<u>First Time Homebuyer's Guide</u>

There is plenty of information on the internet intended to help first-time home buyers get through the home buying process easily. However, the number of steps can confuse or overwhelm first-time buyers. Here's a guide to help you on the way.

Step One: Get Pre-approved

Buying a home is a fantastic investment that every home buyer should enjoy. However, using the right strategy can make all the difference. Many first-time home buyers make the mistake of falling in love with a home or neighborhood before they talk to a mortgage loan officer. Getting pre-approved will take some of the stress away from finding your perfect home.

Benefits for the Buyer

Getting pre-approved will tell the buyer how much they can actually afford. The loan officer will tell the borrower their principal interest payments per month, as well as their estimated taxes, insurance and mortgage insurance granted they need it.

Benefits for the Realtor

The realtor also benefits from the buyer getting pre-approved. Once pre-approved the buyer will be able to let their agent know their budget and agents can then begin looking at homes that match their needs and wants, while also ruling out homes that are above their budget.

After getting pre-approved, the buyer will next be asked to fill out a loan application, which starts the formal loan process.

Loan Application

The first step in getting your home, will be your loan application. The loan application will consist of a lengthy form completed by your loan officer that covers your financial situation.

While much of the loan application is quite detailed, the loan officer will also ask some simple questions. The loan officer will need to gather your name, date of birth, social security number, current home address, and employment information. The address of the home you wish to buy will also be asked if the application is for the purchase of home. However, if you do not have a new address that, it is not needed to complete the loan application.

The loan officer will also need to see two years of employment and residential history. The borrower will also be required to show all their assets.

The term assets is quite broad, but generally consists of: **money available in checking and savings accounts, any property or land ownership, current stock or bond investments, income from business ownership, and retirement accounts.**

The application provides the borrower with an estimate of how much they can borrow, estimated closing costs, and the amount the borrower will need to bring to closing.

Providing the most accurate and up-to-date information about their employment, income and assets, will allow the borrower to have a smoother approve and underwriting process.

Processing The Application

Once the loan officer and borrower have completed the loan application together, and determined the price range for the purchase, the borrower will be asked to provide more information about themselves. The borrower must gather all the necessary documents to qualify for the loan and provide them to the loan officer for review before moving on to the next phase of the loan application.

Borrowers that receive a W-2 and a paycheck will need to provide the loan officer with**: pay stubs for the last 60 days, bank statements (checking and savings) for the last 60 days, W-2 forms from all jobs from the past two years, and a most recent statement from retirement or investment accounts.**

Borrowers that are self-employed have a different set of documents to provide than those on W-2. Self-employed borrowers will need to provide: **their last two years of personal tax returns, last two years of their business' tax returns, a cash flow statement from the current year, personal bank statements (checking and savings) for the last 60 days, and a most recent statement from retirement or investment accounts.**

Once the borrower has provided the loan with their financial documents, the loan officer will then have the borrower sign a couple forms. These forms include the loan application, the Truth in Lending form, and the Good Faith estimate among others. The processor will then go over these documents as well as the financial documents to double check that everything is correct. Once verified, the processor then orders the title insurance binder and an appraisal.

The title insurance binder is a record that benefits the buyer and the lender. A title insurance binder is a temporary form of insurance that ensures the transfer of the ownership, for example, when there could be a gap in the buyer or seller's insurance policy.

The appraisal is used to determine the value of the home the borrower is wishing to buy. The appraisal will compare the borrower's new home against three homes with comparable features that have sold in the last six months. Comparable features include square footage, number of bedrooms, design and location. Once the appraisal is finished the actual value of the home is determined.

Upon completion of the appraisal and title insurance binder and review of all necessary documents, they will all be combined and sent to the next stage: Underwriting.

Types Of Mortgages

Many people understand the basics of a mortgage, but mortgages can be intricate and have many different types of requirements depending on what type of mortgage you are applying for. It will be helpful to go into your mortgage process with some knowledge of the type of loan you need, so this section of the article can help understand the basics on a couple different types of loans.

Conventional- Conventional mortgages are the most common type of mortgages people get. Credit score requirements are typically around 680-700. Conventional mortgages will also require a down payment of at least 3%. Since conventional mortgages are not guaranteed by the federal government they typically have stricter lending requirements.

FHA – FHA mortgages are guaranteed by the Federal Housing Administration. This type of loan is quite common for people who are buying their first home. FHA loans credit score requirements are lower than those of conventional mortgages, and will only require a 3.5% down payment.

VA – VA loans are guaranteed by the Department of Veterans Affairs. The program is strictly for American veterans, active military members, reservists and select surviving spouses. There is no down payment requirement and less strict credit score requirements than other loan programs. The Veteran will need to supply their DD 214 and Certificate of Eligibility.

USDA – USDA loans are guaranteed by the US Department of Agriculture that provided financing for rural areas. If the home value is high enough there is no down payment requirement and the closing costs may be added into the mortgage. However, there are maximum income limits to be eligible for USDA loans. The income limits vary by area, so it's a good idea to check with your lender about your area to make sure you qualify.

These are some of the most common types of loans for first time home buyers, however, there are many more. It's always a good idea to check with a loan about the requirements needed for the type of loan you are looking to get.

The Mortgage Payment

Most everyone understand the basic aspects that make up a loan payment, principal payments and interest payments, because they own cars or credit cards. However, mortgage loans have a couple more variables that must be added into the equation.

Mortgage Insurance

For a couple types of mortgages, you will have to pay mortgage insurance, but for conventional loans, the borrower must only pay for mortgage insurance if they do not pay a down payment of 20%. The insurance is protection for the lender against any losses they might incur. The type of loan the borrower gets, the loan-to-value ratio, the borrower's credit score, and the loan balance. The mortgage insurance is calculated as a percentage of the loan balance.

Homeowner's Insurance

Another variable that gets added into your monthly mortgage payment is your homeowner's insurance. Home buyers will be required to open an escrow account. This acts as a savings account in which every month your mortgage servicer will deposit $1/12^{th}$ of your annual homeowner's insurance premium.

Property Taxes

Similar to homeowner's insurance, property taxes also get included into the home buyer's escrow account. The first-year of taxes will be pro-rated because the seller must pay for the portion of the year that they lived in the home. This requires that the buyer only pay for their portion to make up the rest of the annual property tax bill.

Each month $1/12^{th}$ of annual property taxes will be put into your escrow account and later removed when the annual bill is due.

Principal and Interest

Just like any other type of loan, your principal and interest are added into your monthly mortgage payment. The majority of your monthly mortgage payment will be principal and interest. Each month the amount of interest being paid goes down as the amount of principal goes up, reducing the outstanding balance a little more every month.

Underwriting

The underwriter will be the individual that reviews the borrower's entire loan file. The underwriter will review the loan application and type of loan the borrower needs, and compare that information with the guidelines and regulations of that specific loan type.

There are three decision-making principles that determine whether your loan will be approved.

Credit – A borrower's credit history is one of the stronger indicators on whether they will be successful in obtaining a loan. Their history of paying off different types of debts sends the lender a strong message that they have the intention of repaying the loan.

Capacity – The underwriter will look to make sure that the borrower has enough income to pay for the loan. The underwriter will determine this by looking at the borrower's regular wages, overtime wages, as well as any possible commissions. All of this factors in to the underwriter's determination of whether the borrower has the capacity to take on the mortgage loan.

Collateral – This principle is where the appraisal and title insurance binder come into play. The underwriter will check the appraisal to make sure there are no issues with the home as well as check the value of the home against the comparable homes. The title insurance binder will be checked to make sure that there are no liens on the home that could possibly prevent the buyer from taking ownership.

Once the underwriter has determined that each principle has been met to the standards necessary for the type of loan the borrower is getting, the loan will move on to closing.

Closing

After the underwriter has approved the borrower's loan and sent over their file to closing, the borrower will still need to present a couple items. In the case that the buyer will need to use an escrow service, the buyer will need to set up their insurance policy, determines how much they will pay to the escrow account to replace the value of the home, in the case of a hazard. The buyer will also need to set up their property tax statement. This statement will let the buyer know how much money out of their monthly mortgage goes to their escrow account to pay for property taxes.

Also, at closing, an attorney or representative from a title company will need to be present. The attorney or title representative will be there to help facilitate the transaction. They will identify both parties, notarize all documents that must be notarized, and explain any documents that the buyer and seller may not understand. Lastly all closing, all the numbers and terms of the will be laid out for everyone to see.

The buyer and seller will have many documents to sign and get them explained to them, if they would like. Once all documents are signed, and all questions are answered, you have completed your home buying process!

Summary

As you have just read, there are many steps and details included during the home buying process. However, if the home buyer is able to get their financial documents together, be realistic in their expectations, and maintain in swift and consistent contact with their loan officer, they can have an enjoyable experience buying their first home!