Section 7.3

Buying and Selling a Home

The Home-Buying Process

How do you buy a home?

Many people dream of owning a home. Buying a home, however, is a huge financial commitment. It will probably be the most costly purchase you will ever make. There are a number of steps that you will need to take to purchase a home. You will need to determine your home ownership needs, find and evaluate a property to purchase, price the property, obtain financing, and close the transaction.

STEP 1: Determine Your Home Ownership Needs

What are some of the benefits and drawbacks of owning a home?

To make an informed decision about whether to buy a home, you will need to consider the benefits and drawbacks of ownership. You will also need to consider the types of homes that are available and how much you can afford to spend.

Owning Your Residence: Benefits

While renters may be attracted to the idea of mobility, homeowners may enjoy a sense of stability and permanence. Home ownership also allows individual expression. You have more freedom to decorate and change your own home and to have pets. Many people find this type of flexibility very appealing.

As a homeowner, you will also gain financial benefits. You can deduct the interest charges on your loan payments from your federal income taxes each year. Your property taxes are also deductible. Moreover, the value of many homes rises steadily. Therefore, homeowners can usually sell their homes for a profit, depending on their **equity**, which is the value of the home less the amount still owed on the money borrowed to purchase it. In addition, once the borrowed money is paid off, homeowners have no further payments to make other than property taxes, homeowners insurance, and maintenance costs.

Focus on Reading

Read to Learn

- How to identify the advantages and disadvantages of owning a residence.
- How to explain how to evaluate a property.
- How to discuss the financing involved in purchasing a home.
- How to describe a plan for selling a home.

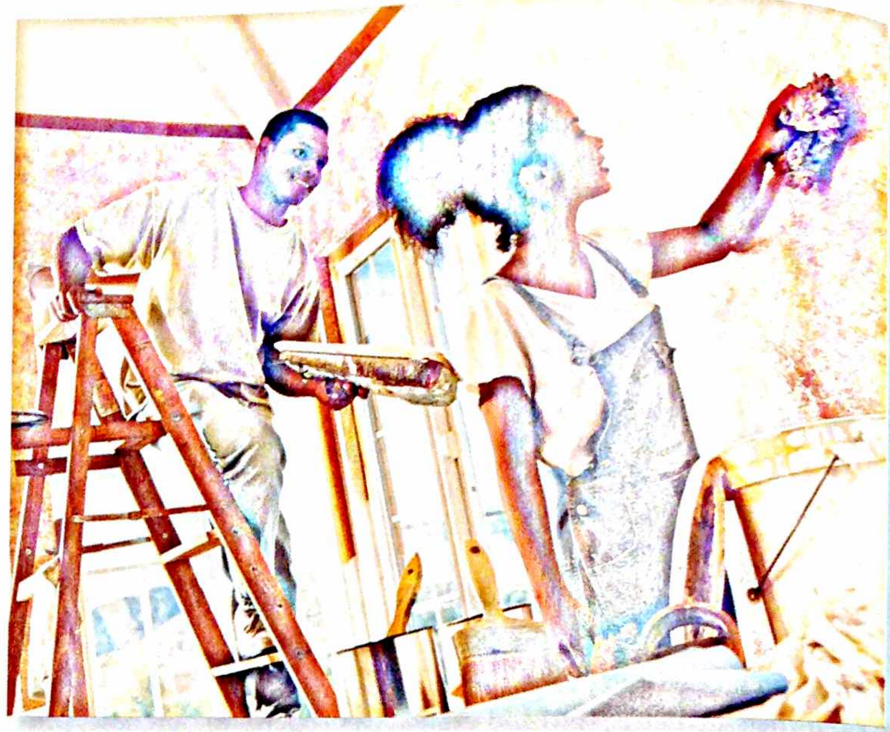
Main Idea

Understanding the processes involved with homeownership is necessary when you buy or sell a home.

Key Terms

- equity
- escrow account
- private mortgage insurance (PMI)
- mortgage
- points
- amortization
- fixed-rate mortgage
- adjustable-rate mortgage (ARM)
- home equity loan
- refinance
- closing
- title insurance
- deed
- appraisal

▶ **FREEDOM OF EXPRESSION** For many people, one of the most appealing advantages of home ownership is the ability to decorate or remodel freely. *Can you think of any situations in which homeowners are not completely free to change the look of their homes?*



Before You Read

PREDICT

If you plan to own a house one day, how do you think you begin the process?

Owning Your Residence: Drawbacks

Of course, buying a home does not guarantee happiness. Home ownership can involve financial risk. Saving money for a down payment to buy a home is very difficult for many people. Moreover, the tax deductions may not make up for high loan payments. Property values do not always go up; in some cases, they may even decline.

A second drawback is limited mobility. A homeowner who wants to move must either sell his or her property or arrange to rent it to tenants. These processes can be slow and may result in financial loss.

Owning a home can involve high expenses. Homeowners must pay for all maintenance and repairs, such as fixing a leaky roof, cleaning out a flooded basement, putting up new wallpaper, and replacing or repairing broken appliances. The cost of taking good care of a home can be quite high, even if homeowners do most of the work themselves.

Types of Housing

Homes come in all shapes and sizes, providing housing alternatives for a range of budgets and lifestyles.

Single-Family Dwellings The most popular type of housing in the United States is the single-family house. A single-family house usually stands on a separate lot with a lawn and some outdoor living space. The home is not attached to any other buildings. Because a single-family dwelling provides the most privacy of any type of housing, it is often the most expensive.

Multiunit Dwellings This category of housing includes duplexes and townhouses. A duplex is a single building divided into living spaces for two families—or two units. A building divided into three units is a triplex. A townhouse is one of many single-family units attached to other units. For these types of housing, each unit has its own outside entrance.

Condominiums A condominium is one of a group of apartments or townhouses that people own instead of rent. Condominium owners pay a monthly fee to cover the cost of maintenance, repairs, improvements, and insurance for the building and its common spaces. The unit owners form a condominium association, which manages the housing complex. Common spaces, such as hallways, lawns, elevators, and recreational areas, belong to the association, not to individual owners.

Cooperative Housing Cooperative housing is another apartment-style living arrangement in which a building that contains a number of units is owned by a nonprofit organization. Members of the organization do not actually own the property. Members pay a monthly fee which covers their rent and the operating expenses of the organization.

Prefabricated Homes Prefabricated houses are manufactured and partially assembled at a factory. The pieces are then transported to a building site and put together there. Prefabricated homes are often cheaper than other single-family houses because the mass production of their pieces and partial assembly at the factory help keep costs down.

◀ **OPTIONS TO BUY**
Attractively designed prefabricated homes are a less costly alternative for housing. *Who might be interested in purchasing these homes? Why?*

$avvy Saver

Furnishing Your First Apartment

1. Buy large items such as sofas and tables at thrift shops.
2. Shop for items such as kitchenware at discount stores.
3. Browse garage or moving sales to find great buys.
4. Ask friends and relatives if they want to get rid of household items they do not use.
5. Be creative: Make curtains from colorful sheets.

Mobile Homes Another type of manufactured home is known as a *mobile home.* Most mobile homes are not truly mobile because they are rarely moved from their original sites. Mobile homes are fully assembled in factories. They contain many of the features of larger houses, such as fully equipped kitchens, bathrooms, and even fireplaces. Some mobile-home owners purchase the land on which their houses are located. Spaces can also be rented in mobile-home parks where access to community recreation facilities is often included.

Compared with other housing choices, mobile homes are relatively inexpensive. However, they are not as well constructed or as safe as many other types of housing, and they usually do not increase in value at the same rate as single-family houses do.

Affordability and Your Needs

Selecting a type of dwelling is only one part of determining your home ownership needs. You will also need to consider the price of a home, its size, and its quality.

Price and Down Payment To determine how much you can afford to spend on a home, you will need to examine your income, your savings, and your current living expenses. Can you afford to make a large down payment when you buy a home? A down payment is a portion of the total cost of an item that is required at the time of purchase. You will need to make monthly payments on a loan, pay property taxes, and buy homeowners insurance. The exact amounts will depend on interest rates and local economic conditions. Is your income enough to cover these costs as well as other current expenses?

Before you look for the home of your dreams, it is smart to know exactly what you can afford to pay. To determine how much you can afford to spend on a home and if you will be approved for a loan, talk to a loan officer at a mortgage company or other financial institution. Many companies and banks will prequalify loan applicants so that prospective home buyers will know in advance if they can get a mortgage loan. This service is usually provided without charge.

Size and Quality Ideally, the home you buy will be big enough for your needs and will be in good condition. If you are a first-time buyer, though, you may not be able to get everything you want.

Trading Up Most financial experts recommend buying what you can afford, even if you have to sacrifice the size and features you would love to have. As you advance in your career and your income increases, you may be able to "trade up" and purchase a home with some extra comforts. For example, eight years ago, Kanya bought a condominium that had only a tiny garden and one small bathroom. Last week she sold it, made a profit, and moved into a larger house, where she will be able to plant a vegetable and flower garden and enjoy the convenience of two full baths.

STEP 2: Find and Evaluate a Property to Purchase

Why is the location of your home important?

When you know what type of residence you would prefer and what you can afford, you will be able to start searching for a property to purchase.

Selecting a Location

The location of your home is very important. Ask yourself if you would rather live in a city, in the suburbs, or in a small-town or country setting. Perhaps you want a neighborhood with parks and trails that accommodate cyclists and runners. If you commute to work by bus, you will have to make sure that your house is close to the bus lines. The distance between home and work, the quality of the local school system, your interests and lifestyle, and other factors all help determine where you will want to live.

Careers in Finance

REAL ESTATE AGENT **Carlos Garza**

RealTime Real Estate, Inc.

Carlos has always had a knack for putting people at ease. This ability has proven very useful in his job as a real estate sales agent. Carlos is also very good at handling the complicated procedures involved in selling real estate. He sees his job as being a matchmaker between buyers and sellers.He works well with both sides, advising sellers on how to make homes more appealing to potential buyers and advising buyers on the suitability and value of the homes they visit. As a real estate agent, he relishes the challenge of making his clients happy and the satisfaction of closing a deal.

SKILLS: Sales, marketing, administration, time-management, communication, negotiation, math, and legal skills

PERSONAL TRAITS: Personable, highly disciplined, persistent, trustworthy, and self-starting

EDUCATION: High school diploma or equivalent; training through a real estate company or organization; and state license

ANALYZE If you were looking for a home to buy, what qualities, in addition to trustworthiness, would you look for in a real estate agent?

To learn more about career paths for real estate agents, visit **persfinance07.glencoe.com**.

Local Zoning Laws Some communities have strict zoning laws, which are regulations that limit how property in a given area can be used. The existence of such laws may also affect your housing decisions. William wanted to live in an all-residential area, so he bought a duplex in a neighborhood where local zoning laws ban any commercial construction of stores or business buildings. In contrast, Alicia bought a condominium in a much less restrictive community because she wanted to be able to walk to nearby restaurants and businesses.

Hiring a Real Estate Agent

Real estate agents are people who arrange the sale and purchase of homes as well as other buildings and land. They are good sources of information about the location, availability, prices, and quality of homes. Potential home buyers often use real estate agents to help them find housing. The agents can also negotiate the purchase price between buyer and seller. They help buyers arrange financing for the purchase, and they can recommend lawyers, insurance agents, and home inspectors to serve the buyers' needs.

Real estate services are usually free to the buyer. The agents may represent the sellers, who pay them a commission of 3 to 6 percent when the property is sold. Some real estate agents also represent buyers. In this case, the agent may be paid by either the buyer or the seller.

As You Read

RELATE

How would you go about finding a real estate agent who suits you?

Conducting a Home Inspection

Before you make a final decision to buy property, it is important to get an evaluation of the house and land by a qualified home inspector. (See **Figure 7.6** on page 216.) When Josh Samuels called in a home inspector to check the house he wanted to buy, the inspector found cracks in the foundation, an overloaded electrical system, and problems with the water quality. Josh still wanted the house, and he was able to negotiate a lower price because he had the inspector's report. A home inspection costs money, but it can save you from problems and unplanned expenses in the future.

Some states, cities, and lenders require inspection documents. The mortgage company will usually conduct an appraisal to determine the fair market value of the property. An appraisal is not a detailed inspection. It is an estimation of the value of the property usually in comparison with other similar properties that have recently sold in the particular area.

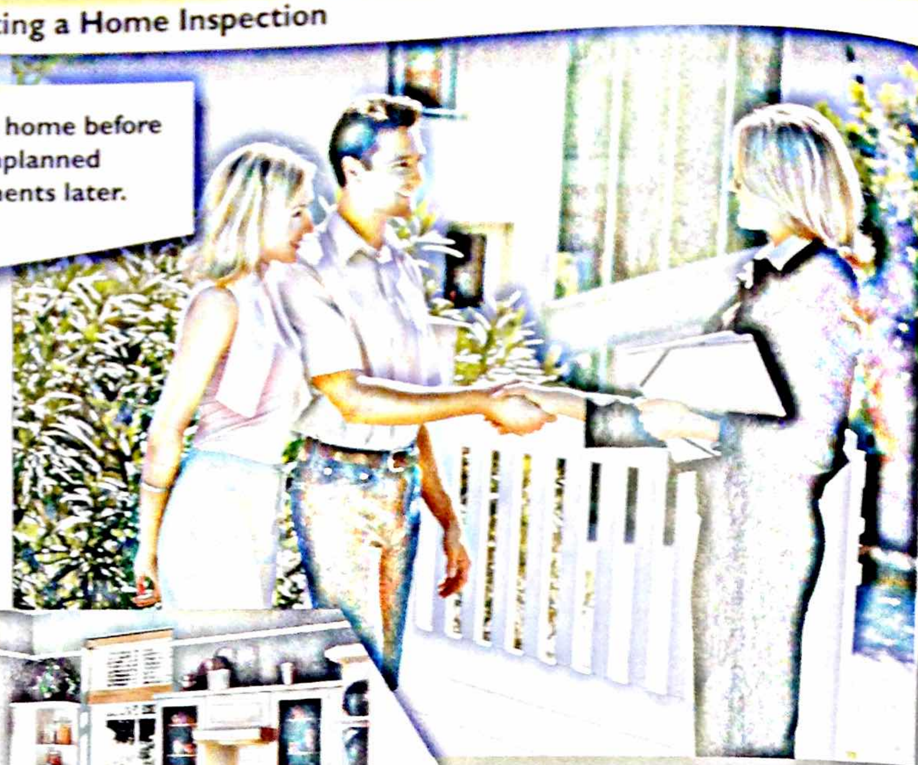
STEP 3: Price the Property

What price should you offer to pay?

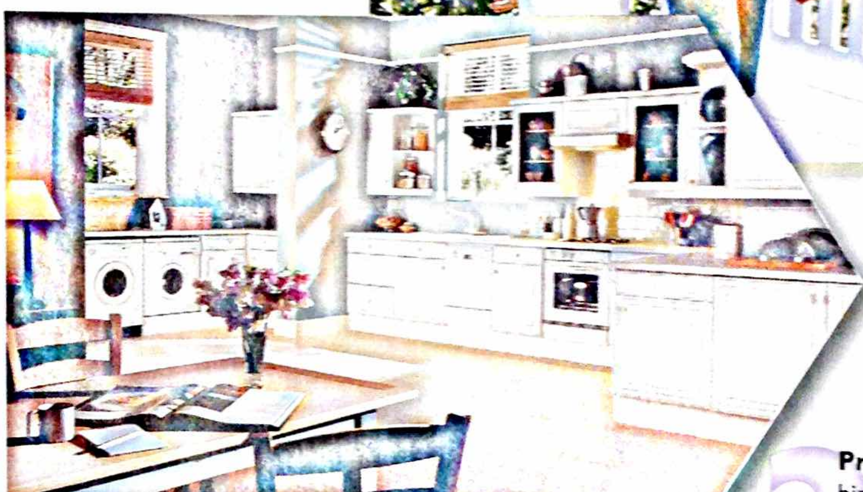
After you have checked out the property as thoroughly as possible, it is time to consider making an offer to the current owner. This is usually done through a real estate agent, unless the owner is acting as his or her own agent.

Figure 7.6 Conducting a Home Inspection

Taking steps to evaluate a home before you buy it may save you unplanned expenses and disappointments later.



1 **The Exterior** The buyer does a "walk-through" of the neighborhood to check the condition of streets and sidewalks. It is also important to check the exterior features of the home.



2 **The Interior** The buyer looks at the interior design of the home to be sure that it will meet his or her needs.

3 **Professional Home Inspection** The buyer hires a home inspector who checks the exterior: windows, foundation, chimney, and roof. The home inspector will also look at the interior construction: wiring, plumbing, heating system, walls, and floors.

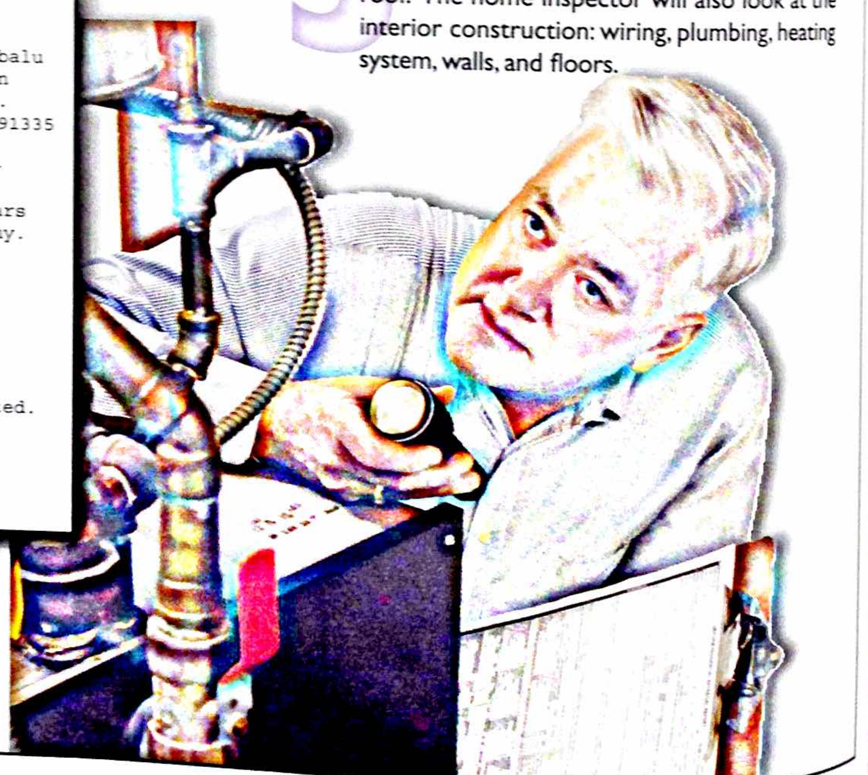
Apple Pie Home Inspection Service
21044 Manitowoc Avenue
Woodland Hills, CA 91364

Inspection No: 099422909
Inspection Date: 09/29/--
Inspector: Michelle Cabalu
Client: Peggie Thompson
Address: 6301 Glade Rd. Carlsbad, CA 91335

The house is a single-family dwelling, one-story structure built on a flat lot. Estimated age is approximately 35 to 40 years old. Weather at time of inspection was sunny.

100 EXTERIOR

101 Driveway: Concrete with cracks noted.
102 Walks: Concrete and brick with cracks noted. Missing bricks noted.
103 Fence/Gates: Wood and chain links. Detached wood fence noted.
104 Siding: Stucco and wood with cracks noted.
105 Trim: Wood.
106 Window Frames: Metal and wood.
107 Elec. Fixtures: S
108 Gutters/Downspouts: S



4 **Inspection Report** The buyer reviews the home inspector's report to decide whether this is the right home to buy.

Determining the Price of the Home

Every home that is for sale has a listing price—the price that the owner is asking for it. That price is not necessarily the price you will pay, however. You are free to make a lower offer. What should you offer? Here are some questions to consider:

- How long has the home been on the market? If a home is on the market for a while, the owner may accept a lower price.
- What have similar homes in the neighborhood sold for recently? If a listing price is too high, you should offer less.
- How tight is the housing market? In a "seller's market," homes are in high demand, and sellers can get the highest prices. In a "buyer's market," there is an abundant supply of homes for sale, and buyers can pay lower prices.
- Do the current owners need to sell in a hurry? If so, they may be willing to accept less than they feel the home is worth.
- How well does the home meet your needs? If a home fits your needs, you may be willing to pay more.
- How easily can you arrange financing? If interest rates are high, your payment will be higher.

Negotiating the Purchase Price

Once you have decided on a reasonable amount to offer, the real estate agent will communicate it to the seller, who may either accept or reject it. If your offer is accepted, congratulations! You will soon have a new home—and at a price you are willing to pay.

Sometimes the seller will not accept your offer if it is below the listing price. In that case, you will have to make a second, higher offer, or start looking for a different home. A seller may also make a counteroffer in response to your bid. Making a counteroffer means dropping the asking price. For example, Jian Wang offered $178,900 for a condominium that was listed at $186,000. The sellers rejected his offer but made a counteroffer of $184,500. Jian thought that the price was still too high, so he submitted a bid of $182,000. They eventually settled on a purchase price of $183,000.

When the buyer and seller agree on a price, they must sign a purchase agreement, or purchase contract, that states their intention to complete the sale. Most purchase contracts are conditional; that is, they take effect only if certain other events occur. For example, the contract may be valid only if the buyers can obtain financing, or only if they can sell their current home in a specified period of time.

At this point in the process, the buyer sometimes must pay the seller a portion of the purchase price, called *earnest money*. This money shows that the offer is serious. It is held in an escrow account until the sale is completed. An **escrow account** is an account where money is held in trust until it can be delivered to a designated party. The earnest money is applied toward the down payment.

Academic Connection
MATH

An average homeowner stays in a home for about six years. With an 8 percent mortgage, the homeowner will sell the home, still owing over 90 percent of the mortgage. If this trend continued, the homeowner would *never* pay off a mortgage in his or her lifetime. *Imagine you have purchased a house for $97,000, with $9,700 down and a simple interest rate of 8 percent. How long would it take to pay off your mortgage if you paid $700 a month?*

STEP 4: Obtain Financing

What are the costs involved in purchasing property?

After you have decided to purchase a specific home and have agreed on a price, you will have to think about how you will pay for your purchase. First, you will have to come up with money for the down payment. Next, you will probably have to get a loan to help pay for the remainder of the purchase price. Finally, you will be responsible for fees and other expenses related to the settlement of the real estate transaction.

Determining Amount of Down Payment

As a general rule, the greater the portion of the total purchase price you can pay up front, the easier it will be to obtain a loan. Many lenders suggest that you put 20 percent or more of the purchase price as a down payment. For example, if the purchase price of the house is $100,000, you would need to make a down payment of $20,000. The most common sources of funds for down payments are personal savings accounts, sales of investments or other assets, or gifts or loans from relatives.

Private Mortgage Insurance Lenders might accept lower down payments. However, if the down payment is less than 20 percent of the purchase price, some lenders will require you to obtain private mortgage insurance. **Private mortgage insurance (PMI)** is a special policy that protects the lender in case the buyer cannot make payments or cannot make them on time. Sometimes buyers will pay the cost of PMI up front, and sometimes they will agree to spread the cost over the life of the loan. When the borrower has paid between 20 to 25 percent of the purchase price, the insurance can be dropped.

Qualifying for a Mortgage

A **mortgage** is a long-term loan extended to someone who buys property. The buyer borrows money from a bank, credit union, savings and loan association, or mortgage company, which pays the full amount of the loan to the seller. In return, the buyer makes monthly payments to the lender. These monthly payments are usually made over a period of 15, 20, or 30 years. The home you buy serves as collateral, a type of guarantee that the loan will be repaid. If you fail to repay the mortgage or make regular payments, the lender can foreclose, or take possession of the property.

Financial Qualifications To take out a mortgage, you need to meet certain criteria, just as you would to qualify for any other type of loan. Lenders look at your income, your debts, and your savings to decide whether you are a good risk. These figures are put into a formula to determine how much you can afford to pay.

As You Read

QUESTION

Lenders want to know how much money you owe. What other information do they look for?

▲ THE TEST Applying for a loan requires paperwork that will be examined by the lender to determine your eligibility for the loan. *Why is this process so important to the lender?*

Interest Rate Factors The size of your mortgage will also depend on the current interest rate. The higher the rate, the more you will need to pay in interest each month. That means that less of your money will be available to pay off the purchase price. When interest rates rise, fewer people are able to afford the cost of an average-priced home. In contrast, low rates increase the size of the loan that you can receive.

For example, Bernadette qualifies for a monthly mortgage payment of $700. If interest rates are 7 percent, she will be able to take out a 30-year loan of $105,215. However, if interest rates increase to 12 percent, she will qualify for a 30-year loan of only $68,053. Both of these loans will carry the same monthly payment of $700. The differences can be quite surprising.

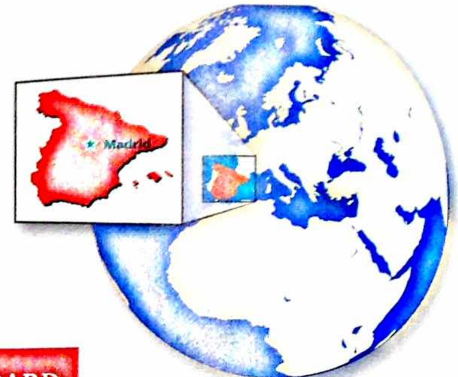
Paying Points

Different lenders may offer slightly different interest rates for mortgages. In addition, when you compare the cost of doing business with various lenders, you will have to consider other factors. If you want a lower interest rate, you may have to pay a higher down payment and **points**—extra charges that must be paid by the buyer to the lender in order to get a lower interest rate. Each point equals 1 percent of the loan amount. For example, suppose that a bank offers you a $100,000 mortgage with two points, or 2 percent. Since 2 percent of $100,000 is $2,000, you will have to pay an extra $2,000 when you get the loan to purchase your home.

STANDARD &POOR'S

Global Financial Landscape

Standard and Poor's publishes the globally recognized S&P 500® financial index. It also gathers financial statistics, information, and news, and analyzes this data for international businesses, governments, and individuals to help them guide their financial decisions.



SPAIN

Each year thousands of people from Britain make their way to Spain, seeking what their homeland does not offer—affordable housing. The average house in England costs more than 150,000 pounds (US $278,000). In comparison, a three-bedroom home not far from the beautiful Spanish coast costs less than 100,000 pounds (US $185,000). A roomy handyman's special can be found for under 20,000 pounds (US $37,000). Many of the British house-hunters may purchase a house to fit their pocketbooks, but there may be other motivations as well. Some buy Spanish property as an investment, and then lease the homes to renters. Others simply prefer the more stress-free life and agreeable climate of sunny Spain.

STANDARD &POOR'S **DATABYTES**

Capital	Madrid
Population	41,334,000
Languages	Castilian Spanish, Catalan, Galician, and Basque
Currency	euro
Gross Domestic Product (GDP)	$885.5 billion (2003 est.)
GDP per capita	$22,000

Industry: Textiles and apparel, food and beverages, metal manufacturing, and chemicals

Agriculture: Grain, vegetables, olives, wine grapes, beef, and fish

Exports: Machinery, motor vehicles, foodstuffs, and other consumer goods

Natural Resources: Coal, lignite, iron ore, and uranium

Think Globally
Would you buy a home in another country? Why or why not?

Comparing Points How does a high interest rate with no points compare to a low interest rate with points? A lower interest rate results in a lower monthly payment, but you pay more money up front.

If you keep your home for only a short time, you may lose money with the lower rate because the monthly savings will not add up to what you had to pay in points. If you keep the home for several years, however, your monthly savings will eventually make up for what you paid in points. As a rule, the longer you keep the home, the better off you are when paying the points in exchange for a lower interest rate.

The Loan Application Process

Most lenders charge home buyers a fee of between $100 and $300 to apply for a mortgage, which is added into the loan amount. To apply, the buyer must fill out forms, giving details of his or her income, employment, debts, and other information. The lender will verify this information by obtaining a buyer's credit report.

After a careful examination of the buyer's financial history and the size, location, and condition of the property, the lender decides to approve or deny the application. If it is approved, the purchase contract between seller and buyer becomes legally binding.

STANDARD & POOR'S

Put on Your Financial Planner's Cap

A client has $27,000 in savings and an excellent credit history. Assuming 20 percent down, what price should your client pay for a house?

Types of Mortgages

How do the various types of mortgages differ?

For most people, a mortgage is the greatest financial obligation of their lives. There are several types of mortgages. Depending on the terms of the loan, a homeowner will have to make monthly payments for many years.

The monthly payments on a mortgage are set at a level that allows amortization of the loan. **Amortization** is the reduction of a loan balance through payments made over a period of time. So the balance is reduced every time you make a payment. The amount of your payment is applied first to the interest owed and then to the principal, which is the original amount you borrowed. In the first years of the loan, only a small part of each monthly payment goes to reduce the principal. Most goes toward paying off the interest. Near the end of the loan period, almost all of each payment goes toward reducing the principal. By the end of the loan period, both the interest and the principal will be completely paid off.

It is possible to pay off a mortgage early. Paying a little extra each month and applying that amount to the principal will save interest charges over the long run. For example, paying $25 extra a month on a 30-year, 10 percent mortgage of $75,000 will save more than $34,000 in interest charges—and will repay the loan in about 25 years. Some lenders charge an extra fee for prepaying.

Fixed-Rate Mortgages

A **fixed-rate mortgage**, or conventional mortgage, is a mortgage with a fixed interest rate and a fixed schedule of payments. A fixed rate is an interest rate that does not change. For example, if the interest rate is 8.75 percent when the loan is granted, the homeowner will continue to pay 8.75 percent throughout the life of the loan, even if interest rates for new loans rise. Conventional mortgages typically run for a period of 15, 20, or 30 years. They offer peace of mind because monthly payments always remain the same.

Adjustable-Rate Mortgages

Fixed-rate loans guarantee a particular interest rate for the life of the loan. An **adjustable-rate mortgage (ARM)**, also known as a variable-payment mortgage, is a mortgage with an interest rate that increases or decreases during the life of the loan. The rate changes according to economic indicators, such as rates on U.S. Treasury securities, the Federal Home Loan Bank Board's mortgage rate index, or the lender's own cost-of-funds index. As a result, your loan payments may go up or down.

Your rates will change according to the terms of your agreement with the lender. Generally, if interest rates decline and stay low, an ARM will save you substantial amounts of money. However, if rates increase and stay high, an ARM may cost you a lot of money because your monthly payment will go up.

Evaluating Adjustable-Rate Mortgages Consider several factors when you evaluate adjustable-rate mortgages:

1. Determine the frequency of and restrictions on allowed changes in interest rates.
2. Consider the frequency of and restrictions on changes in the monthly payment.
3. Find out what index the lender will use to set the mortgage interest rate over the term of the loan.

Rate Caps Most adjustable-rate mortgages have a rate cap, which limits the amount the interest rate can rise or fall. Rate caps generally limit increases (or decreases) of the interest rate to one or two percentage points in a year—or no more than five points over the life of the loan.

Some ARMs also carry payment caps, which limit the size of monthly payments. That may seem like good protection for the buyer, but it has drawbacks. When interest rates rise while monthly payments remain the same, the payments will not cover the interest. As a result, the loan balance increases, and payments may have to be extended over a longer time.

Convertible ARMs Some lenders also offer convertible ARMs. Convertible ARMs permit a borrower to convert, or change, an adjustable-rate mortgage to a fixed-rate mortgage during a certain period of time. If you decide to make the change, your interest rate will be 0.25 to 0.50 percent higher than current rates for conventional 30-year mortgages. You will also have to pay a conversion fee, which is usually $500 or less.

Government Financing Programs The Federal Housing Administration (FHA) and the Veterans Administration (VA) help home buyers obtain low-interest, low-down-payment loans. VA loans are available to eligible veterans of the armed services. These government agencies do not actually lend the money. Instead, they help qualified buyers arrange for loans from regular lenders.

Typically, an agency guarantees repayment to the lender if the borrower defaults, or is unable to make payments. As a result, many government-guaranteed loans have lower interest rates. Although extra insurance fees may be added on to these loans, government-backed mortgages are a good deal for those who qualify for them.

Home Equity Loans

A second mortgage is also called a **home equity loan**, which is a loan based on the difference between the current market value of a home and the amount the borrower owes on the mortgage. To determine the amount of this type of loan, the financial institution will find out the current market value of a home and how much equity is in the property. Such loans can provide money for education, home improvements, or other purposes. However, some states limit the ways in which the money may be used.

Second mortgages are one source of extra cash for homeowners. However, taking out additional loans can keep a homeowner continually in debt. Also, if the borrower cannot make the payments on a second mortgage, the lender can take the home. For more information on home equity loans, see Chapter 19.

Refinancing

Many homeowners need extra money or want to reduce their monthly payments. These options are possible when they **refinance**, which is obtaining a new mortgage to replace an existing one. For example, Esther Aquino originally took out a fixed-rate mortgage at 11 percent interest, and then watched interest rates fall to 6 percent. Fortunately, she was able to refinance her home, and take out a new mortgage at the lower 6 percent interest rate. In Esther's case, her monthly payment decreased considerably.

Refinancing is not always a good choice. To refinance, a homeowner usually pays extra fees, which may reduce any savings from a small drop in interest rates. Moreover, refinancing may extend the life of a loan. In general, refinancing is an advantage when the interest rate drops two or more points below the current rate and when the owner plans to stay in his or her present home for at least two or more years.

WebQuest

Your Own Home
Learn about different kinds of mortgages and how to qualify for one. Then learn how to negotiate the purchase of your first home.

To continue with Tasks 4 and 5 of your WebQuest project, visit **persfinance07.glencoe.com**.

STEP 5: Close the Transaction

What are closing costs?

The final step in the home-buying process is the **closing**, a meeting of the seller, the buyer, and the lender of funds, or representatives of each party, to complete the transaction. At the closing, documents are signed, last-minute details are settled, and money is paid. The seller and buyer must also pay a number of fees and charges, which are *closing costs*.

Closing Costs

Most closing costs involve the legal details related to purchasing a home. For example, a title company researches the property to make sure that no disputes exist over its ownership or that there are no unpaid real estate taxes for the property. The title company also offers **title insurance**, a type of insurance that protects the buyer if problems with the title are found later.

Another typical closing cost is a fee for recording the **deed**, which is the official document transferring ownership from seller to buyer. Buyers also pay for private mortgage insurance, which protects the lender from any loss resulting from default on the loan. See **Figure 7.7** for a list of other common closing costs.

Escrow Account

After the closing, your lender might require that you deposit money into an escrow account. The money, usually held by the lender, is set aside to pay for taxes and insurance. The lender does not have to worry whether the borrower is paying these obligations because the money is available. See **Figure 7.8** for a list of home-buying issues.

Taxes and Insurance Homeowners must pay property taxes and homeowners insurance in addition to their mortgage payments. In most states, property taxes generally cover the cost of public services, such as police and fire protection, schools, and street repair. Homeowners insurance protects the lender's investment in case of damage to the home from fire or other hazards.

Figure 7.7 **Closing Costs**

Item	Cost Range: Buyer	Cost Range: Seller
Title search fee	\$ 50 – \$ 100	\$ 300 – \$ 900
Title insurance	\$ 300 – \$ 900	\$ 50 – \$1000
Attorney's fee	\$ 50 – \$1000	\$ 100 – \$ 500
Property survey	–	–
Appraisal fee	\$ 100 – \$ 350	–
Recording fees	\$ 30 – \$ 65	\$ 35 – \$ 65
Credit report	\$ 35 – \$ 75	–
Termite inspection	\$ 100 – \$ 250	–
Lender's origination fee	1–5% of loan	–
Real estate agent's commission	–	5–7% of purchase price
Insurance, taxes, and interest	varies	–

Costs Add Up Closing costs add to the expense of buying a home.

For a loan amount of \$100,000 with \$3,500 in insurance, taxes, and interest, what could a buyer pay in closing costs, based on the figures in this chart?

Figure 7.8 The Elements of Buying a Home

It is important to consider these factors when making a home purchase:

- **Location** Consider both the surrounding community and the geographic region. The same home may vary greatly in cost depending on where it is located: in Kansas or California, on a busy highway or a quiet street, in a landscaped suburb or an urban neighborhood.
- **Down Payment** A large down payment reduces your mortgage costs, but how much can you afford to pay up front?
- **Mortgage Rates and Points** You will have to choose between a lower mortgage rate with points and a higher mortgage rate without points. You will also need to consider what type of mortgage to arrange. When you apply for the loan, be prepared to provide the lender with copies of your financial records and other relevant information.
- **Closing Costs** Settlement costs may range anywhere from 2 to 6 percent of the total amount you borrow. That is in addition to the down payment.
- **Monthly Payments** Your monthly payment for interest, principal, insurance, and taxes will be among your largest, most enduring expenses. Beware of buying a home that costs more than you can afford.
- **Maintenance Costs** Homes require a lot of repair and maintenance. Be sure to set aside funds for these necessities.

Think It Over Buying a home is a complicated process.

What are some possible results of not thinking through all the elements listed above?

Selling a Home

What can an owner do to his or her home to get the best selling price?

As your needs change, you may decide to sell your home. You will have to get it ready for the market, set a price, and decide whether to sell it on your own or get professional help from a real estate agent.

Preparing a Home for Selling

The nicer your home looks, the faster it will sell at the price you want. Real estate salespeople recommend that homeowners make needed repairs and paint worn exterior and interior areas when preparing a home for selling. For example, Dora and Dennis Muldoon repainted several rooms, replaced some light fixtures, and changed the living room carpet before they put their house on the market. They kept the house as clean, neat, bright, and airy as possible while prospective buyers were visiting. They also made sure that the lawn was cut regularly and that their children did not leave toys in the yard. Their work paid off: They sold their home within a few months of listing their home.

LENDING A HAND

A real estate agent will suggest to a seller ways to improve the "curb appeal" of a home, such as landscaping, to attract buyers. *What is the biggest disadvantage of using a real estate agent?*

Determining the Selling Price

Setting a price on a home can be difficult. A price that is too high may scare off potential buyers. Setting the price too low will result in lost profit. Some sellers will pay for an **appraisal**—an estimate of the current value of the property—and use that as a basis for a listing price. If you ever sell a home, find out whether the current market and demand for housing favors buyers or sellers. Then decide how quickly you need to sell your home and evaluate any improvements you have made to the property. Adding certain features—such as a deck or an extra bathroom—can increase a home's value.

Choosing a Real Estate Agent

Many sellers put the sale of their home into the hands of a licensed real estate agent who is affiliated with an agency. There is a wide choice of firms, from small local real estate agencies to nationally known companies. When choosing an agent, pick someone who knows your neighborhood and is eager to sell your home.

Real Estate Agent Services Real estate agents provide various services. They can help determine a selling price, attract buyers, show your home, and handle the financial aspects of the sale.

They are paid a commission, or fee, upon the sale of a home—usually 5 to 7 percent of the purchase price.

Sale by Owner

Each year about 10 percent of home sales are made directly by homeowners without the help of real estate agents. Selling your home yourself can save you thousands of dollars, but it will cost you time and energy. Advertising the home will be up to you. Showing the home to prospective buyers will also be your responsibility. Be sure to use the services of a lawyer or a title company to help you with the contract, closing, and other legal matters.

Making Choices

Your housing decisions will be affected by many factors, including your lifestyle and financial situation. By carefully reviewing your options, making educated decisions, and following the appropriate processes, you will make the best housing choice to suit your needs.

After You Read

REACT

With the information provided in this chapter, do you feel that you could make a wise decision about whether to rent or buy a home? Why or why not?

Section 7.3 Assessment

QUICK CHECK

1. What are five steps that make up the process of buying a home?
2. What costs are associated with buying a home?
3. What activities are associated with selling a home?

THINK CRITICALLY

4. State three reasons you should carefully inspect the property you plan to purchase.

USE COMMUNICATION SKILLS

5. **Owner Obligations** Imagine that you are a condominium owner attending a meeting of the condominium association. What should the association do about a homeowner who leaves garbage in the hallway? Should the association limit the use of the pool and tennis courts to owners?

Write About It Write a paragraph answering one of the questions.

SOLVE MONEY PROBLEMS

6. **Making an Offer** After several weeks of searching for a new home, Renée has found a house that seems to be in good shape and is located in a nice neighborhood. The listing price is $125,000, which is about $15,000 more than she wants to pay. She would like to make a lower bid, but the housing market is tight, and she worries that someone else may buy the house at the listing price. Renée wonders what she should do.

Analyze Working in a small group, brainstorm some ideas about what factors Renée should consider in making a decision.