



HOME BUYING Closing Costs

Closing Costs

Closing costs are fees paid to complete the mortgage loan. They usually total approximately 2% to 5% of the loan amount and may be paid by the buyer or seller. Some closing costs are one-time fees paid at closing, while others are prepaid recurring expenses.

Sometimes your portion of closing costs can be included as part of your home loan. The lender is required to provide you, no later than three days before closing, a Closing Disclosure. This document details the closing costs and terms of the mortgage.

Examples of closing costs paid at closing include:

- › **Appraisal:** An estimate of current value of a home.
- › **Attorney's or title company's fee:** The buyer usually pays the fees.
- › **Credit report:** Furnishes lenders with information about the buyer's current indebtedness and payment history.
- › **Escrow company:** Acts as a third party to both buyer and seller, handles the paperwork, and collects and distributes the various financial transactions, such as prepaids, real estate commissions, and down payments.
- › **Home inspection:** An independent, professional inspection of the property and its electrical, plumbing, heating and cooling, and kitchen systems.
- › **Home warranty programs:** Offers first-year protection from a breakdown of many household systems, including plumbing, water heater, disposal, heating and cooling, and appliances.
- › **Loan origination fee:** A fee charged by the lender for making the loan; varies from 0% to 2%.
- › **Pest inspection:** Separate from the home inspection; mortgage companies, particularly

for VA loans, require a pest and water damage inspection.

- › **Recording fee:** The cost to record your deed and your mortgage with the city or county in which the home is located.
- › **Survey:** The measurement of the property by licensed engineers or surveyors to determine its area and attest to its boundaries.
- › **Title search and insurance:** Researches the records and ensures that the property's title is free from any encumbrances and that the property will transfer with a clear title. The insurance protects the mortgage company (required) and the buyer (optional) against any claims on the property not found during the title search.

Many of these closing costs can be negotiated for either the buyer or seller to cover as part of the mortgage negotiation. Work toward a contract in your favor.

Prepaid Costs

At closing, the buyer will pay a number of recurring costs up front, with the money placed in escrow with the mortgage company and drawn when needed. Various prepaid costs could include:

- › **Private mortgage insurance (PMI):** Protects the lender against default on the loan. This can be a lump-sum payment, a monthly payment added to the mortgage payment, or a higher interest rate.

Example: \$200,000 purchase price, 10% down (\$20,000), \$180,000 loan amount, monthly PMI = $0.0052 \times \text{loan amount} \div 12 \text{ months}$ = \$78/month added to mortgage payment. PMI can be avoided by putting 20% down on the home purchase.

- › **Mortgage insurance premium (MIP):** FHA requires a mortgage insurance premium for its home-buying programs. An up front premium of 1.75% of the loan amount is paid at closing and can be financed into the mortgage amount. In addition, there is an annual premium, which varies based on the length of the loan, the amount borrowed, and the initial loan-to-value (LTV) ratio. Condominiums do not require upfront MIP, only a monthly MIP.
- › **VA funding fee:** For the VA to guarantee the home loan, there is a closing cost assessed by the VA to originate the loan. This is called a funding fee. This fee will vary, depending upon the type of VA loan, the down payment, whether this is your first time to use your entitlement, whether you are a disabled veteran, and whether you served active duty or in the National Guard or Reserve.
- › **Homeowners insurance:** A total of 14 months' premium payments are collected, 12 of which are used to pay the first year's policy premium. The extra two months are collected and placed in escrow account from which future premium payments are made.
- › **Property taxes:** Prorated buyer's first month's share of taxes and additional months of payments are placed in escrow from which future tax payments are made.
- › **Interest:** The buyer pays a prorated share of the first month's interest due on the loan amount, depending on the closing date.

Useful Website

- › Consumer Financial Protection Bureau (CFPB):
<https://www.consumerfinance.gov/owning-a-home/process/close/>

