comparing apples-to-apples – policies that provide the same levels of coverage.

The Carrier. Simply put, different carriers have different rates. All insurance companies have their own preferred risk profile, and they price aggressively and competitively to target that profile. Some companies will cater to standard risks, others to non-standard or high-value risks.

It all depends on the location of the markets they serve and their loss results from prior years. Therefore, a company's pricing for a particular area can change from year-to-year depending on their experiences insuring risks in that area.

You. Your rate will also depend on your personal risk profile, and the particulars of the house you're buying. The insurance company reviews your personal information to make an underwriting decision based on your background, claim history, even basic demographics. Your rates will be higher if you have a history of expensive claims on your record, or if your risk profile simply conflicts with the type of business that company is trying to write. And your rates will also depend on the home, not just because of the price or the building materials, but where it's located. Some carriers don't want to do business in certain areas, and will command a rate premium for homes there.

For these reason, we recommend you get multiple quotes from an independent agent that is not limited to just one insurance carrier, because you never know whether your risk profile will be a match with that company. Indeed, you'll find that even for the same level of insurance protection, the rates offered you by different companies will vary widely. An independent agent like The Hudson Group Insurance can provide a variety of quotes to find the insurance carrier that is providing the most competitive rate for your particular risk category at the time that you're getting coverage. Indeed, we can help you shop from almost 20 of the nation's leading insurance companies to help you get the best price for your insurance needs. You'll be able to see the quotes from the various carriers, the differences in coverage, and make an informed decision.

Finally, here are some basic suggestions for how you can save money when getting insurance for your new home:

Package Your Home and Auto Policies. Some companies that sell homeowners, auto, and liability coverage will take 5-15% percent off your premium if you buy two or more policies from them. When purchasing a home, it is an excellent time to re-evaluate your auto insurance to find the company that will offer you the best rate for your full bundle of needs.

Make Sure Your Insurance Agent Seeks Out Discounts. Companies offer several types of discounts, but they don't all offer the same discount or the same amount of discount. A well-trained insurance agent should be able to help you explore all potential savings opportunities.

Make Home Improvements. You can save money on your home insurance by adding storm shutters, reinforcing your roof or buying stronger roofing materials, or modernizing your heating, plumbing and electrical systems to reduce the risk of fire and water damage.

Improve Your Home Security. You can usually get discounts of up to 5% for installing a smoke detector, CO detector, burglar alarm or dead-bolt locks. Some companies offer to cut your premium by as much as 10 or 15 percent if you install a sophisticated sprinkler system and a fire and burglar alarm that rings at the police, fire, or other monitoring stations. These systems are not cheap, so before you make a decision, find out what kind your insurer recommends, how much the device would cost, and how much you'd save on premiums.

Raise Your Deductible. The higher your deductible, the more money you can save on your premiums. Today, most insurance companies recommend a deductible of at least $500. If you can afford to raise your deductible to $1,000, or $2,500 a year, you will receive a premium discount.

Pay Upfront. If you pay for your full year's worth of insurance coverage up front, you get a discount over what it will cost if you pay by installments.

Conclusion

Getting a home insurance policy is one of the last things you will do as part of your home buying experience. We've tried to provide you with a comprehensive overview of your options, but you should always make sure to discuss these matters with your insurance agent.

Conclusion: Preparing for Your New York State Closing Costs

Buyers often miscalculate how much money they'll need at the closing table, because they don't prepare for the fees and costs that start to accumulate during the transactional process. As always, it's best to be prepared, so make sure you start thinking about saving up money to cover those costs.

If you're buying a home, you need money. No surprise there. You know that you need to borrow a lot of money from the bank. You need more money for your down payment. And you probably also know that you will need some money for out-of-pocket closing costs. But most people have only a vague idea of what those fees are, or of how much they'll ultimately need at the closing table to complete their purchase.

As always, we want you to be prepared, so we're going to review the typical fees associated with buying a home. We should point out that these are general estimates, and also make clear that the fees are fairly standard across the industry, regardless of where you go for your mortgage, title, and insurance needs.

Attorney Fees. You will need to hire an attorney to handle your real estate transaction, and you will generally pay for those services at the closing. Attorney fees vary wildly depending on your local area and the attorney's experience and overall fee schedule. Generally speaking, most attorneys charge a minimum of $500 and as much as $2,500 to handle your transaction.

Mortgage fees. Most lenders charge borrowers an array of fees as part of the loan application process. Those fees vary depending on the individual lender, but here are some of the most common fees and an estimate of their price range:

- **Appraisal fees.** Fees for performing an appraisal on the property, which generally run around $400-$500 for conforming loans and $650-$750 for higher-priced loans.
- **Credit reports.** Lenders run credit reports on borrowers, charging them about $50-75.
- **Underwriting fees.** Lenders charge borrowers for performing underwriting on their loan application, generally around $700-$850.
- **Bank attorneys.** Lenders will require you to pay for a bank attorney at the closing, who will represent the interests of the bank. The bank attorney generally charges $800-$850.
- **Miscellaneous fees.** Lenders also charge a few miscellaneous fees, such as for tax service and flood certification, which can run a few hundred dollars at most.

All told, these bank fees generally cost about $2,000-$2,500, regardless of the size of your loan.

Title fees. Title insurance protects your interest in your home against any adverse claims of ownership, and is required by all lenders. The premiums are based on the purchase price and the amount financed, but as a general rule of thumb, the insurance premium itself will cost about .5%-1% of the purchase price: closer to .5% for properties above $400,000 and closer to 1% for properties below $400,000. Your attorney and abstract company will give you an accurate calculation of the fees to expect when you order your title insurance. Note that title insurance rates are set by state law, so you won't see a difference among title companies.

In addition to the title premium, you'll also need to pay for some ancillary searches and examinations performed by your abstract company. These fees can vary a little among companies, but generally conform to the following ranges:

- **Survey or survey inspection.** An inspection of an

existing survey only costs about $100, but if the abstract company needs a new survey, that will cost about $700.

- **Municipal searches.** Your abstract company will run a municipal search of the property to check for zoning or building department violations, which costs about $200.
- **Other searches.** Your abstract company will also run some additional bankruptcy and tax searches, which will cost about $100.
- **Recording fees.** You'll have to pay to record your mortgage and deed with the county clerk's office, which will cost about $400.

Altogether, the miscellaneous title fees will end up costing you under $1,000, although that's in addition to the cost of the insurance premium itself.

Taxes. As with any sort of legal transaction, you'll have to pay certain taxes as part of your real estate purchase. Here are the two main taxes that you'll be responsible for:

- **Mortgage taxes.** New York State exacts a mortgage tax that varies depending on the county, but is generally about 1.0%-1.3% of the purchase price. Part of that is a tax to the buyer, and part of it is a tax to the lender, which the lender then charges to the borrower. In our local area, the tax is 1.05% to the buyer and an additional .25% to the lender in Westchester and Rockland, and .80% and .25% in the outer suburban counties. The taxes in the city of Yonkers and in New York City are somewhat higher.
- **Pre-Paid Property taxes**. In addition, buyers need to be prepared at the closing to pay the seller back for property taxes that the seller has already paid on the property. That is, since sellers usually pay property taxes in advance, they might have already paid the taxes for part of the year. Thus, at the closing table, the buyer will reimburse the seller for the amount of taxes that have been pre-paid, depending on when the closing falls within the tax year.

Accordingly, the amount of money you need to pay taxes at the closing table will depend on your purchase price, the county mortgage tax rate, and the property taxes that need reimbursement.

Also, most lenders will require you to have a full year's of property taxes available either to pay your allocation or to put into escrow. Remember, though, that your property tax allocation is not really a "closing cost," even though you have to pay it at the closing table – it's just the your allocation for the property taxes owed during the time that you'll own the house in the tax year.

Total Costs. It's difficult to put a total estimation of closing costs, because most of the fees depend to some extent on the provider and more importantly on the purchase price of your home. On the table provided, we have set out approximations of closing costs at three different price points, which might help you get a general sense. of what you can expect As a rule of thumb, though, you should be prepared to have at least 2%-3% of the purchase price as cash on hand to pay for these closing costs.

Now, if that seems intimidating, remember that in many cases you can roll your closing costs into your mortgage loan. That's obviously a better option for many buyers, since it's much better to add a few thousand dollars to your mortgage, especially at today's rates, rather than come out of pocket. But that option is only available in certain types of situations, so you'll need to discuss it with your lender.

Saving your Money

If you are concerned about saving money toward your closing costs, discuss the matter with your mortgage originator. He or she can give you some good advice about setting up a savings plan to start putting money away not just for your down payment, but for all your other closing costs.

New York Closing Costs Illustrated			
Here are some rough estimations of closing costs at three different price points. Please remember that these are just approximations. You should check with your service professionals to get a more accurate calculation of your expected fees. (Note that the transfer taxes are set for Westchester and Rockland – they would be lower in other counties)			
Purchase Price	$300,000	$500,000	$750,000
Down Payment of 20%	$60,000	$100,000	$150,000
Amount Financed	$240,000	$400,000	$600,000
FEES			
Attorneys Fees	$750	$750	$1,000
TOTAL ATTORNEY	$750	$750	$1,000
Mortgage Fees			
Appraisal	$450	$450	$700
Credit Reports	$50	$50	$50
Underwriting Fee	$800	$800	$800
Bank Attorney	$800	$800	$800
Miscellaneous	$200	$200	$200
TOTAL MORTGAGE	$2,300	$2,300	$2,550
Title Fees			
Homeowner Premium	$1,400	$2,142	$2,987
Mortgage Premium	$349	$524	$732
Municipal Searches	$200	$200	$200
Other Searches	$100	$100	$100
Survey Inspection	$100	$100	$100
Recording Fees	$400	$400	$400
TOTAL TITLE	$2,549	$3,466	$4,519
Taxes			
Mortgage Taxes			
Mortgage Tax to Buyer	$2,490	$4,710	$6,270
Mortgage Tax to Lender	$600	$1,000	$1,500
TOTAL TAXES	$3,090	$5,170	$7,770
TOTAL ALL	$8,689	$11,686	$15,839