Planning for the Future: Buying a Home

The Housing Market in 2020

You might think that the economic downturn caused by the COVID-19 pandemic would also cause the housing market to fall. But, as of August 2020, we've seen quite the opposite.

According to a recent article by BankRate,[1] here are some housing trends in 2020 to keep an eye on:

- Home prices are holding steady, at least for now. Given the coronavirus pandemic and recent economic instability, some sellers are delaying selling their homes, which is causing a reduction in the number of available homes. When you have a decreased number of available homes on the market, that increases the demand since there are fewer homes to choose from. Realtors are even seeing bidding wars during home sales, which cause housing prices to increase.

- There is more demand for houses in the suburbs. When the coronavirus hit in early 2020, many city dwellers started looking for more suburban, less crowded housing options. In addition, with more and more Americans working from home, it became less important to live close to where you work. This trend may reverse once the pandemic subsides and those who moved out of the city want to return.

- Mortgage rates are at a record low. As of July 2020, the average 30-year fixed mortgage is 3.31 percent, including points. Experts predict that mortgage rates will stay low well into 2021. Keep in mind, though, that as mortgage rates drop home prices usually increase.

If you are wondering whether homeownership is a possibility for you, or want to know what to plan for

[1] Ostrowski, Jeff. "6 mortgage and real estate trends for the third quarter of 2020." Jul. 20, 2020. *Bankrate.com* https://www.bankrate.com/real-estate/housing-trends/

and how to get started, this guide will walk you through the following steps:

1. Getting ready;
2. What can you afford?
3. Know your rights: Fair housing laws and predatory lending laws;
4. Mortgage preapproval;
5. Homes, realtors, and shopping for homes;
6. Home inspectors;
7. All about loans, conventional and FHA;
8. Other home-buying programs;
9. Homeowner's insurance.

Getting Ready

The decision to buy a home is one of the most significant financial choices most of us will make in our lifetimes. Buying a home can be a good investment, but whether to buy or continue renting depends on your circumstances. If there is a reasonable chance that you might relocate in a couple of years, then it probably would be better to continue renting.

There are quite a few buy or rent calculators available online that can be helpful if you're unsure. The tool will help you get a better sense of the financial commitment involved in home ownership. "Is It Better to Rent or Buy?" can be found at https://www.realtor.com/mortgage/tools/rent-or-buy-calculator/

If you want to be well-poised when the time comes to buy, then you should begin minding your financial situation early. It will much easier to get approved for a loan if you have a good credit score. If you are able to pay down some of your debts, you'll qualify more easily, too. Lenders will look to see that you have a pattern of paying your bills on time. They will also evaluate your total debt versus your income. You can find more information about credit scores and debt-to-income ratios in this guide's section on loans.

What Can You Afford?

Think about how much you can afford. After you evaluate your finances, decide how much you want to allocate to monthly payments on your home. Remember that the figure should include not only the principle and interest on your loan but other predictable expenses. These include:

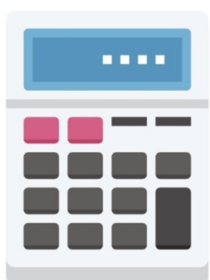
- homeowner's insurance;
- property taxes;
- dues for a homeowner's association; and
- other maintenance costs like regular upkeep, lawn care, garbage removal and utilities.

There is an old rule of thumb for determining how much of your income you should reasonably spend on housing costs. The ballpark figure is no more than 30%. You will hear this, or something like it, from banks, landlords, your parents, friends and advisers. It is, in fact, formally ensconced by lenders in two forms. Conventional lenders, meaning regular mortgage lenders that aren't insured by the Federal Housing Administration (FHA), typically want the figure to be 28%. FHA loans, by contrast, use 31% for the figure.

However, it is certainly possible you will qualify for a loan even when your mortgage payment will be more than 28% of your monthly income; it's just easier to qualify if you stick to the 28% figure.

The 30% "rule" goes back to the 1960s Brooke Amendment or to depression-era policies, depending on who you ask. The National Housing Act of 1937 legislated a public housing program. At the time, it was decided that families whose housing costs were in excess of 20% of their income were, by official measure, "burdened" by those costs. (How things have changed.) In 1969, the Brooke Amendment to the National Housing Act established a rule for determining the monthly payments that were collectible from residents in public housing. It started out at 25%, actually, and this was raised to 30% under Ronald Reagan. That number stuck although many bankers and others dispute its utility. Still, it's hard to argue with the general idea of the 30% rule. The better you are able to provide adequate housing for yourself and family without spending all of your money on it, the better.

Mortgage Calculators



There are a number of mortgage calculators online that can help you estimate the monthly payments on a mortgage with different variables, like the loan term, down payment amount, and the interest rate.

Try the Federal Housing Administration's calculator at www.fha.com/calculator_afford.

How Much Can You Afford?

Here is a rough sketch of what you might want to budget for monthly rent, using the 30% rule, alongside the home value of a mortgage that has the same monthly cost.

Annual Salary	Budget for Monthly Rent: =30% of your Monthly Income	Home Value, based on a 30-Year Mortgage with a Monthly Payment = 30% of your Monthly Income*
15,000	375	79,000
20,000	500	105,000
25,000	625	131,000
30,000	750	158,000
35,000	875	184,000
40,000	1,000	210,000
45,000	1,125	237,000
50,000	1,250	263,000
55,000	1,375	289,000
60,000	1,500	316,000
65,000	1,625	342,000
70,000	1,750	368,000
75,000	1,875	394,000
80,000	2,000	421,000
85,000	2,125	447,000
90,000	2,250	474,000
95,000	2,375	500,000
100,000	2,500	526,000
150,000	3,750	789,000
200,000	5,000	1,050,000
250,000	6,250	1,310,000
300,000	7,500	1,570,000

*Calculations are estimates based on the following parameters: a 20% down payment, 3.222% interest rate, 30 Year Mortgage, with 1.23% property tax and 0.35% homeowners insurance per year.

Fair Housing

The Civil Rights Act of 1968 fought widespread practices of segregation and discrimination in the housing market. Title VIII of the 1968 Civil Rights Act is also known as the Fair Housing Act of 1968.

The act prohibits discrimination concerning the sale, rental, or the financing of housing on the basis of race, religion, national origin, sex, handicap, and family status. If you have concerns about discrimination, you can learn more by visiting the website of the U.S. Department of Housing and Urban Development, hud.gov, or by contacting your local Fair Housing Office.

There is no federal legislation at present that prohibits housing discrimination based on sexual orientation or gender identity. But, there are many state and local laws that strictly prohibit housing discrimination based on sexual orientation or gender identity. Visit https://www.hud.gov/program_offices/fair_housing_equal_opp/housing_discrimination_and_persons_identifying_lgbtq for more information.

There are also laws to ensure fair lending practices. For example, the Equal Credit Opportunity Act (ECOA) prohibits discrimination in credit practices on the basis of race, color, religion, national origin, sex, marital status, age, and some aspects of class-based discrimination, such as whether or not you receive income from public assistance. The Federal Reserve was once responsible for enforcing the ECOA. That responsibility passed to the Consumer Financial Protection Bureau (CFPB) when it was founded in 2010. If you feel that you have faced discrimination in lending or credit practices, you can go to the CFPB website at www.consumerfinance.gov and file a complaint.

Many newer rules were put into place after the housing bubble in the 2000s, when widespread practices of predatory lending became apparent.

What is predatory lending? While each situation has its own circumstances, there are certain practices that stand out as predatory:

Equity stripping. If a lender makes a loan to someone who is realistically unable to repay it, then forecloses and seizes the house in order to sell it, this is called equity stripping.

Bait and switch. You might sign for a loan with a variable interest rate thinking it's a fixed rate because the details were hidden in the fine print, only to find out months later that your rate has increased. You've been sold

one product and given another, classically called bait and switch.

Packing. This predatory practice can occur with any kind of contract. You sign for a loan, only to discover later that it's been packed with services, and charges for them, that you didn't know were there.

In order to discourage predatory practices, beginning in 2011, the Consumer Financial Protection Bureau requires lenders to give you clear and accurate information about your mortgage during the lending process. This is called the "Know Before You Owe" rule, and it was made mandatory by the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA).

What does "Know Before You Owe" look like in practice? The rule requires lenders to give you two forms. The first form, the Loan Estimate, describes plainly and clearly the costs and risks of the loan. It's meant to help you with comparison shopping. The second form, the Closing Disclosure, shows all of the additional costs involved in the mortgage transaction. These disclosures are meant to help prevent loan packing and bait-and-switch attempts and other predatory practices.

Check Your Credit Score

It matters a lot. Credit scores, also called FICO scores, run from 300 to 850, the higher the better. The best mortgages, with the lowest costs, will go to borrowers with credit scores in the mid-700s or higher. But if your credit isn't that high, don't forget about buying just yet, you can still qualify for a mortgage. A 2018 Fannie Mae study reported that most people, including those who are actively planning on buying a home in the next three years, overestimate the minimum credit score and down payment required to qualify for a mortgage, and many are not familiar with available low down payment programs.[2] Fannie Mae's Eligibility Matrix sets the minimum credit score at **620**.

If your credit score is low, you can improve it by paying down debt, especially credit card debt, and getting any mistakes corrected. Remember that it takes time for changes to be reflected in your credit score, so the more conscientious you are early on, the better.

2 Palim, et. al. "Consumers Continue to Overestimate Mortgage Requirements" Fannie Mae, June 5, 2019. https://www.fanniemae.com/portal/research-insights/perspectives/mortgage-requirements-consumers-060519.html

Online Banks vs. Brick & Mortar

You have a lot of options to consider when choosing a mortgage lender, and now, more than ever, you're not limited to the bank in your neighborhood. Here are some things to consider when deciding whether an online bank is a better option for you, compared to a neighborhood bank.

- Applying online makes it easier to comparison shop and fill out applications.
- Many of the brick and mortar banks now allow you to fill out a pre-qualification application online.
- The major benefit of a brick and mortar bank is that you have a point person with expertise to prevent holdups and push the loan through the underwriting process.
- Many online lenders can process loans more quickly because they aren't subject to the same strict regulations as large commercial banks.
- Also, some online lenders will look at "non-traditional" qualifications, such as education and career experience to get you approved.
- Whether going through traditional channels or through one of the many online offerings, it's important to shop around and do your homework, because fee structures can vary greatly from bank to bank.

Get a Mortgage Preapproval

A preapproval isn't necessary, but it will definitely help you stand out from other buyers, and it can speed up the mortgage process. That is, in fact, why it was invented. A preapproval for a mortgage differs from a standard loan preapproval in that it's a more formal commitment on the part of the lender. It's different than a pre-qualification, too.

Step 1. Pre-Qualification

This is an informal process where you meet with a lender, over the phone, on the internet, or in person, and provide information about your assets, liabilities and income. The lender will take a quick assessment of your information to provide a rough estimate of the amount you might

expect to be approved for. Because this is an informal process, this is not a guarantee of a loan amount.

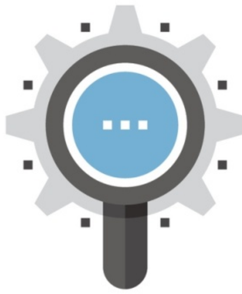
Step 2. Pre-Approval

To get a pre-approval, you'll have to provide all of the same information and paperwork as for a mortgage. The lender will do a full review of your credit history, your assets, income, and ability to pay before issuing the approval.

There is a fair amount of paperwork involved in obtaining pre-approval, so you'll want to start early. Typically, the lender will want to see the following:

- Federal income tax returns from the previous two years;
- Recent pay stubs that show your present income, including year-to-date;
- Bank statements for checking and savings;
- Quarterly or other statements on investments like CDs, IRAs, stocks, bonds, etc.;
- History of residence for the previous two years, including contact information for your landlord if you are renting; and
- Information about other real estate if you own any.

If you are shopping for a house with a pre-approval letter from your lender in hand, it suggests not only that you are a serious buyer; it means that the seller can anticipate with confidence that the deal won't fall through pending approval of your mortgage application. It also means, again from the seller's point of view, that the transaction is likely to close quickly.



Shopping for a Home

Once you have a good idea what you can afford, it's time to shop. Maybe you like shopping and maybe you don't. Either way, the more you know before you begin, the smoother the process and the more informed your decision will to be. Note that the average home buyer looks at ten houses over ten weeks[3], before making an offer on one, so settle in and be patient.

You'll want to look in the neighborhoods that you like, obviously, but remember to investigate the tax rates, crime statistics, commute times, accessibility to shopping, and schools if you have or are planning on having children. If

[3] https://www.realtor.com/advice/buy/how-many-homes-will-it-take/

there is a house that you particularly love, make an effort to visit the neighborhood several times, including during rush hour, so that you can get a clear idea what you're getting into. In cities, real estate firms sometimes offer guided tours of neighborhoods as a service distinct from open houses.

Make a list of your housing needs and wants. Prioritize your list of wants so that the most important items are at the top of the list. As you are shopping for homes, keep this list in mind to help you stay on track.

Take your time as you look at each property. Do you feel comfortable there? Is the house in good repair? Look inside closets and bathrooms. Is the roof in good shape? Is the neighborhood to your liking? Is the house on a busy street? Bring a digital camera and a notebook, so you can review photos and notes later.

Types of Homes

Most homes on the market are **detached single-family residences.** You will have the greatest amount of freedom to alter the property – repaint, renovate, build – if you buy a detached home.

Detached houses are preferred by most buyers, and, as a result, they have increased in value – at least in recent years – at a higher rate than other options. However, especially in urban or suburban areas close to a city, condos and townhouses are in plentiful supply and might be your preference.

What is the difference between a condominium and townhouse?

A **townhouse** is a single-family home that shares one or more walls with other single family homes. The buyer owns the interior and exterior walls, the roof and the property on which the townhouse sits, and is responsible for their maintenance. The owner also maintains insurance for both the home and property. Shared spaces, parking areas, trash removal, snow plowing are handled by the **Home Owners Association** (HOA).

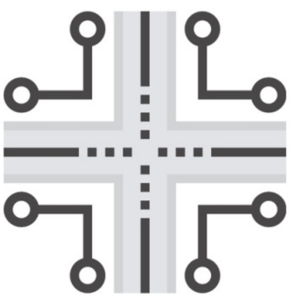
A **condominium**, or condo, is a building or group of buildings with individual units. The buyer owns and maintains the interior of their unit, but does not own the property that the building is on. In this case, the exterior of the building, parking area, lawn and other shared spaces are maintained by the Home Owners Association (HOA). The buyer is responsible for their own homeowners insurance, but insurance for the property is shared and is paid via dues to the HOA.

There are all sorts of variations for what the HOA controls and what the owners of individual units are responsible for. If you're looking at a townhouse, be sure to study the details carefully. Townhouses are considerably less expensive than detached houses, and many buyers prefer the convenience of having the HOA tend the landscaping and parking area for their home.

A condominium will typically offer less privacy and higher HOA costs, but more affordability than either townhouses or detached houses, and they may offer amenities like a door man, a gym, a swimming pool, etc. They are more common, naturally, in cities.

You also might want to consider a **cooperative**, also referred to as a co-op. Unlike a condominium or townhouse, where the buyer owns the deeds to their dwelling, in a co-op the buyer becomes a shareholder in a corporation that owns the property. As a shareholder, you have exclusive use of a housing unit on the property. If you buy into a co-op, you would take out a "share loan" instead of a traditional mortgage. You will also be responsible for paying the corporation for maintenance fees for running and maintaining the property. Co-ops can be less expensive than renting an apartment, especially in areas where cost of living is relatively high.

If privacy is one of your goals, then these shared living spaces might not be right for you. But, if you are looking for a social atmosphere, or if you like the idea of having someone else manage the lawn chores or snow removal, a townhouse, condominium or cooperative might be the right choice for you.



Location, Location, Location

It's true! The location of your home is very important. Will you be happy there? Is it close to work, or will you have a long commute? Is it close to shopping and attractions? Is the neighborhood safe? Do you like the school system? The location of your home can affect its resale value too, so keep that in mind as you are selecting properties.

House Hunting: Checklist

Type of Home

___ Single Family Detached ___ Townhouse ___ Condominium ___ Cooperative

Price Range: ____

Square Footage: ____

Neighborhood/Location

___ City ___ Suburbs ___ Country
___ Close to Work ___ Close to Grocery/Shopping ___ Close to School/Daycare
___ Public Transportation ___ Close to Park/Playground

Interior

___ # Bedrooms ___ # Bathrooms ___ Single Level ___ Multi-Level
___ Open Floor Plan ___ Eat in Kitchen ___ Formal Dining Room ___ Master Suite
___ Finished Basement ___ Fireplace

Heating System

___ Furnace ___ Oil Heat ___ Gas Heat ___ Electric Heat
___ Wood Burning Stove/Fireplace

Storage

___ Walk in Closets ___ Laundry Room ___ Attic ___ Basement ___ Outdoor Shed

Exterior

___ Pool ___ Patio/Deck ___ Garage ___ Security System ___ Pet-Friendly

Priorities

_____ Price/Affordability _____ Location
_____ Commute to Work _____ School System
_____ Privacy _____ Storage Space
_____ Outdoor Space _____ Architectural Style
_____ Modern vs. Historical _____ Move-In Ready
_____ Needs Renovations _____ Fenced Yard
_____ Play Area _____ Garden
_____ Other: ____

Notes: ____
____
____
____
____

Hiring a Realtor

Real estate agents have not gone the way of travel agents. In fact, according to 2019 data from the National Association of Realtors, 89% of buyers purchased their homes that year through real estate agents or brokers. That's up from 69% in 2001.[4]

On the other hand, 52% of home buyers that year actually found their home on the Internet, compared to only 29% who found the home that they bought through their real estate agent. So the question arises, do you need a real estate agent to buy your home? The short answer is yes.

Buying a house is a much more complicated transaction than buying a plane ticket, and a real estate agent does a lot more than point out closet space or stick signs in yards. A lot of things can happen between showing a house, signing a contract, and closing. A good, experienced agent will know how to negotiate to get you the best price. They will also be able to handle problems that might arise regarding appraisals, home inspections and repairs, lender requirements, and more.

If you're a buyer, your agent will receive a percentage of the total commission on the sale, along with the seller's agent. That commission – as well as your agent's portion of it – is decided by, and paid by, the seller who is listing the property.

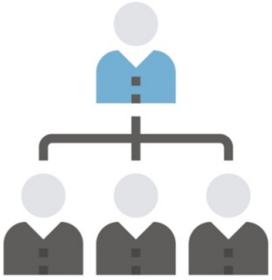
Most real estate business is commission based, meaning that if you don't buy a home, you don't owe any money to your realtor.

So what should you look for when looking for an agent?

Look for someone with experience and a good track record and who specializes in your market – both the neighborhood you prefer and the price range of the homes you are interested in. Look for someone who you feel comfortable talking to, who listens to your wants and concerns and who advises you about your options. You might want to ask about how much of their business is representing buyers. Some agents specialize in this; more commonly, an agent will have varying degrees of experience working with buyers and sellers. Some agents work part-time and others full-time. This might matter if you want your agent to be available quickly. An agent with another job might not be able to respond as quickly as you want.

See a sample list of questions to ask a potential realtor on the next page.

4 "Quick Real Estate Statistics." July 17, 2020. National Association of Realtors. www.nar.realtor/research-and-statistics/quick-real-estate-statistics.



Questions to Ask Potential Realtors

Having a good relationship with your realtor is important. Buying a home is a big decision, so selecting a realtor who will help guide you through this process will be a big help. Here are some questions to ask when interviewing potential realtors:

- How long have you been in the business?
- How many homes have you bought or sold last year? What was their price range?
- Is this your full-time job?
- Are you a member of the National Association of Realtors?
- Do you specialize as a buyer's agent? (That's a realtor who specializes in working with home buyers rather than sellers. Some realtors specialize in first time home buying too.)
- Which neighborhoods do you primarily work in?
- How many clients are you currently representing?
- How much time do I have to look at and review documents?
- Do you have recommendations for other professionals to work with, like a mortgage lender, home inspector or attorney?
- Can you provide me with some references from recent clients?

As a buyer, your real estate agent may ask you to sign a **Buyer's Broker Agreement**. This agreement outlines the rights and responsibilities the buyer and the agent. You can request that your agreement be non-exclusive, which means that you can work with several real estate agents.

You can also ask for a short term agreement, like a 15 or 30 day term. If you sign a Buyer's Broker Agreement on the first day that the realtor shows you listings, you can set the term for as little as 24 hours. You can also specify a price range or a neighborhood in this agreement.

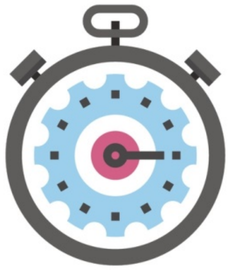
You don't need to sign a Broker Agreement right away. You can spend time with the realtor to make sure they are the individual you want to do business with, prior to signing any agreement.

You can ask for a satisfaction guarantee. That way, if things aren't working out, you can terminate the agreement so you can begin to work with another agent.

In most cases, the buyer works with their real estate agent and the seller is represented by a different real estate agent. There are situations where both the buyer and seller are represented by the same agent, also known as **dual agency**. This practice is illegal in some states and should be addressed with caution. You want your real estate agent to be hard at work to get the best deal for you!

A Buyer's Market or a Seller's Market?

This is all about supply and demand. If there are a lot of homes on the market and not very many buyers, then it's a Buyer's Market. If there are just a few homes for sale and a lot of buyers competing for them, then it's a Seller's Market. Knowing which type of market you're buying in will help you make better decisions about any offers you might make.

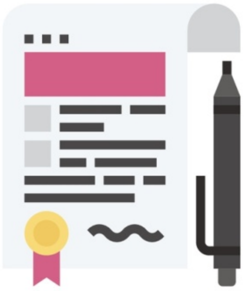


How Long Does it All Take?

On average, it takes buyers between thirty and sixty days to find a house they want to make an offer on. The time from contract to closing can take anywhere from a couple of weeks to two months. This doesn't mean you won't find the home you want in only week, but it should give you an idea of what to expect.

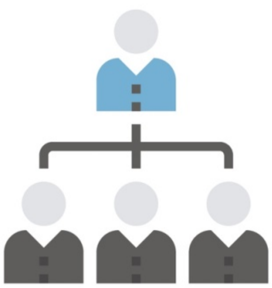
A common rule of thumb is to make an offer 5% below the asking price and negotiate from there. But, this rule of thumb will not work in all cases. A house that has sat on the market for months might be poised to go for much less than the asking price. On the other hand, in a very competitive seller's market, an offer of 5% below the asking price might get rejected, since the sale price might end up higher than the listed price! In all cases, rely on the expertise of your realtor.

Your realtor can provide you with a list of comparable properties that have sold in the area, so you have a better picture of the local market.



Formal Offer

When you are ready, your realtor will write up a **formal offer**. The details of this step can vary, but typically the offer lays out some written contingencies that are to your benefit. You'll want to have an inspector look at the house before you actually buy it, so the offer will usually have a clause about that. Also, a formal offer can have a mortgage contingency that gives you the option of backing out if you are unable to secure the financing you need. If the seller accepts your offer, you'll have to give the seller a deposit to show your good faith while the financing is worked out. This will count towards the down payment.



Multiple Offers & Negotiations

In a competitive market, there may be several buyers making offers on a home at the same time. Your real estate agent will help you refine your offer to make it more appealing to the seller. Of course, being prequalified or pre-approved for your loan makes you more attractive to the seller than a prospective buyer who has not secured financing yet.

Some things to keep in mind during counter offers or negotiations:

- Offering a larger good faith deposit;
- Increasing your offering price; or
- Buying the home "as is," which means that any repairs found during inspection would be the buyer's responsibility.

Home Inspection

Once you have an accepted offer, it's time to hire a home inspector. Your real estate agent will probably have someone he or she recommends, but feel free to hire your own. Home inspectors are typically state-certified; ask if your inspector has certification. Also ask if he or she is a member of the National Association of Certified Home Inspectors or the American Society of Home Inspectors. Both organizations require members to have performed at least 250 inspections, so membership is a good sign that they are experienced and knowledgeable. The cost is usually a few hundred