

10 Must-Know Mortgage Terms

Shopping for a new home is fun and exciting. Yet securing financing to buy real estate can be stressful. The more you know about the home mortgage business, however, the smoother your transaction will be. To help you get a handle on financing terminology before you buy a home, we have defined 10 commonly used mortgage terms.

Adjustable Rate Mortgage (ARM Loan): An ARM Loan has an initial interest rate that is often lower than a conventional fixed-rate mortgage. This initial rate is usually locked in for one or more years. Once the initial term is over, the interest rate on an ARM loan may go up within specified limits over predetermined intervals during the course of the loan. The lower initial interest rate associated with an ARM loan translates to a lower initial monthly payment. The tradeoff, however, is the potential for a higher payment if interest rates go up as the ARM loan progresses.

Annual Percentage Rate (APR): The APR for your home loan is an annual calculation that includes the interest rate quoted by your mortgage company plus additional home loan costs such as origination fees and points. The important thing to keep in mind about your loan's APR is that it will be higher than advertised interest rates because of these additional factors.

Closing Costs: With each real estate transaction, there are many expenses to pay and agencies to compensate. These fees, which are often shared by the buyer and the seller, are referred to as the closing costs. When you buy a home, the closing costs might include loan origination fees, escrow payments, title insurance, attorney fees and even discount points paid to lower your loan's interest rate.

Escrow: During the home loan process, a neutral third party known as Escrow holds documents and money (including earnest money deposits) for safekeeping until the real estate transaction is complete. An Escrow account is also used once you complete your home loan to hold the property tax and insurance monies that are collected with each mortgage payment.

Fixed-Rate Mortgage: A conventional fixed-rate mortgage means that your interest rate will be the same for the entire life of the home loan. Financing for this type of loan is typically spread out over 10, 15, 20, or 30 years, depending on the needs and payment capability of the buyer. A fixed-rate mortgage provides buyers with the security of knowing exactly what their monthly house payment will be during the entire loan term.

Loan to Value Ratio (LVR): When you buy a home, this term refers to the amount of financing you are getting in relationship to your new home's value. For example, an \$80,000 mortgage on a \$100,000 home has an LVR of 80 percent. This is important because an LVR of more than 80 percent will require you to purchase private mortgage insurance (PMI). Using the same example to illustrate this point, if you finance \$90,000 of your \$100,000 home, your LVR will be 90 percent, initiating the need for PMI.

Lock-In: Home mortgage interest rates vary from day to day. While you buy a home and secure financing, you may decide to lock in a particular interest rate with your lender. This lock-in guarantees that your home loan will be processed with this rate, even if interest rates rise before your loan closes.

Points: There are two types of points that can be applied to a home mortgage. Discount points are used to reduce the loan's interest rate and origination points may be added to cover the expenses associated with processing a loan. One point equals one percent of the loan amount. This means that, to lower your interest rate by one point on a \$300,000 mortgage, you'll need to pay an additional \$3,000 at closing.

Private Mortgage Insurance (PMI): When you finance more than 80 percent of your new home's value, your lender will require you to purchase PMI. This protects the lender against loss if you default on your home loan. Your monthly PMI payment is added to the cost of your mortgage payment. It is important to

note that when you have accumulated 20 percent equity in your home, you will want to check into canceling your PMI to lower your monthly mortgage payment.

Title Insurance: A home mortgage requirement, title insurance protects both the buyer and the seller against legal defects in a home's title. This policy ensures that a property owner has the legal right to transfer a home's title to the seller. If a problem occurs, the title company pays the associated legal fees to correct the situation.

Knowledge is power, even when you buy a home and apply for a loan. By familiarizing yourself with these 10 must-know mortgage terms, and doing additional research as needed, you will be positioned to negotiate the best home loan that your money can buy!