

WHAT TO KNOW

The Buying Process

Now that you've decided to take the plunge, let's explore what you can expect from the homebuying process itself. This can be a chaotic time with offers and counteroffers flying furiously, but if you are prepared for the hassle (and the paperwork), you can get through the process with your sanity intact. Here is the basic progression you can expect:

Find a home

Make sure to take advantage of all the available options for finding homes on the market, including using your real estate agent, searching for listings online, and driving around the neighborhoods that interest you in search of for-sale signs. Put some feelers out with your friends, family, and business contacts, too. You never know where a good reference or lead on a home might come from. Once you're seriously shopping for a home, don't walk into an open house without having an agent (or at least being prepared to throw out the name of someone you're working with). You can see how it might not work in your best interest to start dealing with a seller's agent before contacting one of your own. If you're on a budget, look for homes whose full potential has yet to be realized. Even if you can't afford to replace the hideous wallpaper in the bathroom now, you may be willing to live with it for a while in exchange for getting into a place you can afford. If the home meets your needs in terms of the big things that are difficult to change, such as location and size, don't let physical imperfections turn you away. First-time homebuyers should look for a house they can add value to, as this ensures a bump in equity to help them up the property ladder.

Consider your financing options and secure financing

First-time homebuyers have a wide variety of options to help them get into a home—both those available to any purchaser, including Federal Housing Authority (FHA)-backed mortgages, and those geared especially to novices. Many first-time homebuyer programs offer minimum down payments as low as 3% to 5% (vs. the standard 20%), and a few require no down payment at all. Be sure to look into or consider:

- HUD's resource list. Although the government agency itself does not make grants directly to individuals, it does grant funds earmarked for first-time homebuyers to organizations with IRS tax-exempt status. The HUD website has details. The FHA (and its loan program) is part of HUD.
- Your IRA. Every first-time homebuyer can withdraw up to \$10,000 out of their individual traditional IRA or Roth IRA without paying the 10% penalty for early withdrawal (but you'll still pay taxes if you use a traditional IRA). That means a couple could withdraw a maximum of \$20,000 (\$10,000 from each account) to use toward a first-home purchase. Just know that if you don't repay the money within 120 days—and you're under 59½—it becomes subject to the 10% penalty. You also will owe income taxes on the withdrawal(s).
- Your state's programs. Many states, including Illinois, Ohio, and Washington, offer financial assistance with down payments and closing costs, as well as with expenses to rehab or improve a property, for first-time homebuyers who qualify. Typically, eligibility in these programs is based on income and, often, the size of a property's purchase price. Native American options. Native American homebuyers can apply for a Section 184 loan. This loan requires a 1.5% loan up-front guarantee fee and a 2.25% down payment on loans over \$50,000 (for loans below that amount, it's 1.25%). Section 184 loans can only be used for single-family homes (one to four units) and for primary residences.

Don't be bound by loyalty to your current financial institution when seeking a preapproval or searching for a mortgage: Shop around, even if you only qualify for one type of loan. Fees can be surprisingly varied. An FHA loan, for example, may have different fees depending on whether you're applying for the loan through a local bank, credit union, mortgage banker, large bank, or mortgage broker. Mortgage interest rates, which of course have a major impact on the total price you pay for your home, can also vary. Once you've settled on a lender and applied, the lender will verify all of the financial information provided (checking credit scores, verifying employment information, calculating DTIs, etc.). The lender can preapprove the borrower for a certain amount. Be aware that even if you have been preapproved for a mortgage, your loan can fall through at the last minute if you do something to alter your credit score, such as finance a car purchase. Some authorities also recommend having a back-up lender. Qualifying for a loan isn't a guarantee your loan will eventually be funded: Underwriting guidelines can shift, lender risk-analysis can change, and investor markets can alter. Clients may sign loan and escrow documents, and then be notified 24 to 48 hours before the closing that the lender has frozen funding on their loan program. Having a second lender that has already qualified you for a mortgage gives you an alternate way to keep the process on, or close to, schedule.

Make an offer

Your real estate agent will help you decide how much money you want to offer for the house, along with any conditions you want to ask for. Your agent will then present the offer to the seller's agent; the seller will either accept your offer or issue a counteroffer. You can then accept, or continue to go back and forth until you either reach a deal or decide to call it quits. Now that you've decided to take the plunge, let's explore what you can expect from the homebuying process itself. This can be a chaotic time with offers and counteroffers flying furiously, but if you are prepared for the hassle (and the paperwork), you can get through the process with your sanity intact.

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Before submitting your offer, take another look at your budget. This time, factor in estimated closing costs (which can total anywhere from 2% to 5% of the purchase price), commuting costs, and any immediate repairs and mandatory appliances you may need before you can move in. Think ahead: It's easy to be ambushed by higher or unexpected utilities and other costs if you are moving from a rental to a larger home. You might request energy bills from the past 12 months, for example, to get an idea of average monthly costs. When you review your budget, don't overlook hidden costs, such as the home inspection, home insurance, property taxes, and homeowners association fees. If you reach an agreement, you'll make a good-faith deposit and the process then transitions into escrow. Escrow is a short period of time (often about 30 days) during which the seller takes the house off the market with the contractual expectation that you will buy it—provided you don't find any serious problems with it when you inspect it.

Have the home inspected

Even if the home you plan to purchase appears to be flawless, there's no substitute for having a trained professional do a home inspection of the property for the quality, safety, and overall condition of your potential new home. You don't want to get stuck with a money pit or with the headache of performing a lot of unexpected repairs. If the home inspection reveals serious defects that the seller did not disclose, you'll generally be able to rescind your offer and get your deposit back. Alternatively, you can negotiate to have the seller make the repairs or discount the selling price.

Close—or move on

If you're able to work out a deal with the seller, or better yet, if the inspection didn't reveal any significant problems, you should be ready to close. Closing basically involves signing a ton of paperwork in a very short time period, while praying that nothing falls through at the last minute. Things you'll be dealing with and paying for in the final stages of your purchase may include having the home appraised (mortgage companies require this to protect their interest in the house), doing a title search to make sure that no one other than the seller has a claim to the property, obtaining private mortgage insurance or a piggyback loan if your down payment is less than 20%, and completing mortgage paperwork. Other closing costs can include loan-origination fees, title insurance, surveys, taxes, and credit-report charges.

Congratulations, New Homeowner! Now What?

You've signed the papers, paid the movers, and the new place is starting to feel like home. Game over, right? Not quite. Homeownership costs extend beyond down payments and monthly mortgage payments. Let's now go over some final tips to make life as a new homeowner more fun and secure.

Keep saving

With homeownership comes major unexpected expenses, such as replacing the roof or getting a new water heater. Start an emergency fund for your home so that you won't be caught off-guard when these costs inevitably arise.

Perform regular maintenance

With the large amount of money you're putting into your home, you'll want to make sure to take excellent care of it. Regular maintenance can decrease your repair costs by allowing problems to be fixed when they are small and manageable.

Ignore the housing market

It doesn't matter what your home is worth at any given moment except the moment when you sell it. Being able to choose when you sell your home, rather than being forced to sell it due to job relocation or financial distress, will be the biggest determinant of whether you will see a solid profit from your investment.

Don't rely on the sale of your home to fund your retirement

Even though you own a home, you should do your best to save the maximum in your retirement savings accounts every year. Although it may seem hard to believe for anyone who has observed the fortunes some people made during the housing bubble, you won't necessarily make a killing when you sell your house. If you want to look at your home as a source of wealth in retirement, once you've paid off your mortgage, consider the money you were spending on monthly payments as a source of funding for your living and medical expenses in retirement. Also, retirees often want to stay put (despite all the articles you see about downsizing or retiring in exotic locales).

The Bottom Line

This overview should help put you on the path to filling in any gaps in your home-buying knowledge. Remember that the more you educate yourself about the process beforehand, the less stressful it will be, and the more likely you will be to get the house you want for a price you can afford. When it's done, you'll have the confidence that comes from successfully negotiating a major step in your life.