

Closing Costs & Information



Congratulations! You have decided to buy a new home. This will help you take this big financial step by describing the home buying, home financing, and settlement process. Lenders and mortgage brokers are required by federal law, the Real Estate Settlement Procedures Act (RESPA), to give you this information. You should receive it when applying for a loan, or within three business days afterwards. Real estate brokers frequently hand out a booklet as well. You probably started the home buying process in one of two ways: you saw a home you were interested in buying or you consulted a lender to figure out how much money you could borrow before you found a home (sometimes called pre-qualifying). The next step is to sign an agreement of sale with the seller, followed by applying for a loan to purchase your new home. The final step is called settlement or closing, where the legal title to the property is transferred to you. At each of these steps you often have the opportunity to negotiate the terms, conditions and costs to your advantage. This will highlight such opportunities. You will also need to shop carefully to get the best value for your money. There is no standard home buying process used in all localities. Your actual experience may vary from those described here. This takes you through the general steps to buying a home, to eliminate, as much as possible, the mysteries of the settlement process.

Buying and Financing a Home

Role of the Real Estate Broker

Frequently, the first person you consult about buying a home is a real estate agent or broker. Although real estate brokers provide helpful advice on many aspects of home buying, they may serve the interests of the seller, and not your interests as the buyer. The most common practice is for the seller to hire the broker to find someone who will be willing to buy the home on terms and conditions that are acceptable to the seller. Therefore, the real estate broker you are dealing with may also represent the seller. However, you can hire your own real estate broker, known as a buyers broker, to represent your interests. Also, in some states, agents and brokers are allowed to represent both buyer and seller. Even if the real estate broker represents the seller, state real estate licensing laws usually require that the broker treat you fairly. If you have any questions concerning the behavior of an agent or broker, you should contact your States Real Estate Commission or licensing department. Sometimes, the real estate broker will offer to help you obtain a mortgage loan. He or she may also recommend that you deal with a particular lender, title company, attorney or settlement/closing agent. You are not required to follow the real estate brokers recommendation. You should compare the costs and services offered by other providers with those recommended by the real estate broker.

Selecting an Attorney

Before you sign an agreement of sale, you might consider asking an attorney to look it over and tell you if it protects your interests. If you have already signed your agreement of sale, you might still consider having an attorney review it. An attorney can also help you prepare for the settlement. In some areas attorneys act as settlement/closing agents or as escrow agents to handle the settlement. An attorney who does this will not solely represent your interests, since, as settlement/closing agent, they may also be representing the seller, the lender and others as well.

*Please note, in many areas of the country attorneys are not normally involved in the home sale. For example, escrow agents or escrow companies in western states handle the paperwork to transfer title without any attorney involvement.

If choosing an attorney, you should shop around and ask what services will be performed for what fee. Find out whether the attorney is experienced in representing home buyers.

You may wish to ask the attorney questions such as:

- What is the charge for negotiating the agreement of sale, reviewing documents and giving advice concerning those documents, for being present at the settlement, or for reviewing instructions to the escrow agent or company?
- Will the attorney represent anyone other than you in the transaction?
- Will the attorney be paid by anyone other than you in the transaction?

Terms of the Agreement of Sale

If you receive this information before you sign an agreement of sale, here are some important points to consider. The real estate broker probably will give you a preprinted form of agreement of sale. You may make changes or additions to the form agreement, but the seller must agree to every change you make. You should also agree with the seller on when you will move in and what appliances and personal property will be sold with the home.

Sales Price: For most home purchasers, the sales price is the most important term. Recognize that other non-monetary terms of the agreement are also important.

Title: Title refers to the legal ownership of your new home. The seller should provide title, free and clear of all claims by others against your new home. Claims by others against your new home are sometimes known as liens or encumbrances. You may negotiate who will pay for the title search which will tell you whether the title is "clear."

Mortgage Clause: The agreement of sale should provide that your deposit will be refunded if the sale has to be canceled because you are unable to get a mortgage loan. For example, your agreement of sale could allow the purchase to be canceled if you cannot obtain mortgage financing at an interest rate at or below a rate you specify in the agreement.

Pests: Your lender will require a certificate from a qualified inspector stating that the home is free from termites and other pests and pest damage. You may want to reserve the right to cancel the agreement or seek immediate treatment and repairs by the seller if pest damage is found.

Home Inspection: It is a good idea to have the home inspected. An inspection should determine the condition of the plumbing, heating, cooling and electrical systems. The structure should also be examined to assure it is sound and to determine the condition of the roof, siding, windows and doors. The lot should be graded away from the house so that water does not drain toward the house and into the basement. Most buyers prefer to pay for these inspections so that the inspector is working for them, not the seller. You may wish to include in your agreement of sale the right to cancel, if you are not satisfied with the inspection results. In that case, you may want to re-negotiate for a lower sale price or require the seller to make repairs. Lead-Based Paint Hazards in Housing Built Before 1978. If you buy a home built before 1978, you have certain rights concerning lead-based paint and lead poisoning hazards. The seller or sales agent must give you the EPA pamphlet Protect Your Family From Lead in Your Home or other EPA-approved lead hazard information. The seller or sales agent must tell you what the seller actually knows about the homes lead-based paint or lead-based paint hazards and give you any relevant records or reports.

You have at least ten (10) days to do an inspection or risk assessment for lead-based paint or lead-based paint hazards. However, to have the right to cancel the sale based on the results of an inspection or risk assessment, you will need to negotiate this condition with the seller.

Finally, the seller must attach a disclosure form to the agreement of sale which will include a Lead Warning Statement. You, the seller, and the sales agent will sign an acknowledgment that these notification requirements have been satisfied.

Other Environmental Concerns: Your city or state may have laws requiring buyers or sellers to test for environmental hazards such as leaking underground oil tanks, the presence of radon or asbestos, lead water pipes, and other such hazards, and to take the steps to clean-up any such hazards. You may negotiate who will pay for the costs of any required testing and/or clean-up.

Sharing of Expenses: You need to agree with the seller about how expenses related to the property such as taxes, water and sewer charges, condominium fees, and utility bills, are to be divided on the date of settlement. Unless you agree otherwise, you should only be responsible for the portion of these expenses owed after the date of sale.

Settlement Agent/Escrow Agent or Company: Depending on local practices, you may have an option to select the settlement agent or escrow agent or company. For states where an escrow agent or company will handle the settlement, the buyer, seller and lender will provide instructions.

Settlement Costs: You can negotiate which settlement costs you will pay and which will be paid by the seller.

Shopping For a Loan: Our choice of lender and type of loan will influence not only your settlement costs, but also the monthly cost of your mortgage loan. There are many types of lenders and types of loans you can choose. You may be familiar with banks, savings associations, mortgage companies and credit unions, many of which provide home mortgage loans. You may find a listing of some mortgage lenders in the yellow pages or a listing of rates in your local newspaper.

Mortgage Brokers: Some companies, known as mortgage brokers offer to find you a mortgage lender willing to make you a loan. A mortgage broker may operate as an independent business and may not be operating as your agent or representative. Your mortgage broker may be paid by the lender, you as the borrower, or both. You may wish to ask about the fees that the mortgage broker will receive for its services.

Government Programs: You may be eligible for a loan insured through the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs or similar programs operated by cities or states. These programs usually require a smaller down payment. Ask lenders about these programs. You can get more information about these programs from the agencies that run them.

CLO's: Computer loan origination systems, are computer terminals sometimes available in real estate offices to help you sort through the various types of loans offered by different lenders. The CLO operator may charge a fee for the services the CLO offers. This fee may be paid by you or by the lender that you select.

Types of Loans: Loans can have a fixed interest rate or a variable interest rate. Fixed rate loans have the same principal and interest payments during the loan term. Variable rate loans can have any one of a number of indexes and margins which determine how and when the rate and payment amount change. If you apply for a variable rate loan, also known as an adjustable rate mortgage (ARM), a disclosure and booklet required by the Truth in Lending Act will further describe the ARM. Most loans can be repaid over a term of 30 years or less. Most loans have equal monthly payments. The amounts can change from time to time on an ARM depending on changes in the interest rate. Some loans have short terms and a large final payment called a balloon. You should shop for the type of home mortgage loan terms that best suit your needs.

Interest Rate, Points & Other Fees: Often the price of a home mortgage loan is stated in terms of an interest rate, points, and other fees. A point is a fee that equals 1 percent of the loan amount. Points are usually paid to the lender, mortgage broker, or both, at the settlement or upon the completion of the escrow. Often, you can pay fewer points in exchange for a higher interest rate or more points for a lower rate. Ask your lender or mortgage broker about points and other fees.

A document called the Truth in Lending Disclosure Statement will show you the Annual Percentage Rate (APR) and other payment information for the loan you have applied for. The APR takes into account not only the interest rate, but also the points, mortgage broker fees and certain other fees that you have to pay. Ask for the APR before you apply to help you shop for the loan that is best for you. Also ask if your loan will have a charge or a fee for paying all or part of the loan before payment is due (prepayment penalty). You may be able to negotiate the terms of the prepayment penalty.

Lender-Required Settlement Costs: Your lender may require you to obtain certain settlement services, such as a new survey, mortgage insurance or title insurance. It may also order and charge you for other settlement-related services, such as the appraisal or credit report. A lender may also charge other fees, such as fees for loan processing, document preparation, underwriting, flood certification or an application fee. You may wish to ask for an estimate of fees and settlement costs before choosing a lender. Some lenders offer no cost or no point loans but normally cover these fees or costs by charging a higher interest rate.

Comparing Loan Costs: Comparing APRs may be an effective way to shop for a loan. However, you must compare similar loan products for the same loan amount. For example, compare two 30-year fixed rate loans for \$100,000. Loan A with an APR of 8.35% is less costly than Loan B with an APR of 8.65% over the loan term. However, before you decide on a loan, you should consider the up-front cash you will be required to pay for each of the two loans as well.

Another effective shopping technique is to compare identical loans with different up-front points and other fees. For example, if you are offered two 30-year fixed rate loans for \$100,000 and at 8%, the monthly payments are the same, but the up-front costs are different:

Loan A - 2 points (\$2,000) and lender required costs of \$1800 = \$3800 in costs.

Loan B - 2 ¼ points (\$2250) and lender required costs of \$1200 = \$3450 in costs.

A comparison of the up-front costs shows Loan B requires \$350 less in up-front cash than Loan A. However, your individual situation (how long you plan to stay in your house) and your tax situation (points can usually be deducted for the tax year that you purchase a house) may affect your choice of loans.

Lock-ins: Locking in your rate or points at the time of application or during the processing of your loan will keep the rate and/or points from changing until settlement or closing of the escrow process. Ask your lender if there is a fee to lock-in the rate and whether the fee reduces the amount you have to pay for points. Find out how long the lock-in is good, what happens if it expires, and whether the lock-in fee is refundable if your application is rejected.

Tax and Insurance Payments: Your monthly mortgage payment will be used to repay the money you borrowed plus interest. Part of your monthly payment may be deposited into an escrow account (also known as a reserve or impound account) so your lender or service can pay your real estate taxes, property insurance, mortgage insurance and/or flood insurance. Ask your lender or mortgage broker if you will be required to set up an escrow or impound account for taxes and insurance payments.

Transfer of Your Loan: While you may start the loan process with a lender or mortgage broker, you could find that after settlement another company may be collecting the payments on your loan. Collecting loan payments is often known as servicing the loan. Your lender or broker will disclose whether it expects to service your loan or to transfer the servicing to someone else.

Mortgage Insurance: Private mortgage insurance and government mortgage insurance protect the lender against default and enable the lender to make a loan which the lender considers a higher risk. Lenders often require mortgage insurance for loans where the down payment is less than 20% of the sales price. You may be billed monthly, annually, by an initial lump sum, or some combination of these practices for your mortgage insurance premium. Ask your lender if mortgage insurance is required and how much it will cost. Mortgage insurance should not be confused with mortgage life, credit life or disability insurance, which are designed to pay off a mortgage in the event of the borrowers death or disability.

You may also be offered lender paid mortgage insurance (LPMI). Under LPMI plans, the lender purchases the mortgage insurance and pays the premiums to the insurer. The lender will increase your interest rate to pay for the premiums -- but LPMI may reduce your settlement costs. You cannot cancel LPMI or government mortgage insurance during the life of your loan. However, it may be possible to cancel private mortgage insurance at some point, such as when your loan balance is reduced to a certain amount. Before you commit to paying for mortgage insurance, find out the specific requirements for cancellation.

Flood Hazard Areas: Most lenders will not lend you money to buy a home in a flood hazard area unless you pay for flood insurance. Some government loan programs will not allow you to purchase a home that is located in a flood hazard area. Your lender may charge you a fee to check for flood hazards. You should be notified if flood insurance is required. If a change in flood insurance maps brings your home within a flood hazard area after your loan is made, your lender or service may require you to buy flood insurance at that time.

Selecting a Settlement Agent

Settlement practices vary from locality to locality, and even within the same county or city. Settlements may be conducted by lenders, title insurance companies, escrow companies, real estate brokers or attorneys for the buyer or seller. You may save money by shopping for the settlement agent.

In some parts of the country (particularly western states), settlement may be conducted by an escrow agent. The parties sign an escrow agreement which requires them to provide certain documents and funds to the agent. Unlike other types of settlement, the parties do not meet around a table to sign documents. Ask how your settlement will be handled.

Securing Title Services: Title insurance is usually required by the lender to protect the lender against loss resulting from claims by others against your new home. In some states, attorneys offer title insurance as part of their services in examining title and providing a title opinion. The attorney's fee may include the title insurance premium. In other states, a title insurance company or title agent directly provides the title insurance.

Owner's Policy. A lenders title insurance policy does not protect you. Similarly, the prior owner's policy does not protect you. If you want to protect yourself from claims by others against your new home, you will need an owner's policy. When a claim does occur, it can be financially devastating to an owner who is uninsured. If you buy an owner's policy, it is usually much less expensive if you buy it at the same time and with the same insurer as the lender's policy.

Choice of Title Insurer: Under RESPA, the seller may not require you, as a condition of the sale, to purchase title insurance from any particular title company. Generally, your lender will require title insurance from a company that is acceptable to it. In most cases you can shop for a company that meets the lenders standards.

Review Initial Title Report: In many areas, a few days or weeks before the settlement or closing of the escrow, the title insurance company will issue a Commitment to Insure or preliminary report or binder containing a summary of any defects in title which have been identified by the title search, as well as any exceptions from the title insurance policies coverage. The commitment is usually sent to the lender for use until the title insurance policy is issued at or after the settlement. You can arrange to have a copy sent to you (or to your attorney) so that you can object if there are matters affecting the title which you did not agree to accept when you signed the agreement of sale.

Coverage & Cost Savings: To save money on title insurance, compare rates among various title insurance companies. Ask what services and limitations on coverage are provided under each policy so that you can decide whether coverage purchased at a higher rate may be better for your needs. However, in many states, title insurance premium rates are established by the state and may not be negotiable. If you are buying a home which has changed hands within the last several years, ask your title company about a "reissue rate," which would be cheaper. If you are buying a newly constructed home, make certain your title insurance covers claims by contractors. These claims are known as mechanics liens in some parts of the country. Survey, Lenders or title insurance companies often require a survey to mark the boundaries of the property. A survey is a drawing of the property showing the perimeter boundaries and marking the location of the house and other improvements. You may be able to avoid the cost of a complete survey if you can locate the person who previously surveyed the property and request an update. Check with your lender or title insurance company on whether an updated survey is acceptable.

RESPA Disclosures: One of the purposes of RESPA is to help consumers become better shoppers for settlement services. RESPA requires that borrowers receive disclosures at various times. Some disclosures spell out the costs associated with the settlement, outline lender servicing and escrow account practices and describe business relationships between settlement service providers.

Good Faith Estimate of Settlement Costs: RESPA requires that, when you apply for a loan, the lender or mortgage broker give you a Good Faith Estimate of settlement service charges you will likely have to pay. If you do not get this Good Faith Estimate when you apply, the lender or mortgage broker must mail or deliver it to you within the next three business days.

Be aware that the amounts listed on the Good Faith Estimate are only estimates. Actual costs may vary. Changing market conditions can affect prices. Remember that the lender's estimate is not a guarantee. Keep your Good Faith Estimate to compare it with the final settlement costs and ask lender about any changes.

Servicing Disclosure Statement: RESPA requires the lender or mortgage broker to tell you in writing, when you apply for a loan or within the next three business days, whether it expects that someone else will be servicing your loan (collecting your payments).

Affiliated Business Arrangements: Sometimes, several businesses that offer settlement services are owned or controlled by a common corporate parent. These businesses are known as affiliates. When a lender, real estate broker, or other participant in your settlement refers you to an affiliate for a settlement service (such as when a real estate broker refers you to a mortgage broker affiliate), RESPA requires the referring party to give you an Affiliated Business Arrangement Disclosure. This form will remind you that you are generally not required, with certain exceptions, to use the affiliate and are free to shop for other providers.

HUD-1 Settlement Statement: One business day before the settlement, you have the right to inspect the HUD-1 Settlement Statement. This statement itemizes the services provided to you and the fees charged to you. This form is filled out by the settlement agent who will conduct the settlement. Be sure you have the name, address, and telephone number of the settlement agent if you wish to inspect this form. The fully completed HUD-1 Settlement Statement generally must be delivered or mailed to you at or before the settlement. In cases where there is no settlement meeting, the escrow agent will mail you the HUD-1 after settlement, and you have no right to inspect it one day before settlement.

Escrow Account Operation & Disclosures: Your lender may require you to establish an escrow or impound account to insure that your taxes and insurance premiums are paid on time. If so, you will probably have to pay an initial amount at the settlement to start the account and an additional amount with each month's regular payment. Your escrow account payments may include a cushion or an extra amount to ensure that the lender has enough money to make the payments when due. RESPA limits the amount of the cushion to a maximum of two months of escrow payments.

At the settlement or within the next 45 days, the person servicing your loan must give you an initial escrow account statement. That form will show all of the payments which are expected to be deposited into the escrow account and all of the disbursements which are expected to be made from the escrow account during the year ahead. Your lender or service will review the escrow account annually and send you a disclosure each year which shows the prior years activity and any adjustments necessary in the escrow payments that you will make in the forthcoming year.

Processing Your Loan Application: Here are several federal laws which provide you with protection during the processing of your loan. The Equal Credit Opportunity Act (ECOA), the Fair Housing Act, and the Fair Credit Reporting Act (FCRA) prohibit discrimination and provide you with the right to certain credit information.

No Discrimination: ECOA prohibits lenders from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age, the fact that all or part of the applicant's income comes from any public assistance program, or the fact that the applicant has exercised any right under any federal consumer credit protection law. To help government agencies monitor ECOA compliance, your lender or mortgage broker must request certain information regarding your race, sex, marital status and age when taking your loan application.

The Fair Housing Act also prohibits discrimination in residential real estate transactions on the basis of race, color, religion, sex, handicap, familial status or national origin. This prohibition applies to both the sale of a home to you and the decision by a lender to give you a loan to help pay for that home. Finally, your locality or state may also have a law which prohibits discrimination.

Frequently, there are differences in the types and amounts of settlement costs charged to the borrower -- for example, some borrowers are charged greater fees for mortgages depending on their credit worthiness. These differences may be justified or they may be unlawfully discriminatory. It is important that you examine your settlement documents closely and do not hesitate to compare your settlement costs with those of your friends and neighbors.

If you feel you have been discriminated against by a lender or anyone else in the home buying process, you may file a private legal action against that person or complain to a state, local or federal administrative agency. You may want to talk to an attorney or you may want to ask the federal agency that enforces ECOA (the Board of Governors of the Federal Reserve System) or the Fair Housing Act (HUD) about your rights under these laws.

Prompt Action/Notification of Action Taken: Your lender or mortgage broker must act on your application and inform you of the action taken no later than 30 days after it receives your completed application. Your application will not be considered complete, and the 30 day period will not begin, until you provide to your lender or mortgage broker all of the material and information requested.

Statement of Reasons for Denial: If your application is denied, ECOA requires your lender or mortgage broker to give you a statement of the specific reasons why it denied your application or tell you how you can obtain such a statement. The notice will also tell you which federal agency to contact if you think the lender or mortgage broker has illegally discriminated against you.

Obtaining Your Credit Report: The Fair Credit Reporting Act (FCRA) requires a lender or mortgage broker that denies your loan application to tell you whether it based its decision on information contained in your credit report. If that information was a reason for the denial, the notice will tell you where you can get a free copy of the credit report. You have the right to dispute the accuracy or completeness of any information in your credit report. If you dispute any information, the credit reporting agency that prepared the report must investigate free of charge and notify you of the results of the investigation.

Obtaining Your Appraisal: The lender needs to know if the value of your home is enough to secure the loan. To get this information, the lender typically hires an appraiser, who gives a professional opinion about the value of your home. ECOA requires your lender or mortgage broker to tell you that you have a right to get a copy of the appraisal report. The notice will also tell you how and when you can ask for a copy.

RESPA Protection Against Illegal Referral Fees: RESPA was enacted because Congress felt that consumers needed protection from "... unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country." Some of the practices Congress was concerned about are discussed below. Most professionals in the settlement business provide good service and do not engage in these practices.

Prohibited Fees: It is illegal under RESPA for anyone to pay or receive a fee, kickback or anything of value because they agree to refer settlement service business to a particular person or organization. For example, your mortgage lender may not pay your real estate broker \$250 for referring you to the lender. It is also illegal for anyone to accept a fee or part of a fee for services if that person has not actually performed settlement services for the fee. For example, a lender may not add to a third party fee, such as an appraisal fee, and keep the difference.

Permitted Payments: RESPA does not prevent title companies, mortgage brokers, appraisers, attorneys, settlement/closing agents and others, who actually perform a service in connection with the mortgage loan or the settlement, from being paid for the reasonable value of their work. If a participant in your settlement appears to be taking a fee without having done any work, you should advise that person or company of the RESPA referral fee prohibitions. You may also speak with your attorney or complain to a regulator.

Penalties: It is a crime for someone to pay or receive an illegal referral fee. The penalty can be a fine, imprisonment or both. You may be entitled to recover three times the amount of the charge for any settlement service by bringing a private lawsuit. If you are successful, the court may also award you court costs and your attorney's fees.

Private Lawsuits: If you have a problem, the best place to have it fixed is at its source (the lender, settlement agent, broker, etc.). If that approach fails and you think you have suffered because of a violation of RESPA, ECOA or any other law, you may be entitled to sue in a federal or state court. This is a matter you should discuss with your attorney.

Government Agencies: Most settlement service providers are supervised by a governmental agency at the local, state and/or federal level, some of which are listed in the Appendix to this Booklet. Your state's Attorney General may have a consumer affairs division. If you feel that a provider of settlement services has violated RESPA or any other law, you can complain to that agency or association. You may also send a copy of your complaint to the HUD Office of Consumer & Regulatory Affairs.

Servicing Errors: If you have a question any time during the life of your loan, RESPA requires the company collecting your loan payments (your servicer) to respond to you. Write to your servicer and call it a qualified written request under Section 6 of RESPA. A qualified written request should be a separate letter and not mailed with the payment coupon. Describe the problem and include your name and account number. The servicer must investigate and make appropriate corrections within 60 business days.

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