

## **Glossary of Mortgage Terms**

Shopping for a mortgage? If you are one of the tens of thousands of today's home shoppers, you probably have discovered that mortgage lending has a language all its own. For example, you've probably heard about "points", "margins", and "repayment penalties." Should you look for an "assumption?" What are "acceleration clauses?" For the unprepared, this new terminology can be quite confusing. As with any contract, before you sign your mortgage, you should know what you are signing.

### **Acceleration Clause**

Allows the lender to speed up the rate at which your loan comes due or even to demand immediate payment of the entire outstanding balance of the loan should you default on you loan.

### **Adjustable Rate Mortgage (ARM)**

A mortgage in which the interest rate is adjusted periodically based on a pre-selected index.

### **Adjustment Interval**

On an adjustable rate mortgage, the time between changes in the interest rate and/or monthly payment, typically one, three or five years, depending on the index.

### **Amortization**

Means loan payment by equal periodic payments calculated to pay off the debt at the end of a fixed period, including accrued interest on the outstanding balance.

### **Annual Percentage Rate (APR)**

an interest rate that reflects the cost of a mortgage as a yearly rate.

### **Appraisal**

An estimate of the value of property, made by a qualified professional called an "appraiser."

### **Assumption**

The agreement between buyer and seller where the buyer takes over the payments on an existing mortgage from the seller. Assuming a loan can usually save the buyer money. Since this is an existing mortgage debt, unlike a new mortgage where closing costs and new, possibly higher, market-rate interest charge will apply.

### **Balloon (Payment) Mortgage**

Usually a short-term fixed-rate loan which involves small payments for a certain period of time and one large payment for the remaining amount of the principal at a time specified in the contract.

### **Broker**

An individual in the business of assisting in arranging funding or negotiating contracts for a client, but who does not loan the money himself. Brokers usually charge a fee or receive a commission for their services.

### **Buydown**

When the lender and/or the home builder subsidizes the mortgage by lowering the interest rate during the first few years of the loan. While the payments are initially low, they will increase when the subsidy expires.

**Caps (Interest)**

Consumer safeguards which limit the amount the interest rate on an adjustable rate mortgage may change per year and/or the life of the loan.

**Caps (Payment)**

Consumer safeguards which limit the amount monthly payments on an adjustable rate mortgage may change.

**Closing**

The meeting between the buyer, seller and lender or their agents, where the property and funds legally change hands. Also called settlement.

**Closing Costs**

Usually include an origination fee, discount points, appraisal fee, title search and insurance, survey, taxes, deed recording fee, credit report charge and other costs assessed at settlement. The costs of closing are usually about 3 percent to 6 percent of the mortgage amount.

**Commitment**

An agreement, often in writing, between a lender and a borrower to loan money at a future date subject to the completion of paperwork or compliance with stated conditions.

**Construction Loan**

A short term interim loan to pay for the construction of buildings or homes.

**Conventional Loan**

A mortgage not insured by FHA or guaranteed by the VA or Farmers Home Administration (FmHA).

**Credit Ratio**

The ratio, expressed as a percentage, which results when a borrower's monthly payment obligation on long-term debts is divided by his or her net effective income (FHA/VA loans) or gross monthly income (Conventional loans).

**Debt-to-income Ratio**

The ratio, expressed as a percentage, which results when a borrower's monthly payment obligation on long-term debts is divided by his or her gross monthly income.

**Deed of Trust**

In many states, this document is used in place of a mortgage to secure the payment of a note.

**Default**

Failure to meet legal obligations in a contract, specifically, failure to make the monthly payments on a mortgage.

**Deferred Interest**

See Negative Amortization.

**Delinquency**

Failure to make payments on time. This can lead to foreclosure.

**Department of Veterans Affairs (VA)**

An independent agency of the federal government which guarantees long-term, low- or no-down payment mortgages to eligible veterans.

**Discount Points**

Prepaid interest assessed at closing by the lender. Each point is equal to 1 percent

of the loan amount (e.g. two points on a \$100,000 mortgage would cost \$2,000).

**Down Payment**

Money paid to make up the difference between the purchase price and mortgage amount. Down payments usually are 10 percent to 20 percent of the sales price on Conventional loans, and no money down up to 5 percent on FHA and VA loans.

**Due-On-Sale Clause**

A provision in a mortgage or deed of trust that allows the lender to demand immediate payment of the balance of the mortgage if the mortgage holder sells the home.

**Earnest Money**

Money given by a buyer to a seller as part of the purchase price to bind a transaction or assure payment.

**Equal Credit Opportunity Act (ECOA)**

A federal law that requires lenders and other creditors to make credit equally available without discrimination based on race, color, religion, national origin, age, sex, marital status or receipt of income from public assistance programs.

**Equity**

The difference between the fair market value and current indebtedness, also referred to as the owner's interest.

**Escrow**

An account held by the lender into which the homebuyer pays money for tax or insurance payments.

**Fannie Mae**

See Federal National Mortgage Association.

**Farmers Home Administration (FmHA)**

Provides financing to farmers and other qualified borrowers who are unable to obtain loans elsewhere.

**Federal Home Loan Mortgage Corporation (FHLMC)**

Also called **Freddie Mac**, is a quasi-governmental agency that purchases conventional mortgages from insured depository institutions and HUD-approved mortgage bankers.

**Federal Housing Administration (FHA)**

A division of the Department of Housing and Urban Development. Its main activity is the insuring of residential mortgage loans made by private lenders. FHA also sets standards for underwriting mortgages.

**Federal National Mortgage Association (FNMA)**

Also known as **Fannie Mae**. A tax-paying corporation created by Congress that purchases and sells conventional residential mortgages as well as those insured by FHA or guaranteed by VA. This institution, which provides funds for one in seven mortgages, makes mortgage money more available and more affordable.

**FHA Loan**

A loan insured by the Federal Housing Administration open to all qualified home purchasers. While there are limits to the size of FHA loans, they are generous enough to handle moderate-priced homes almost anywhere in the country.

**FHA Mortgage Insurance**

Requires a small fee (up to 3 percent of the loan amount) paid at closing or a

portion of this fee added to each monthly payment of an FHA loan to insure the loan with FHA. On a 9.5 percent \$75,000 30-year fixed-rate FHA loan, this fee would amount to either \$2,250 at closing or an extra \$31 a month for the life of the loan. In addition, FHA mortgage insurance requires an annual fee of 0.5 percent of the current loan amount, the more years the fee must be paid.

**Fixed-Rate Mortgage**

A mortgage on which the interest rate is set for the term of the loan.

**Foreclosure**

A legal procedure in which property securing debt is sold by the lender to pay a defaulting borrower's debt .

**Freddie Mac**

See Federal Home Loan Mortgage Corporation.

**Ginnie Mae**

See Government National Mortgage Association.

**Government National Mortgage Association (GNMA)**

Also known as **Ginnie Mae**, provides sources of funds for residential mortgages, insured or guaranteed by FHA or VA.

**Graduated Payment Mortgage (GPM)**

A type of flexible-payment mortgage where the payments increase for a specified period of time and then level off. This type of mortgage has negative amortization built into it.

**Gross Monthly Income**

The total amount the borrower earns per month, before any taxes or expenses are deducted.

**Guarantee**

A promise by one party to pay a debt or perform an obligation contracted by another, if the original party fails to pay or perform according to a contract.

**Hazard Insurance**

A form of insurance in which the insurance company protects the insured from specified losses, such as fire, windstorm and the like.

**Housing Expenses-to-Income Ratio**

The ratio, expressed as a percentage, which results when a borrower's housing expenses are divided by his/her net effective income (FHA/VA loans) or gross monthly income (Conventional loans).

**Impound**

That portion of a borrower's monthly payments held by the lender or servicer to pay for taxes, hazard insurance, mortgage insurance, lease payments, and other items as they become due. Also known as reserves.

**Index**

A published interest rate against which lenders measure the difference between the current interest rate on an adjustable rate mortgage and that earned by other investments (such as one-, three-, and five-year U.S. Treasury Security yields, the monthly average interest rate on loans closed by savings and loan institutions, and the monthly average Costs-of-Funds incurred by savings and loans), which is then used to adjust the interest rate on an adjustable mortgage up or down.

**Investor**

Money source for a lender.

**Jumbo Loan**

A loan which is larger than the limits set by the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation. Because jumbo loans cannot be funded by these two agencies, they usually carry a higher interest rate.

**Lien**

A claim upon a piece of property for the payment or satisfaction of a debt or obligation.

**Loan-To-Value Ratio**

The relationship between the amount of the mortgage loan and the appraised value of the property expressed as a percentage.

**Margin**

The amount a lender adds to the index on an adjustable rate mortgage to establish the adjusted interest rate.

**Market Value**

The highest price a buyer would pay and the lowest price a seller would accept on a property. Market value may be different from the price a property could actually be sold for at a given time.

**Mortgage Insurance**

Money paid to insure the mortgage when the down payment is less than 20 percent. See Private Mortgage Insurance or FHA Mortgage Insurance.

**Mortgagee**

The lender.

**Mortgagor**

The borrower or homeowner.

**Negative Amortization**

Occurs when your monthly payments are not large enough to pay all the interest due on the loan. This unpaid interest is added to the unpaid balance of the loan. The danger of negative amortization is that the homebuyers ends up owing more than the original amount of the loan.

**Net Effective Income**

The borrower's gross income minus federal income tax.

**Non-Assumption Clause**

A statement in a mortgage contract forbidding the assumption of the mortgage without the prior approval of the lender.

**Origination Fee**

The fee charged by a lender to prepare loan documents, make credit checks, inspect and sometimes appraise a property; usually computed as a percentage of face value of the loan.

**PITI**

Principal, interest, taxes, and insurance. Also called monthly housing expense.

**Points**

See Discount Points

**Power of Attorney**

A legal document authorizing one person to act on behalf of another.

**Prepays**

Expenses necessary to create an escrow account or to adjust the seller's existing escrow account. Can include taxes, hazard insurance, private mortgage insurance and special assessments.

**Prepayment**

A privilege in a mortgage permitting the borrower to make payments in advance of their due date.

**Prepayment Penalty**

Money charged for an early repayment of debt. Prepayment penalties are allowed in some form (but not necessarily imposed) in 36 states and the District of Columbia.

**Principal**

The amount of debt, not counting interest.

**Private Mortgage Insurance (PMI)**

On conventional loans, if your down payment on a home is less than 20 percent of the appraised value or sale price, you must obtain private mortgage insurance, known as PMI, with your lender. This will enable you to obtain a mortgage with a lower down payment because your lender is now protected against any default on the loan.

**Realtor**

A real estate broker or an associate holding active membership in a local real estate board affiliated with the National Association of Realtors.

**Rescission**

The cancellation of a contract. With respect to mortgage refinancing, the law that gives the homeowner three days to cancel a contract. In some cases, once it is signed if the transaction uses equity in the home as security.

**Recording Fees**

Money paid to the lender for recording a home sale with the local authorities, thereby making it part of the public records.

**Renegotiable Rate Mortgage (RRM)**

A loan in which the interest rate is adjusted periodically. See Adjustable Rate Mortgage.

**Real Estate Settlement Procedures Act (RESPA)**

RESPA is a federal law that allows consumers to review information on known or estimated settlement costs once after application and once prior to or at settlement. The law requires lenders to furnish information after application only.

**Reverse Annuity Mortgage (RAM)**

A form of mortgage in which the lender makes periodic payments to the borrower using the borrower's equity in the home as security.

**Servicing**

All the steps and operations a lender perform to keep a loan in good standing, such as collection of payments, payment of taxes, insurance, property inspections and the like.

**Settlement**

See Closing.

**Settlement Costs**

See Closing Costs.

**Shared Appreciation Mortgage (SAM)**

A mortgage in which a borrower receives a below-market interest rate in return for which a lender (or another investor such as a family member or other partner) receives a portion of the future appreciation in the value of the property. May also apply to mortgages where the borrower shares the monthly principal and interest payments with another party in exchange for a part of the appreciation.

**Survey**

A measurement of land, prepared by a registered land surveyor, showing the location of the land with reference to known points, its dimensions, and the location and dimensions of any building.

**Term Mortgage**

See Balloon Payment Mortgage.

**Title**

A document that gives evidence of an individual's ownership of property.

**Title Insurance**

a policy, which insures a homebuyer against errors in the title search.

**Title Search**

An examination of municipal records to determine the legal ownership of property. Usually is performed by a title company.

**Truth-in-Lending**

A federal law requiring disclosure of the Annual Percentage Rate to homebuyers shortly after they apply for the loan.

**Two-Step Mortgage**

A mortgage in which the borrower receives a below-market interest rate for a specified number of years (most often seven or 10 years), and then receives a new interest rate adjusted (within certain limits) to market conditions at that time. The lender sometimes has the option to call the loan, due within 30 days notice at the end of seven or 10 years. Also called "Super Seven" or "Premier" mortgage.

**Underwriting**

The decision whether to make a loan to a potential homebuyers based on credit, employment, assets, and other factors and the matching of this risk to an appropriate rate and term or loan amount.

**VA Loan**

A long-term, low-or no-down payment loan guaranteed by the Department of Veterans Affairs. Restricted to individuals qualified by military service or other entitlements.

**VA Mortgage Funding Fee**

a premium paid on a VA-backed loan. .

**Variable Rate Mortgage (VRM)**

See Adjustable Rate Mortgage.

**Verification of Deposit (VOD)**

A document signed by the borrower's financial institution verifying the status and balance of his/her financial accounts.

**Verification of Employment (VOE)**

A document signed by the borrower's employer verifying his/her position and

salary.

**Wraparound**

Results when an existing assumable loan is combined with a new loan, resulting in an interest rate somewhere between the old rate and the current market rate.

The payments are made to a second lender or the previous homeowner, who then forwards the payments to the first lender after taking the additional amount off the top.