



## HOME BUYING

# Mortgage Loan Types

### **Fixed rate loans:**

These are the most popular loans because they offer stable, consistent payments throughout the life of the loan. The most common is the 30-year fixed rate.

### **Adjustable rate loans:**

These loans have a variable interest rate that fluctuates according to the financial index they are tied to and the type of adjustable-rate mortgage (ARM) obtained. The interest rate is usually capped over the life of the loan and it can rise only one or two points a year, depending on the loan type.

### **FHA loans:**

Government-backed Federal Housing Administration (FHA) loans are designed for first-time or lower-income home buyers. The interest rate is usually less than the rate for a conventional loan. FHA loans are available as fixed-rate and adjustable-rate mortgages. The minimum down payment is 3.5% of the loan amount. There are limits to the maximum loan amount.

### **VA loans:**

These loans are available to veterans of the U.S. Armed Forces and backed by the Department of Veterans Affairs. Typically, no down payment is required. The VA limits certain closing costs that a veteran can pay. There is a one-time VA funding fee that can be included in the loan.

### **Assumptions:**

Consider assuming the seller's existing loan and interest rate if the rate on the assumable loan is lower than the prevailing rate for a new loan. By assuming a loan, you take responsibility for paying the mortgage owed by the seller.

### **Buydown:**

If you cannot afford the prevailing interest rate, consider a buydown mortgage. The buyer can pay extra points to buy down the mortgage for the first few years. Buydowns are common among new construction homes and first-time home buyers.

### **Balloon loans:**

With this loan, interest paid during the term of the loan does not fully pay off the mortgage. At the end of the loan term, the homeowner must pay the remaining principal in one lump sum. Balloon loans usually have lower interest rates than fixed-rate loans. Balloon loans are most useful to home buyers who stay in the home no longer than the term of the loan. A balloon loan is typically not a good choice for a first-time home buyer.

### **Seller financing:**

With this type of loan, the seller takes on the role of lender. Instead of giving cash to the buyer, the seller extends enough credit to the buyer for the purchase price of the home, minus any down payment. The buyer and seller sign a promissory note (which contains the terms of the loan). This is often a short-term loan and a balloon payment is due at end of the loan term. The advantage for buyers is they get the prevailing interest rate or a better rate without paying points or fees.



### **State veterans program:**

Many states offer veterans benefits. These benefits may include home loans, veteran's homes, educational grants and scholarships, special exemptions or discounts on fees and taxes, free hunting and fishing privileges, and more. Each state manages its own benefit programs. Be sure to take advantage of the benefits you have earned by linking to your state department of veterans affairs.

### **Beware of:**

#### **Interest-only mortgage:**

An interest-only mortgage allows you to pay only the interest for a specified number of years. Since there is no payment on the loan principal, a borrower who takes this type of loan is depending on the housing market to increase the value of the home. Most interest-only mortgages have adjustable interest rates, which means the interest rate and monthly payment will change over the term of the loan. The interest-only mortgage payment period is typically between three and 10 years. After that, your monthly payment will increase even if interest rates stay the same, because you must pay back the principal as well as the interest.

#### **80/20 mortgages:**

An 80/20 mortgage is essentially two mortgage loans that equal the total amount of the purchase price, with the first mortgage being 80% and the second mortgage covering the remaining 20%. The first is typically at the going rate for a conventional mortgage, while the second is usually significantly higher.

#### **Subprime lending:**

Subprime lending, also called "B-Paper," "near-prime" or "second chance" lending, is a general term that refers to the practice of making loans to borrowers who do not qualify for market interest rates because of problems with their credit history. Because subprime borrowers are considered at higher risk to default, subprime loans typically have less favorable terms than their traditional counterparts. These terms may include higher interest rates, regular fees, or an upfront charge.

### **You can learn more about mortgages at:**

- › Consumer Financial Protection Bureau (CFP):  
<https://www.consumerfinance.gov/consumer-tools/mortgages/>
- › Military Consumer:  
<https://www.militaryconsumer.gov/spend/your-home/buying-home-%E2%80%93-active-duty>

