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## Closing Costs FAQ and Some Pointers on Points



### DWELLING ON DWELLINGS:

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Perhaps the most confusing time for a homebuyer is at closing. It's easy to be intimidated by myriad fees and an alphabet soup of terms. If, however, you understand what to expect at closing, you'll be better prepared to open the prospect of buying a house. You'll have a better idea of what you can afford and what you'll be expected to pay. And perhaps, you'll be better prepared to negotiate some of your fees.

To help you understand, the process, here some answers to a few frequently asked questions.

#### **What are closing costs and how much should I expect to pay?**

If you're buying a piece of property, you should expect to pay a tad more than just the cost of the property. When it comes time to "close the deal," there will be an assortment of fees due. Some of these fees will be assigned to the seller. Some are customarily paid by the buyer. And some are completely open to negotiation.

At or before closing, buyers typically are expected to pay a mortgage down payment; loan fees, such as points, application fees, credit report fees, and underwriting fees; documentation preparation fees; inspection fees; appraisal and survey fees; courier fees; mortgage insurance; hazard insurance; attorney fees; title insurance; city, county, and state recording and transfer charges; and pre-paid interest and escrow amounts.

The amount of such fees can vary greatly. Some mortgage types, for example, require greater down payments. Some vary on the amount of points paid. However, you should have a reasonable idea of how much you'll owe before you sit down at the closing table. By law, your lender is required to give you a good-faith estimate on your closing costs.

Typically, minimum required down payments range from 3 to 5 percent of the home price. The other closing costs may add up to an additional 3 to 6 percent of the sales price.

#### **What are points?**

A "point" -- sometimes called a "discount point" -- is equal to 1 percent of the loan amount. For example, on a \$150,000 mortgage, a point would be \$1,500. The interest rate you choose and current market conditions determine how many

points a lender usually charges to secure a mortgage .

### **What's the point of points and why do I have to pay them?**

Think of points as up-front interest paid ... and as a way to lock in on a lower interest rate. Generally, the more points you pay, the lower the interest rate you'll get on your loan. Lenders charge points as a way to recoup their costs of processing and making a loan. With interest rates dropping so low, and the competition within the mortgage industry rising, lenders are facing very thin profit margins. Closing costs such as points help them stay in business and maintain their support staffs and underwriting departments.

To determine whether you should pay points for a lower interest rate mortgage or seek a no-point loan, do a quick break-even analysis. First calculate the cost of the points. For example, if the lender is asking for two points on a \$150,000 mortgage, your cost is \$3,000.

Next, calculate the monthly savings on the loan as a result of getting a lower interest rate. According to Freddie Mac, the average rate on a 30-year fixed rate mortgage as of November 14, 2002, was 5.94 percent with 0.6 points. A typical "no-point" 30-year fixed-rate loan these days might go for 6.25 percent.

So let's take our \$150,000 mortgage example. At 5.94 percent for 30 years, you might expect to pay \$893 monthly (not counting taxes!). At 6.25 percent, your payments will be around \$923 -- \$30 more than the loan with the points .

So let's divide the cost of the points by the monthly savings to come up with a number of months you need to break even. In our example, 0.6 points equals \$900 (*i.e.*, \$150,000 x 1 percent x 0.6). \$900 divided by \$30 equals 30 months. So if you plan to live in your new house for more two and a half years, you'd be better off paying the points in this case.

In short, you should shop around for the best mortgage deal. And the best time to do your shopping is long before you make an offer. Talk to lenders. With today's competition, there are some great deals out there. Get pre-qualified. And then, when the seller is ready to open the bidding, you'll be better prepared for the closing.

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