

## Closing Costs and Prepays

Buyer fees are paid to various service providers in the transaction. Some are collected at the time of mortgage application, such as the application fee or the credit report. Most are collected at closing. Buyer funds are allocated to the down payment, closing costs, and prepaid items. Sometimes your closing costs and prepaids are paid by the seller when negotiated in the contract.

Closing costs are fees for services necessary to the transaction. Fees which cover the appraisal, survey, tax certificates, escrow fees, loan application, underwriter, courier, title insurance, and attorney are examples of closing costs.

Prepays are fees paid by either you or on your behalf are collected for payment of a bill due in the future. Many prepaid items are put into an escrow account where they accumulate until the actual bill is due. Examples of prepaid items are taxes, insurance, private mortgage insurance, prepaid interest, etc.

Lenders are required to disclose charges involved in the financing of the home. The Truth in Lending Act requires the lender to disclose credit terms clearly, conspicuously, meaningfully, and in writing. The lender discloses terms by providing a Good Faith Estimate.

The Good Faith Estimate is only an estimate. The actual charges will be affected by information not known by the lender at the time of the mortgage application. These charges will be affected by the date of closing, the specific vendors providing services, the municipality where the property resides, and the underwriter providing funds to you.

At closing, you will sign a HUD-1 Settlement Statement which lists the disbursement of all funds associated with the purchase. To learn more about closing costs, prepaids, and the HUD-1, go to <http://www.hud.gov/offices/hsg/sfh/res/sfhrestc.cfm>.

## Escrow Accounts and Prepaid Items

Many lenders will set up an optional escrow account for you at closing. This is an account used at a later date to pay for items for which you are responsible. When you make your monthly payment, you pay principal, interest, taxes, homeowner insurance, and private mortgage insurance, (PITI) if applicable.

An escrow account provides you a way to set aside monthly funds that will be due later in the year. Property taxes are due annually toward year end. Escrow accounts limit the lender's risk that you would not have enough funds when bills come due.

At closing, sellers will be charged with taxes from the first of the year until the day of closing. These funds are placed in your escrow account. You will also prepay several months of taxes. Then, on the first of every month when you make your payment, you will deposit a month's worth of taxes into your escrow account. Thus, when the tax bill is due, the sellers' tax contribution, your prepaid tax plus your monthly tax contribution will add up to 12 months worth of taxes. This should be enough to pay the tax bill.

Homeowner's insurance is also deposited in the same escrow account. At closing you pay the yearly premium. The next premium will be due on the one year anniversary. Thus, when you make your monthly payment, you are contributing one month's worth of property insurance. When the premium is due in a year, there will be enough funds in the escrow account to pay the bill. Mortgage insurance is handled in a similar manner.

If you sell your home, you will owe taxes and insurance through the day you close. Excess funds in the escrow account will be refunded to you.

## The HUD-1 Settlement Statement

When you close on the home you're buying, you will sign the HUD-1 Settlement Statement. This two-page form lists the closing costs for all of the items paid by you and the seller.

Each page has a seller's column and a buyer's column. The first page is a summary of the transaction. It takes items charged to you and subtracts items which are credits. The result will be the cash you should bring to closing in the form of a cashier's check. The last line of page two (Item 1400) lists the total settlement charges for you and the seller.

The seller's summary takes the items that the seller should be receiving and subtracts the charges. The difference is the amount of money that the seller will net at closing.

## The Right Offer Price

As a buyer, your goals are very different from the sellers during negotiations. You want to pay as little as possible while sellers want to sell for the highest possible price. Buyer advantage comes with market knowledge.

You may have seen enough to decide your offer price. However, it's wise to ask your sales professional to provide you with sold property data. By examining recent sales of similar properties you can reduce the risk of overbuying.

Know how the market has behaved recently to focus your offer price. You can assess the likelihood the seller will take less by looking at the number of competing properties and days on market. If comparable homes are selling quickly, your selection might not last long. This would prompt an offer price closer to list.

Understand your market. In a buyer's market with plenty of inventory, a lower offer will have a better chance. In a seller's market, where inventory is scarce, a low offer price makes you vulnerable to a competing offer. In general, a seller will take less in a buyer's market and budge little in a seller's market.

If you are competing with another buyer(s) for the same house, consider making an offer greater than list price. Your sales professional can advise you how to view the market and hone in on a prudent offer price. Consider how long you have searched, how motivated you are, and if you have a back-up property.

Always remember that time is of the essence. Long negotiations increase the likelihood that another buyer could make an offer on the same property or that the sellers might change their minds.