


## Assess Your Debt

## Ten Questions to Ask Before You Get Your Next Mortgage

Whether you are one of millions of Americans hoping to refinance your adjustable rate mortgage (ARM) to a fixed rate loan before your interest rate rises, or you are hoping to take advantage of the buyer's market in many parts of the country to purchase a home, you want to find the best mortgage loan. After all, just a small difference in your interest rate can add up to thousands of dollars over the life of your loan.

But finding the right loan can be confusing and overwhelming. Don't be intimidated. Union members can turn to the **Union Plus Mortgage Program**, the nation's only mortgage with benefits that are not available to the general public. Here are ten smart questions to ask a loan officer before you apply for your next mortgage:

### 1. What type of loan is best for me?

There are many different types of loans, including:

- **Adjustable rate mortgages (ARMs)** which carry a fixed rate for an initial period (usually the first two to seven years) but then change based on current interest rates at the time of the change. These have been popular with homeowners who either expected to refinance or move after a few years, as well as those who needed the lower rate offered by an ARM to qualify for a loan. With interest rates rising, though, many borrowers with ARMs are finding it difficult to make their rising payments.
- **Fixed rate mortgages** are usually repaid in fifteen or thirty years. You make the same monthly payment toward the balance of the loan (principal and interest) until it is paid off or you refinance. Mortgage interest rates are still low by historical standards. Choosing a fixed-rate loan will likely be a safe choice because if rates rise over time your rate will not. And, if you cannot afford the payment on a fixed-rate loan, you may want to choose a less expensive home.
- **Interest-only loans** may offer a lower payment, because you only pay interest each month. But you don't reduce your loan balance, and at some point during the loan (usually at the ten-year mark) you will have to make significantly higher payments in order to pay back the amount you borrowed, plus the remaining interest. And, if your home value declines, you can find yourself owing more than what your home is worth.
- **Government sponsored loans** such as FHA or VA loans (for veterans) may offer lower down payments, but be sure to compare them to other available loans before you choose.
- **First-time home buyer programs** may allow you to purchase a home even if you do not have a lot of money saved for your down payment, or haven't established a strong credit history.

### 2. How much will my taxes and insurance cost, and who will make the payments?

In addition to paying back the principal and interest on your loan, you will be required to pay property taxes and homeowner's, or "hazard," insurance. If your home is in a high-risk area for floods (visit **www.floodsmart.gov** for information) you will also have to purchase flood insurance on your own and provide proof to your lender that you have done so.

Most borrowers choose to allow their lender to set up an escrow account to handle their hazard insurance and tax payments. If you choose this option, your monthly payment to your mortgage lender will include enough money to cover the estimated costs of these bills when they come due, plus a small cushion.

Many experts recommend first-time homeowners allow the lender to escrow taxes and insurance, so they won't have to worry about saving for those annual bills. Keep in mind, though, that your taxes and insurance costs may change each year, and if they do, the lender will increase your payment so it has enough money to pay the higher bills. That means that even with a fixed rate loan you may find your total monthly payments rising over time.

### 3. How much can I borrow?

Lenders will typically look at three things to determine how much you can borrow:

- Your estimated monthly mortgage payment including the amount needed to pay back the amount you borrowed (principal and interest) plus taxes and insurance. Together, that total payment for principal, interest, taxes and insurance is known as "PITI."
- They will compare your mortgage payment to your income to calculate what's known as your "front-end debt ratio." As a rule of thumb your mortgage payment should be less than 28 to 32 percent of your before-tax monthly income, though some programs allow for higher debt ratios.
- The lender will also take a look at your other debts such as credit cards, car payments and student loans, and add the minimum monthly payments on those debts to your PITI to come up with your "back-end debt ratio" or your total monthly debt compared to your gross income. Generally your total monthly debts shouldn't be greater than 38 to 42 percent of your before tax income, although again, some programs are more lenient.

You can get an idea of how much home you can afford by using the calculators at the **Union Plus Home Finance Center**. However, your best bet is to talk with a loan professional who can help you find out how much home you can afford.

### 4. What is my credit score?

When you apply for a loan, your loan officer will order your credit reports and scores from all three major credit reporting agencies. Ask your loan officer to go over each credit report with you line by line. Even if your credit rating is strong, there may be mistakes or debts that don't belong to you, and if those items are corrected you may be eligible for a better loan.

Your loan officer will also be required to provide you with a written disclosure of your credit scores. Most lenders use the middle of the three agency scores as a basis for choosing which loan programs and rates you can get. For example, if your credit scores are 680, 700 and 720, the middle score — 700 — will be used as the basis for choosing your loan program. Better credit scores usually mean better rates.

Tip: Don't wait until you have found your dream house, or need to refinance, to check your credit reports and scores. Review them early so you know where you stand and have time to correct mistakes. Union members can save on credit score information from MyFico with the **Union Plus Credit Score discount**. Another tip: At least a week before you apply for a mortgage loan call 1-888-5OPT-OUT or visit **www.OptOutPrescreen.com** to have your name removed from marketing lists sold by credit reporting agencies. Otherwise, the moment your loan officer requests your credit report, the credit reporting agencies will sell your name and personal information to other lenders as a "hot prospect."

### 5. Can I get pre-approved for my loan?

If you are buying a home, it is essential to get pre-approved for your loan before you start looking at homes. With a written pre-approval letter from a lender, a seller will be confident you can get a loan to buy their home. And you'll save time by only looking at houses you can truly afford to buy.

### 6. Can I lock in my interest rate?

Because rates can change daily, you may want to "lock" your interest rate when you apply. A rate lock guarantees you can get that rate (if your application is approved) and is usually good for thirty or sixty days. Ask for confirmation in writing that your rate has been locked.

### 7. What are my fees?

There are always fees associated with the cost of a mortgage loan. They may include the appraisal, title insurance, attorney fees, taxes, lender fees and more. Within three days of when you apply for a mortgage, the lender must send you a Good Faith Estimate spelling out the estimated costs of the loan. Question any fees you don't understand, and plan to bring the estimate with you when you close, to compare to the final closing statement. While some fees may vary somewhat at closing, you typically should not see new fees sprung on you as you are ready to sign the final loan papers.

Tip: While you may have seen advertisements for "no cost" loans, keep in mind that lenders still need to make a profit. Those no-cost loans may carry higher interest rates to offset the lack of fees. Let your loan officer compare a no-cost loan to other options before you make your decision.

### 8. Who will collect my payments?

The days of banks lending their own money and collecting payments until a mortgage is fully repaid are the exception now, rather than the rule. Most lenders will make a loan, and then sell the "servicing" to another lender. That means you may no longer be sending your payments to your original lender, but to a new one. Sometimes your loan servicing may be sold more than once. The **Union Plus Mortgage Program** never sells the servicing of your loan. Keep copies of your loan documents, payments, and your monthly statements in case any problems arise in the transfer of your loan.

### 9. Is there a prepayment penalty?

A prepayment penalty requires you to pay the lender a fee, which can vary based on the type of loan you select, if you pay off your loan before the prepayment penalty period ends. Many prepayment penalties (usually 1 percent of your mortgage amount) are good for one year, but some can last two or three years. A "soft" prepayment penalty applies only if you refinance your home, but a hard prepayment penalty applies if you sell or refinance. Avoid prepayment penalties if at all possible, and make it clear to your loan officer when you apply that you do not want a loan with a prepayment penalty.

### 10. What happens if I have trouble making my payments?

Few things are as stressful as falling behind on your mortgage, and one or two missed payments can quickly escalate into foreclosure. The **Union Plus Mortgage and Real Estate Program** for union members offers programs to help Union Plus mortgage holders make their payments if they are on strike, or if they become disabled or unemployed. You can talk to a Union Plus Mortgage specialist at 1-800-848-6466 (8:30 a.m. to 7:00 p.m. E.T., Monday - Friday) to discuss possible options.

The Save My Home Hotline through the **Union Plus Credit Counseling Service** (1-866-490-5361) offers advice from HUD-certified housing counselors if you are falling behind on your mortgage payments or are having money problems.

**Download a PDF of this article**



Union Plus benefits are for participating union members, retirees and their families.
Copyright © 2007 Union Privilege. All rights reserved.
Union Privilege, 1125 15th St., N.W., Suite 300, Washington, DC 20005