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When Not to Buy a House

1. *Are you going to move in the next five years?* Real estate is a good investment *if you hold on to it for at least five years*. Any less than that and the house in most areas won't appreciate enough to get your expenses out of it—i.e. you won't have any new equity in the house. That means it's not a good idea to buy when you are moving to a city on a temporary assignment or if there is a chance you could get transferred in the next one or two years.
2. *Is your life in a state of flux?* It's not a good idea to buy a house when you are right out of school, between jobs, or likely to marry but not yet engaged. That dream job you just interviewed for may fall through, and you may have to take a job in a different town. Or, as unbelievable as it seems you could meet someone else and get married in a year or two. If you have a house, your new bride or groom will inevitably hate it because he/she has different tastes from yours. Or he or she may already have children and the house you bought it not big enough for your new family.
3. *Have you been married less than a year?* Married couples should wait at least a year before buying a house. That gives you time to figure out the perfect distance from the in-laws, as well as time to get to know each other, start defining your mutual tastes, pay off past debts, and save money. Your parents and in-laws may start saying, "you are throwing money down a rat hole by renting." Ignore them for at least a year. You probably are not ready to buy yet.

4. *How much of a down payment do you have?* You need to have saved at least 5 percent to even be considered for a mortgage loan. Twenty percent is even better. With twenty percent you can avoid paying private mortgage insurance (PMI), which protects the mortgage company in case they have to foreclose on you and sell the house at a loss. PMI insurance costs about \$47 a month per \$100,000 of loan so you can save almost \$600 a year on a \$100,000 loan if you pay 20 percent down.
5. *Do you already have an emergency fund savings account of at least \$1,000 you won't be dipping into for your down payment on your home?* You could end up in trouble and house poor if someone gets laid off or you have a financial emergency such as medical bills or car repairs.
6. *Have you paid all your debts?* Pay off all your other consumer debt before putting all your savings, less your emergency fund, into a down payment on a home.

If you answered yes to any of the above questions, you are not ready to buy a house now. But that is now. Remember, it will take you about two years to reach your IDA savings goal. During that two years you can build up your emergency savings account and pay off all your consumer debts. Your life can settle quite a bit and you will have a better idea of where you want to live for five years, who you are going to be married to, and just how close you want to live to your in-laws.

Adapted from material in The Financial Peace Planner by Dave Ramsey.

How Much House Can I Afford?

Purchasing your first home is exciting! Homeownership is the most common symbol of the American Dream. You get to begin investing in yourself instead of investing in your landlord. Homeownership builds wealth through the increasing equity in the home, but even more importantly, it offers the potential to build an asset that can be transferred to future generations.

Many things figure into the selection of this home. You need a home that is large enough to accommodate your family and family members yet unborn! You want a home in a location convenient to your work or your children's school or is close to family and friends. You may have a personal preference for older homes on tree-lined streets or you may want to live in a new subdivision. But perhaps the biggest item to consider is, **How Much House Can I Afford?**

Take a few minutes to complete the worksheet below. It is similar to the worksheets we completed when we were doing our budgeting session and you may want to refer back to those worksheets for answers.

Part One Total Monthly Income

Monthly salary/wages before deductions \$ _____

Any other regular monthly income \$ _____

Total Gross Monthly Income (GMI) \$ _____

Part Two Total Monthly Debts

Car loan payments \$ _____

Student loans \$ _____

Child Care \$ _____

How Much House Is That?

Based on a 30-year fixed-rate 6% mortgage and assuming the property taxes and insurance do not total more than \$125 per month you can estimate the size of mortgage you can afford if you know the size of monthly payments you can afford. You can use the following table as a rough guideline of what you could afford.

If you can afford a monthly house payment of \$350 . Your total home mortgage can be:

\$350	\$37,500
	3% Down <u>1,160</u>
	Home Cost \$38,660

If you can afford a monthly house payment of \$450 . Your total home mortgage can be:

\$450	\$54,000
	3% Down <u>1,670</u>
	Home Cost \$55,670

If you can afford a monthly house payment of \$550 . Your total home mortgage can be:

\$550	\$70,000
	3% Down <u>\$2,165</u>
	Home Cost \$72,165

Is It Better for Me to Buy or Rent Right Now?

Here is an example of a price comparison of purchasing or renting a 3 bedroom, 2 bath home in the same area.

Purchase Price	75,000	Monthly Rent	575
Down Payment (10%)	<u>7,500</u>	Security Deposit	<u>200</u>
Closing Costs (2.5%)	<u>1,875</u>		
Mortgage Rate	<u>6.5</u>		
Loan Term (years)	<u>25</u>		
Number from table	6.7521		
Multiplied by the	<u>75</u>		
Total Loan Amount (number in thousands)	<u>506.41</u>		
Monthly Payment	<u>506.41</u>		

Remember that you will now be responsible for all the maintenance, physically and financially. Do you want to mow the lawn every week or pay someone to come do it for you? Does your budget allow for leaky roof repairs? Consider these extra time and money costs before you commit yourself, selling isn't as easy as buying and buying wasn't very easy.

Table: Monthly payment per \$1,000 Borrowed

Interest Rate (%)	Number of Years Financed		
	15	25	30
5.0	7.9079	5.8459	5.3682
5.5	8.1708	6.1409	5.6779
6.0	8.4386	6.4430	5.9955
6.5	8.7111	6.7521	6.3207
7.0	8.9883	7.0678	6.6530
7.5	9.2701	7.3899	6.9921
8.0	9.5565	7.7182	7.3376
8.5	9.8474	8.0523	7.6891
9.0	10.1427	8.3920	8.0462
9.5	10.4422	8.7370	8.4085
10.0	10.7461	9.0870	8.7757

Homeownership

You may use the table from the previous page to fill out this table when you are considering a purchase. If the purchase price appears to high consider purchasing a different house or continue renting if the cost of purchasing is not within your means right now. Try to squirrel away some savings towards the down payment and closing costs for a while longer, then evaluate your purchase decision again.

A home is a good asset, but not if you are working solely for the house payment. You need to put money into other things including some type of recreation. You don't want to be house poor (paying for a nice house, but barely making ends meet). Learn to manage your money and stick with a budget so that you won't become house poor.

Purchase Price	_____	Monthly Rent	_____
Down Payment (10%)	_____	Security Deposit	_____
Closing Costs (2.5%)	_____		
Mortgage Rate	_____		
Loan Term (years)	_____		
Number from table	_____		
Multiplied by the	_____		
Total Loan Amount	_____		
(number in thousands)	_____		
Monthly Payment	_____		

Adapted from Planning Your Financial Future, second ed., by Louis E. Boone, David L. Kurtz, Douglas Hearth

Instructional Designer Sally Kahl

Get the Most House for Your Money

Buy a used home instead of a new one. You'll get more square footage and a better buy.

Buy a house that is not very attractive now but could be. Potential is everything. Bad landscaping, ugly carpet pet stained carpet, avocado green wallpaper, and the Elvis print in the bedroom can all become negotiating points and reasons to ask the seller to lower the price. These are

characteristics of the house that can be fixed. What you don't want to buy is a poorly built, architecturally ugly house, one that needs a new foundation or face. Structural problems will come back to haunt you when you try to sell the house.

Buy a good floor plan. Just because a house is big doesn't mean the space is well used. Some houses have a lot of wasted space, such as in a corner where you can't put anything. As you walk through the house, notice whether there is a wall to put the couch on or a space to put the bed without covering a window. Also look at the floor plan in terms of your needs. If all of your children are small (or maybe not yet born) you may not want a floor plan that has bedrooms on a different floor from the master bedroom. However, if you have teenagers (or soon to be teenagers) different floor bedrooms can be very nice.

Buy a house near water or with a view. Aesthetics are everything when you are trying to sell a house, so buy a house in an attractive area. Avoid buying a house that overlooks an electrical plant or that is near an airport or freeway where you have to listen to plane or truck noise. In fact, it may be helpful to visit the neighborhood at several different times of day to observe the traffic on the street, whether there are families out in the yards, and what kind of noise pollution is in the area.

Make sure the house and the location fit your lifestyle now. If you have school age children, being close to schools may be the most important consideration when selecting a location. If your children are nearly grown you may prefer to be out of town and away from neighborhood noise.

Check on utilities and services. If your house is not in an area with city water and sewer, check on the condition of the well and septic system. If it is an all electric home, ask to see the electric bills from the past few

years. In fact, you have a right to ask about the utility bills of the past few years on any house you buy.

Check on the taxes and insurance. If you are buying a home through a realtor, he or she should have this information. If you are buying independently, be sure to ask about the taxes and cost of homeowners insurance for the past several years. One price we pay for living out in the country is higher fire insurance rates. Check to see what they are so you can factor them into the cost of owning the house.

Creative Financing*

The most common form of home financing is through a bank or other traditional financial institution. This is known as a conventional loan. However, there are other options for home financing. When you begin your search for a home to buy spend as much time searching for your financing as you do looking for a home.

1. *Conventional loan.* You usually obtain conventional loans through a bank or other traditional financial institution. Down payment is usually between 5 to 20 percent.
2. *VA, or Veterans Administration loan.* The Veterans Administration insures these loans, which were designed to benefit veterans and allow a true zero-down purchase. Competitive interest rates make these appealing.
3. *Owner financing.* This is sometimes called buying on contract. If the current owner is willing to finance the home you pay the owner the agreed upon monthly payments instead of paying the mortgage company.

One benefit of owner financing is it provides flexibility in the way you pay off the loan. For example, if the house needs a lot of work, you may agree with the owner to forgo payments for a year so you can put your money into fixing up the house. Or you may decide to pay graduated interest rates or receive a discount for early payoff. One word of caution with owner financing. *Get everything in writing.* This protects both the buyer and the seller. It may be worth the expense of hiring an attorney to draw up the contract to protect both parties from disagreement later about the accepted terms of the sale of the house and the financing of the house.

4. *Assumable loans.* These are pre-1986, fixed-rate FHA and VA loans that can be assumed without any bank qualification. The buyer pays the seller the equity he has in the house and takes over the loan.

Also look for creative forms of down payment. Most of the down payment from my first home came in the form of *sweat equity*. My husband and I did much of the work on the construction of the home – painting the interior and exterior, shingling the roof, laying drainage tile around the foundation, etc. and that labor applied to the down payment on the home.

**Adapted from The Financial Peace Planner by Dave Ramsey*

Contract Considerations When Buying a House

I. General Contract Principles

- A. A Contract is a Binding Legal Document.** What is in writing counts, even when the other side says they won't hold you to it. If you don't understand it, don't sign it.
- B. Parties are free to agree to virtually any term in a contract, and all terms are negotiable.** The only practical limitations are:
 1. Both the buyer and seller must agree.
 2. The title insurance will insure the title

3. The lender will approve the loan.

II. Comments on the terms of the Contract


A. Purchase Price The contract must be subject to the buyer's ability to obtain financing. The terms must specify:

1. The amount of cash paid at closing (the down payment)
2. The type of loan (conventional, VA, FHA, etc.), and the amount of the loan.

The terms must include:

- a. The loan to be payable over a period of ____ years
- b. Discount points not to exceed _____ percent of the loan at closing
- c. Interest rate will be: (check only one blank)

 Fixed(a) rate not to exceed _____ percent per year; or

 Variable rate with an initial rate not to exceed ____ percent per year and a maximum rate not to exceed _____ percent per year.

B. Loan and Closing Costs. Who pays these is negotiable, but there are some rules of practice:

1. Buyer pays all costs related to the loan.
2. Seller pays for title insurance for buyer.
3. The parties generally split the costs of closing the loan.

C. Earnest Money This is not the same thing as a down payment. It is a sign of good faith, and a minimum penalty that will be forfeited if Buyer cancels the contract without a legal right to do so or otherwise breaches the contract. At closing, this amount is credited toward the down payment. Generally, \$500.00 is sufficient earnest money, but the exact amount is negotiable.

D. Conveyance. Issues related to how title is held and whether mineral rights will be included should be specific.

E. Title Requirements. Seller should furnish, at Seller's cost, title insurance in the amount of the purchase price. Buyer pays for the lender's title policy. It is good practice to insist that the title policy not exclude tax liens, bankruptcy filings, and child support matters. It is common practice for title insurance companies to exclude these clouds on the title, but the average buyers are not equipped to investigate these matters for themselves. Study all title exceptions carefully.

F. Survey. If a survey is required, its due date and who pays for it should be set forth.

- G. Prorations.** Real property taxes are prorated as of the date of closing.
- H. Closing.** A date is set, with provisions for extension, if, for example, the lender is slow getting the final loan paperwork together.
- I. Possession.** Possession is generally delivered to the buyer at closing. If the seller stays after closing, rent should be agreed on, and a lease signed.
- J. Other Contingency.** Any other conditions whatsoever that give either party additional rights to cancel the contract should be specified.
- K. Fixtures and Attached Equipment.** A fixture is an item of personal property that is attached to real property. Example: window air conditioners. If the seller keeps anything, it should be specifically excluded.
- L. Inspection and Repairs.** Buyer should spell out inspection rights and time limits. If Seller is obligated to make repairs, a dollar limit should be specified. Beware of “as is, where is” sales – INSPECT, INSPECT, INSPECT.
- M. Home Warranty.** If one is offered, specify any conditions relating to it.
- N. Seller Property Disclosure.** This is a realty form containing a lengthy list of questions relating to the property’s condition. It is informational only. Never rely on a disclosure. It is NOT a substitute for a thorough inspection.
- O. Termite Control Requirements.** Lenders require a termite treatment and certificate. Spell out who pays for it.
- P. Lead-Based Paint Risk Assessment/Inspection.** This is an issue for houses built before 1978 and for houses of unknown construction dates. Buyer needs to condition the contract on lead-based inspection if that is an issue.
- Q. Risk of Loss.** Risk of loss or damage to the Property before closing must be assumed by Seller. (Only Seller has an insurable interest prior to closing)

III. Other Matters

- A. Insurance.** Most lenders require payment one (1) year in advance.
- B. Private Mortgage Insurance (“PMI”).** Do not assume that the lender will drop this requirement when you have paid 20 percent of the loan.
- C. Final Inspection.** Generally this may be requested within 24 hours of closing.

Material developed by Justin L. Garrett, II, Attorney at Law

Appendix A

The Fannie Mae Foundation has some excellent publications to help more Americans better understand what it takes to finance a home and how the mortgage process works.

If you or any of your friends, relatives, or neighbors would like more information on the home-buying process you may get some well-written information at no cost.

For a free copy of *Opening the Door to a Home of Your Own* or *Choosing the Mortgage That's Right for You* call Fannie Mae.

When you call ask for the publications by name.

For free copies of *Opening the Door to a Home of Your Own* in English, Chinese, Korean, Vietnamese, Russian, Haitian-Creole, Polish, or Portuguese call 1-800-688-4663.

For free copies of *Opening the Door to a Home of Your Own* in Spanish call 1-800-782-2729.

For a free copy of *Choosing the Mortgage That's Right for You* in English, call 1-800-688-4663.

Appendix B

United States Department of Agriculture as a Home Lender

If you want to own a home in a rural area, United States Department of Agriculture (USDA) Rural Development may be able to help. Any community with a population of less than 25,000 qualifies as a rural area which would only exclude Fayetteville, Springdale and Rogers in this area.

Home Purchase Programs

Section 502 Direct Loan Program

Benton, Washington, Madison Counties – call 501-273-9018 ex 4
Carroll, Newton, Boone, Baxter Counties – call 870-741-8600 ex 4

The Direct Homeownership Loan program is available to lower income individuals and families who wish to live in rural areas, cities or towns. Under the program individuals and families receive a loan directly from Rural Development. Payments are based on income, with no down-payment required. As an IDA participant you would have money for a down-payment. This would allow you to get a lower mortgage and have lower monthly house payments. Or perhaps you would be able to use your IDA savings towards improvements on the home. You must be unable to obtain a homeownership loan from a bank or other conventional sources.

Loans under the Direct Homeownership Loan program are made to families with incomes below 80% of the median income level of the communities in which they intend to live. Call your local USDA office to see what that income level is.

Loans under this program may be made for the purchase of an existing home or to build a new home.

Other uses include purchasing and preparing sites – including providing water and sewage facilities – and repairing or renovating a house being purchased.

Each USDA office has a very limited number of Direct Loans available each year. If you are interested, you should inquire soon.

Guaranteed Loans

If your income is too high to qualify for a direct housing loan, you may qualify for a guaranteed loan. These loans are made by lenders, such as banks or credit unions, and are guaranteed by Rural Development. This allows other lenders to make loans to people they would not otherwise be able to serve. Guaranteed housing loans are available to applicants whose incomes are below 115% of the median area income.

Appendix C

United States Department of Agriculture as a Lender for Home Repairs

If you are already a rural homeowner and your house needs repairs or modifications to make it accessible to a person with a disability, you may be eligible for home improvement or repair assistance through USDA Rural Development. Any community with a population of less than 25,000 qualifies as a rural area which would only exclude Fayetteville, Springdale and Rogers in this area.

Home Improvement and Repair Programs

Section 502 Single Family Housing Home Improvement Loans

Benton, Washington, Madison Counties – call 501-273-9018 ex 4
Carroll, Newton, Boone, Baxter Counties – call 870-741-8600 ex 4

In addition to providing loans for the purchase of a house, the Section 502 Single Family Housing Direct Loan program can help lower income rural homeowners make vital improvements to their homes. Section 502 loans are available to make substantial home repairs when other loan options are not available.

Section 504 Home Repair Loan and Grant Programs

For families and individuals with very low incomes, Rural Development makes loans for repairs to improve or modernize a home, make it safer or more sanitary, or to remove health hazards. For seniors 62 and older who cannot afford a loan, grant funds are available for these repairs.

The most common types of repairs financed by the Section 504 program include fixing or replacing roofs, modernizing heating or wiring systems, and making houses accessible to people with disabilities.

You can also apply for funds to install insulation and storm windows, put in a septic system and install or repair a bathroom.

The maximum amount you can borrow under the Section 504 Home Repair Loan program is \$20,000. The interest rate for these loans is 1% and is limited to very low-income rural residents whose incomes fall below 50% of the areas median income.

For very-low-income homeowners 62 and older who can't afford to borrow the full amount required to make the necessary repairs, grant funds are available. Grants may be used or to remove health or safety hazards or to remodel dwellings to make the house accessible to household members with disabilities. Grants are limited to \$7,500. They are often combined with loans to increase the amount available for repairs.