

Saving for the Down Payment

Saving funds for a down payment should be part of an overall program to get your finances in order prior to shopping for a home. This includes rounding up financial records, examining your spending habits, and setting a budget you can live with. Remember, too, that the down payment is not the only up-front expense. An allowance for closing costs should also be included in your savings budget.

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How much is required?

The down payment is usually expressed as a percentage of the overall purchase price of the home, and varies depending on the lender, the type of financing and amount of money being lent. In the past, the typical down payment was 20%, but in recent years lenders have been willing to offer conventional financing with as little as 3% down. U.S. Government financing programs, such as those offered by the Dept. of Veterans Affairs (VA) or the Federal Housing Administration (FHA), also require minimal down payments.

Private mortgage insurance

Typically, if your down payment is less than 20% of the purchase price, lenders will require you to carry PMI, or private mortgage insurance. This insurance protects the lender in case of loan default, and usually involves an up-front payment at closing, as well as a monthly premium. However, once you have paid off 20% of the loan, you can request the policy be canceled. Some lenders cancel the premium automatically, while others require you to make a request in writing.

Gifts

If you are having trouble saving enough money, many lenders will allow you to use gift funds for the down payment--as well as for related closing costs. The gift may come from family, friends or other sources, but remember that lenders usually require a "gift letter" stating the gift doesn't have to be repaid. In addition, some lenders will also require you to pay at least a portion of the down payment with your own cash. Thus, if you plan to use gift money to purchase your house, ask your lender about their policies regarding gifts.

Earnest money

Buyers are usually required to deposit earnest money with

the seller when they make an offer. If the offer is accepted, the earnest money is then credited towards the down payment. The amount varies widely depending on the seller and local custom, but be prepared from the outset to have funds earmarked for this purpose.

Don't forget closing costs

In addition to the down payment, you will also need to save for additional fees associated with the loan. Known as closing costs, these charges cover items such as title insurance, documentary stamps, loan origination fees, the survey, attorney's fees, etc. When you submit your loan application, lenders are required to supply you with a good faith estimate of your closing costs.

Some buyers are surprised by the amount of the closing costs, which can easily run into the thousands of dollars. Remember, though, that closing costs can be negotiated with the seller. For example, you may agree to pay the full asking price in exchange for the seller paying all the allowable closing costs.