Financial Empowerment Curriculum

Moving Ahead Through Financial Management

Module Four:

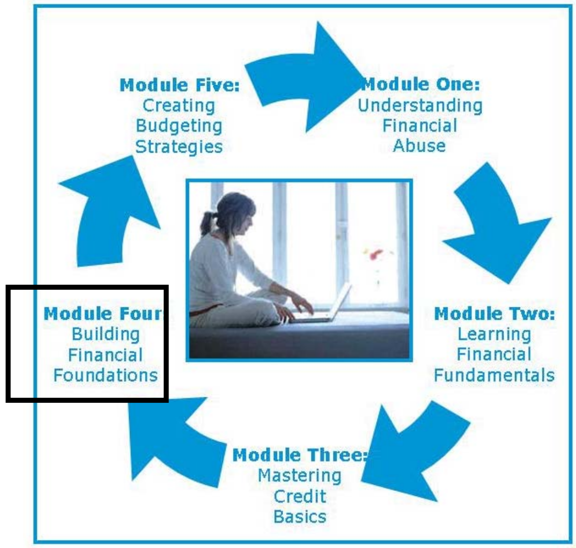
Building Financial Foundations

Homes, Loans and Automobiles

Allstate Foundation

NNEDV

MODULE FOUR:
Building Financial Foundations



Now that you have learned the basics of finance management in Modules One and Two, as well as credit report information in Module Three, this module reviews advanced finance management principles and topics.

Please note that the information in this curriculum is intended to be general advice for individuals involved in an abusive relationship. However, not everyone's situation is the same. So, if you need specific advice regarding your particular situation, you should contact a domestic violence advocate, financial adviser or attorney.

The objectives of this module are:

- ❒ Recall the various home options to consider when seeking financial living independence.
- ❒ Describe the difference between various loan options.
- ❒ Apply for a loan and recall how to prepare for the application process.
- ❒ Describe the path to achieve home ownership.

Key topics covered in this module include:

- Home Options
- Loan Options
- Loan Application Process
- Home Ownership

National Domestic Violence Hotline: 1-800-799-SAFE (7233)

Story of Survival

Joelle loves her job. She works 20 hours a week for an organization that advocates for, and provides support to, families in low-income communities. In 1999, she was convicted of a drug felony, incarcerated and went through a drug treatment program. Following her release, she became pregnant and had a child. However, the father was abusive and the relationship did not last.

Joelle must now earn a living and pay for childcare. Because of her felony conviction, she is ineligible for welfare, subsidized childcare, training or education funding, or HUD or Section 8 housing. She supplements her income by selling jewelry and she has moved in with her cousin to hold her expenses down; although the father of her child was beginning to harass her at the cousin's home.

Joelle's story is one of many domestic violence survivors, but there is hope and there are people, programs and organizations willing and ready to help Joelle.

In 2005, Joelle decided to contact the National Network to End Domestic Violence and ask for help. By working with her local advocate, she was able to secure another side job independently and allowed her to work from home. She also worked with her advocate on innovative ways to save money and remain in hiding from her abusive partner.

Today, Joelle is living in a one-bedroom apartment near the organization she works for and continues to be a strong and proud mother to her child. Although her place is small and she is still on a very restrictive budget, she is no longer sought after by her abusive partner and she is happy.

Read this module to learn how more about finance management.

Home Options

Transitional Housing

Transitional housing programs can be an option for someone who is leaving an emergency shelter or is not yet in a position to afford living completely independently. In addition to affordable housing, many of these programs also provide supportive services to help residents build skills in money management or offer savings programs. These programs allow you to develop the skills you need to obtain permanent housing. Some transitional housing programs offer rent-subsidies, allowing participants to find and keep their own housing while the program assists them for a set period of time with rent. Other programs allow participants live in apartment-style quarters owned or managed by the program and some are group settings or congregate living where several individuals or families share a household.

Many times, transitional housing units are dedicated specifically for victims of domestic violence and their families. Services that may be available include childcare; advocacy and counseling or emotional support; and job training and/or placement. Most programs offer assistance for up to two years. To learn more about transitional housing programs, contact your local domestic violence program. Public, private and transitional housing options may be available in your community.

Rental Properties

Before you look for an apartment, room or house to rent, determine how much you can afford to pay each month. Housing experts generally recommend that you limit your rent to 25 to 30 percent of your income. Example, if your gross monthly income is $1,600, you should look for something that costs no more that $400-$480 a month.

Also, determine the size of home you need and whether you need to live near your work, family, bus line, store, bank, etc.

If Planning to Rent:

- ❒ Define your needs. Do you prefer to rent an apartment, town home, or mobile home? What size rental do you need (studio, one bedroom, two bedrooms or more)? Keep in mind that additional fees such as utilities or lawn maintenance fees vary from landlord to landlord. Be sure to inquire about any additional fees that you may be expected to pay.
- ❒ Pay outstanding utility bills. Make sure all utility bills in your name are current. Not doing so may impact your ability to secure new housing.
- ❒ Look for a rental. There are several ways to find rentals, word of mouth, newspaper, online, or by driving through areas where you'd like to live.
- ❒ If utilities are not included, ask the landlord to provide you with a copy of the average costs for the utilities over the past year. This will give you an indication of the additional costs prior to locking yourself into a lease.

Home Options (cont'd)

❒ Submit your application. In most cases, you will need to complete an application. Typical applications include questions about your rental history, employment, and financial and personal information. Be prepared to provide the name and contact information for previous landlords. If your rental history was damaged due to domestic violence, talk through the pros and cons of disclosing this with your advocate.

❒ Move in. Once your application is approved and you accept the landlord's terms, sign the lease (after reading it carefully) and move in.

Lease Bifurcation

If you are on a lease or rental agreement with your current or former partner, you may be able to remove your name or have your partner's name removed from the lease. This process is called lease bifurcation. Laws vary by state, so ask an attorney or a domestic violence advocate about the relevant bifurcation laws in your state.

Many lease bifurcation laws require landlords to allow one party to be released or removed from a jointly held lease if there is good cause, such as domestic violence. This process may allow you to remove your name so that you can leave the unit without further obligation or have your partner or former partners name removed, so that he has no legal rights or responsibilities for the property. Once a name is removed from the lease, that person has no responsibility to pay rent, utilities or other expenses and no right to be on the property.

Section 8 Federal Housing

The Section 8 program makes privately owned rental housing affordable to low-income households. It provides rent subsidies (either rental certificates or vouchers) for eligible tenants. These subsidies usually equal the difference between 30 percent of the household's adjusted income and the Department of Housing and Urban Development (HUD) approved market rent (for certificates) or the Public Housing Authority-approved payment standard (for vouchers). Example, if your rent is $600 and you can only pay $480, a Section 8 voucher can cover the remaining $120. Availability of Section 8 and federal housing varies by state and often has a long waiting list.

Although many property owners rent or lease units to individuals with Section 8 vouchers, some do not. If you believe you are a victim of housing discrimination, contact a domestic violence program advocate, legal services or the public housing authority to file a complaint.

Home Options (cont'd)

Addressing Property Damage

If your abusive partner damages the property and your name is on the lease, you may be held responsible for the damage.

- ❒ If your abusive partner has damaged your property, you may be able to obtain financial assistance to make repairs through your state's Crime Victims Compensation Fund.
- ❒ Crime victim compensations programs provide funding to cover out-of-pocket expenses resulting from a crime.
- ❒ For more information about your Crime Victims Compensation Fund, contact a local domestic violence program (or visit http://www.nacvcb.org/).
- ❒ You may need to provide a police report or cooperate with law enforcement to access this fund.
- ❒ However, if you live in public housing, be mindful when calling law enforcement as some public housing units may evict their residents if police are called to their unit.
- ❒ If you have renter's insurance, your policy may cover the costs of damage to the property.
- ❒ You may need to file a police report for your insurance company to repair the damage.
- ❒ Consult your policy agreement for more information or call your insurance company to discuss your options.
- ❒ You may be able to get financial assistance from a local domestic violence program. Some programs have direct-assistance funds for making minor repairs to your home (e.g. changing locks, repairing a door or window).
- ❒ For more information about how direct assistance funds are used in your community, contact your local domestic violence program.

At the end of your tenancy (after an inventory check and condition inspection with no damage or missing items), you should receive your deposit money within 30 days.

Keep in mind, however, that you must pay the last month's rent before you receive your deposit.

Home Options (cont'd)

The following is a sample of the first page of a lease agreement to provide you an idea of what this legally binding contract looks like. Lease agreements can vary in length depending on how many clauses and riders are attached to the basic agreement. If you have any questions about the document, contact a housing organization in your community or an attorney. They can answer your questions and help explain the document to you.

If the landlord agrees to something verbally, but it does not appear in writing on the lease agreement, do not sign it without adding or changing the conditions.

LEASE AGREEMENT

THIS LEASE AGREEMENT (hereinafter referred to as the "Agreement") made and entered into this ________________ day of ____________, ____________________, by and between ____, whose address is ___________________________________ (hereinafter referred to as "Lessor") and ______________________________________ (hereinafter referred to as "Lessee").

WITNESSETH:

WHEREAS, Lessor is the fee owner of certain real property being, lying and situate in ________________ County, ______________, such real property having a street address of ____.

WHEREAS, Lessor is desirous of leasing the Premises to Lessee upon the terms and conditions as contained herein; and

WHEREAS, Lessee is desirous of leasing the Premises from Lessor on the terms and conditions as contained herein;

NOW, THEREFORE, for and in consideration of the sum of TEN DOLLARS ($10.00), the covenants and obligations contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto hereby agree as follows:

1. TERM. Lessor leases to Lessee and Lessee leases from Lessor the above described Premises together with any and all appurtenances thereto, for a term of ________________ year(s), such term beginning on __________________, and ending at 12 o'clock midnight on

Home Options (cont'd)

General Rights of Tenants

Livable rental units must provide:

- Accommodations that are weather and waterproof
- Plumbing in good working order
- Enough hot and cold running water
- A heating system in good working order
- An electrical system in good working order
- Accommodations that are free from infestations of insects and rodents
- Sufficient trash cans
- Floors, stairways and railings in good repair
- Natural lighting in every room
- Working windows that open at least halfway or mechanical ventilation
- Fire or emergency exits that lead to street or hallway
- A working deadbolt lock on the main entrance
- Working security devices on windows
- Working smoke detectors

Tenants have a right to **written 24-hour advance notice** of the owner's intent to enter the property, except in case of an emergency. When a tenant has provided a written **request for repairs** to the landlord, the tenant has the right to a prompt response.

Tenants must receive 30 days written notice of a **rent increase** under 10 percent and 60 days written notice of a rent increase of more than10 percent.

Tenants must receive the **return of their security deposit** within 21 days of vacating a unit. They have a right to an itemized statement of any money withheld by the landlord.

General Tenant Responsibilities

Tenants must:

- Pay the rent on time
- Keep the unit clean and sanitary
- Use gas, electrical and plumbing fixtures properly
- Fix or pay for repairs of items they or their guests damage
- Not remove anything from the structures or buildings that they have not put there and must not allow anyone else to do so
- Use the premises and the rooms for their intended purpose
- Not engage in illegal activities on the premises
- Limit household tenants to the number allowable by law

Home Options (cont'd)

Before Signing a Lease

- Do not put money down unless you're sure you want the apartment. Although you may be legally entitled to have your deposit returned, it may be difficult to recover.
- Calculate the anticipated costs of utilities (e.g. heat, water, electricity) when determining whether you can afford an apartment.
- Check the apartment to ensure that it's in acceptable condition. Put all agreements for repairs in writing.
- Evaluate how the superintendent or owner responds to "after hours" emergencies.
- Talk with prospective neighbors about the competency and reputation of the landlord and/or management company.
- Visit the property at night and/or during the weekend to see what the community is like.

How to Handle Evictions

There are three types of eviction notices.

Notice from Landlord: The landlord is required to give notice before he or she files a lawsuit against you. The notice may state "Pay the rent or vacate in three days." If you fail to do either during the designated time, the landlord may file an eviction lawsuit in court.

> **How to handle this notice**: Comply with this notice by paying the overdue rent. If you do not have enough money to pay the rent, contact a local domestic violence program or other community organization to learn about possible grants or loans.

NEVER PAY RENT IN CASH OR WITHOUT RECEIVING A RECEIPT

Notice from Court: This summons notifies you that the landlord has filed an eviction lawsuit against you. You can defend yourself in court if you act quickly.

> **How to handle this notice**: Talk to a lawyer as soon as possible. The time limit for responding to a summons may be as little as three days, and your lawyer will need time to prepare. If you do not have a lawyer, contact a nonprofit organization like Legal Aid (www.legal-aid.org).

Notice from Sherriff: The landlord can get an order to vacate after he or she sues you. The order will indicate when you must vacate.

> **How to handle this notice:** Comply with this notice and move your family and your belongings as soon as possible. If you leave any items behind, you may have to pay storage fees to get them back. If you did not receive a summons before you received the order to vacate, see a lawyer immediately. The lawyer may be able to get the order set aside on grounds that you did not have a chance to defend yourself.

Home Options (cont'd)

Illegal Evictions

Illegal eviction takes place when you are forced to leave your home by someone who does not have a legal right to evict you. Your landlord has the legal right to exclude you from your home only in certain circumstances. Some tenants can be evicted more easily than others, including women who share living accommodations with their landlord.

You may be illegally evicted if your landlord:

- ❒ Changes the locks while you're out or stops you from getting into your home;
- ❒ Makes life so uncomfortable for you that you're forced to leave your home; or
- ❒ Physically removes you from the property or has anyone who is not a bailiff employed by the county court remove you.

Illegal eviction is a serious civil and criminal offense. The courts may force your landlord to allow you back into your home, impose fines and in extreme cases, award compensation.

If your landlord has illegally evicted you or is attempting to evict you, inform him or her in writing that this action is illegal. Some landlords are unaware of the law and may not realize they're acting illegally. Ask your landlord to:

- ❒ Allow you back into the property;
- ❒ Stop trying to evict you illegally;
- ❒ Stop harassing you; and
- ❒ Return your belongings.

Get help from a nonprofit organization like Legal Aid and keep copies of any letters you send to (or receive from) your landlord.

The police are not required to get involved in cases of illegal eviction unless the eviction is violent. However, it's wise to contact them immediately if you're illegally evicted so there is a record you can use later, if necessary.

If you have been evicted, you will need to find another place to live. Contact your local domestic violence program to learn about housing resources in your community or call the National Domestic Violence Hotline 1-800-799-7233.

Loan Options

As you begin to rebuild your financial foundation, you may want to look at obtaining a loan to meet your financial goals. Taking on debt isn't always bad and can actually be very helpful in building a positive credit score. The key is to not to take on more debt that you can manage. Knowing about different kinds of loans will help you make better decisions. After all, knowledge is power and the most important piece of knowledge to share is this: avoid taking out any loan unless you have a solid plan for repayment. Also, be aware that if you are attempting to keep your location or actions confidential, taking out ANY loan, including credit cards, may make you vulnerable and are traceable via your credit report.

There are essentially two types of loans: unsecured and secured.

Unsecured Loan

An unsecured loan is a loan obtained without collateral (property or goods used as security against a loan and forfeited if the loan is not repaid). This loan is also called a signature loan. There are three main types of unsecured loans: I.O.U. Loan, Credit Card Loan and Personal Loan.

Unsecured Loan: I.O.U. Loan

The simplest unsecured loan is a personal loan from a friend or family member, with an I.O.U. as signature of agreement to pay back the loan. This type of loan may be a good option but before taking a loan from family or friends consider the following: what might happen if you are unable to repay the loan, how might this damage the relationship, and what if the family member or friend changes their mind and wants to be paid back earlier? If you decide that this is a good option, consider putting the agreement on paper, spelling out all of the terms of the loan, interest to be paid and when payments are due. Having the agreement clearly stated in writing can avoid problems in the future. Below is example of an I.O.U loan.

Step 1	Include the date, month and year the agreement is made.
Step 2	Include the full name of the person lending the money and their address.
Step 3	Include the full name of the person receiving and borrowing the money and the person's address.
Step 4	Include the amount of the loan.
Step 5	Include the number of months or years the loan is for.
Step 6	Include the amount of each scheduled payment.
Step 7	Include the interest charged on the loan, if applicable.
Step 8	Both the borrower and lender need to sign and retain an original copy the IOU loan agreement.

Loan Options (cont'd)

PayDay Loans

Many consider payday loans predatory lending. Typically, these short-term loans are offered to individuals without regard to credit. Though these loans are relatively easy to obtain, they are granted at unreasonably high interest rates. In fact, an individual who borrows from a payday loan company may pay more than 100 percent interest over the life of the entire loan.

With interest rates so high, many payday loan borrowers find repaying their loans very difficult and in a far worse situation then when they originally applied for the loan.

Unsecured Loan: Credit Card Loan

Another common type of unsecured loan is a purchase made on a credit card. Each time you make a credit card purchase, you sign a form which authorizes the payment and agree to pay the money borrowed. The term and amount of the loan are predetermined when you first applied for and receive the credit card.

With this type of loan, the money is not loaned on the basis of collateral, such as home or property ownership. The credit card company merely has the borrower's agreement to pay any funds borrowed. However, if the loan is not paid in appropriate time, additional fees may be assessed, the account may be sent to collections, and legal proceedings can be taken against the borrower.

Below is an example of using a credit card to take advantage of a lucrative purchasing opportunity.

Domestic Violence Survivor Example

Gwen has just moved into a new house and has little furniture. After some shopping around she is able to find a sofa for $750. The furniture store offers zero percent interest on all purchases over $500 for a period of six months. After the six month period, any remaining balance is subject to 25 percent interest.

Monthly Payment to Pay Off in Six Months:
$750 (total cost of sofa) / six months = $125 per month

Monthly Payment by Paying Minimum Due:
Minimum Monthly Payment = $50
Balance after Six Months = $450
Balance of $450 at 25 percent = $112 per month (until loan is paid in full)

In Gwen's scenario above, her $750 sofa has the potential of costing over $1200 if she only makes minimum payments.

Loan Options (cont'd)

Unsecured Loan: Credit Card Loan (cont'd)

As mentioned previously, the key to any loan (especially credit cards) is to only utilize it if you have the ability to repay.

With that said, credit cards can be a good option for short-term needs and for establishing credit. However, discipline is the key to using credit cards. Before putting something on a credit card, consider the interest rate, the monthly payment and how long it will take you to pay off the loan.

Unsecured Loan: Personal Loan

Also, banks can offer an unsecured loan to a borrower. Usually banks will assess the creditworthiness of the borrower before handing over cash without collateral. Those who have lower credit scores tend to have less chance obtaining an unsecured loan, and if they can get one, they may be assessed high interest rates, since the lender is taking more of a risk.

Usually, an unsecured loan is for a small amount, perhaps for a one-time medical fee or short-term needs. When your credit is good, shopping around for the best interest rate for an unsecured loan is a good idea. Frequently, the best rates for an unsecured loan are offered through credit unions. If you have an existing account with the credit union, obtaining an unsecured loan should not be a problem.

Secured Loan

Secured loans are those loans that are protected by an asset or collateral of some sort (such as a car or house). From a lender's point of view, these types of loans are less of a risk because the lender can recover their loss from the asset used for the loan.

Benefits of Secured Loans

- Best way to obtain large amounts of money.
- Since there is less risk for the lender, the rates tend to be lower.

Drawbacks of Secured Loans

- If the loan is not repaid, the lender may take possession of the asset.
- Since the loan amount is generally higher, the application process may take longer.

There are three main types of secured loans: Debt Consolidation Loan, Car Loan and Home Loan.

Loan Options (cont'd)

Secured Loan: Debt Consolidation Loan

One type of secured loans is a debt consolidation loan where a home or personal property is used as collateral. Instead of having many high interest credit card payments to make each month, money is loaned to pay the original lenders off, and the borrower then only has to repay the one loan. This is not only more convenient, but it will also save a lot of money over time, since interest rates for secured loans are lower. A debt consolidation loan usually offers a lower monthly payment as well.

Secured Loan: Car Loan

A car loan is a very popular type of secured loan (the loan is secured with the value of the vehicle). The primary difference between loans for new and used cars is that new car loans tend to come at a lower interest rate. This is because the car itself has more value and if they need to repossess the car; they are more likely to get its full value at resale. On the other hand, because it is a new car, the loan itself will likely be larger, increasing your overall monthly payment as well. This may be an important factor for people with poor credit, as the higher interest rate could make a used car substantially more expensive. For people with good credit, the difference in interest rate may not make a huge impact. In either case, you should be very careful when shopping for a car loan to ensure that they get the best loan to meet your needs.

New car loans tend to be large, because new cars are more expensive than used cars, but the interest rate tends to be lower than that for a used car. You can also obtain things like cash rebates or no money down financing with new car loans. Taking out a loan will add to the cost of the car over time, because people will be paying interest in addition to the principal balance, but for people who cannot afford cash for a new car, new car loans can be an option.

Used car loans are generally smaller, because of the reduced value of the car, but they carry some extra risk which is why they tend to have a higher interest rate. The lender's concern is that the value of the car may go below the value of the loan before the loan is fully paid, and if a borrower defaults, the lender may have trouble recovering the full amount of the loan. Hence, a high interest rate is charged to make the loan less dangerous for the lender.

Before shopping for used cars or loans, it is a good idea to sit down and determine what kind of car payment you can afford. Drivers should remember that in addition to monthly payments, the car will also need to be insured, and the car will require gas and periodic repairs and maintenance.

Loan Options (cont'd)

Secured Loan: Car Loan (cont'd)

All of these costs can add up, and it is important to provide for them in a monthly budget to avoid surprises or a loan which is too big to carry comfortably. While putting together a loan, it can help to use a car loan calculator (such as, www.edmonds.com) to get a rough idea of how things like the amount of a loan, the length of a loan, and the interest rate can change monthly payments and the total cost of the loan over time. As a general rule, loans with short-terms are better (36 vs. 60 months), because borrowers pay less interest, and the lower the interest rate, the less costly the car financing.

Before buying any car, call an insurance agent to get a quote on coverage to ensure you will be able to cover all costs associated with owning the car.

Car Financing Through a Car Dealer

If considering financing a car through the dealer, make sure you understand all of the costs. Some car dealers may have working relationships with local lenders to make the financing process easier, but these relationships may involve payments to the dealers for routing loans to particular lenders. Be sure to ask the dealer to fully explain all of the costs involved to understand what you are paying for in the process. Consider finding a lender first then select a dealer to identify the particular car to buy.

Car Financing Online

It is also possible to find used car financing online, and through lenders which are not locally based, although the customer service may not be as good. To avoid a negative impact on their credit scores, borrowers should shop around without actively applying for any loans, and ask only one or two online lenders which appear to have good rates and terms for pre-approval on a used car loan. In a pre-approval, the lender will provide the borrower with paperwork indicating how much the lender will give out, and what the interest rate and terms of the loan would be.

Loan Options (cont'd)

Secured Loan: Car Loan (cont'd)

Car Financing With No Credit

While there may be good reasons to consider a no credit car loan, there can also be some dangers.

In some cases, a no credit car loan may seem like a good solution for those who have bad credit or no credit history.

Some of the drawbacks include:

- Typically only available on used cars.
- Many lenders that offer this type of loan do not report to the credit reporting agencies (which makes it difficult to rebuild your credit).
- The interest rate is typically higher due to the increased risk.
- If a payment is missed, the interest rate may increase and the lender can repossess the vehicle.

If you have bad credit, chances are good that you'll find at least some lenders who are willing to finance your automobile purchase. However, it's wise to be extra careful when shopping for car loans in this situation.

Some lenders prey on borrowers who have bad credit, as they may be compelled to take just about any offer because they feel desperate.

Loan Options (cont'd)

Secured Loan: Mortgage Loan

The most popular secured loan is a mortgage (home) loan. The terms of the mortgage loan are usually different from a standard bank loan, both in terms of structure and in duration. In most mortgage financing arrangements, the property that is purchased with the financing is used as collateral for the debt. There are four main types of mortgage loans: fixed-rate, adjustable rate, balloon, and sub-prime. Each loan is explained in further detail below.

Fixed-Rate Loan

The two most common loan terms (length of the loan) today are the 15-year and the 30-year mortgage. If a borrower selects a 15-year mortgage, she agrees to repay the amount borrowed and all interest within 180 monthly payments, or 15-years from the date of the loan. If a borrower selects a 30-year mortgage, she agrees to repay the amount borrowed and any and all interest within 360 monthly payments, or 30 years from the date of the loan. The loan also provides the same interest rate during the life of the loan. Selecting a loan term that is right for your specific needs is one of the most important decisions you can make when choosing a mortgage. So how do you choose between a 15- or 30-year mortgage? While there are many factors to consider, most borrowers make the choice based on the monthly payment that is most comfortable. The longer the repayment term of the loan, the less the monthly payment will be. The drawback to this is that over the life of the loan, the borrower will pay more in interest with a longer term than with a shorter term.

Adjustable Rate Mortgages (ARMs) Loan

An adjustable rate mortgage, also known as ARM or floating rate mortgage, is a type of mortgage with a flexible interest rate. This means the interest rate fluctuates depending on the index. There are basically five types of indexes used to calculate the interest rate on adjustable rate mortgage: Constant Maturity Treasury (CMT), the 11th District Cost of Funds Index (COFI), the 12-month Treasury Average Index (MTA), the National Average Contract Mortgage Rate, and the London Interbank Offered Rate (LIBOR). An adjustable rate mortgage is not necessarily a bad arrangement, just a more risky one. In the case of the index falling, you may end up paying less than you would on a regular mortgage loan; however, when the index rises, you would end up paying more. An adjustable rate mortgage often comes with a cap or limitation on charges, which controls either the frequency or the lifetime change of the interest rate. For example, an adjustable rate mortgage can have a cap of a two percent maximum per year, or six percent total during the lifetime of the mortgage. This protects you while still ensuring the lender a fairly safe transaction.

Loan Options (cont'd)

Balloon Loan

A balloon loan is a type of short-term mortgage. Balloon loans have set loan terms, just like other types of mortgages. As discussed previously, typical fixed rate loans last for 15 or 30 years and once you make your final monthly installment payment, you are given the deed to the property and cleared of the mortgage debt. However, balloon loans often extend for about five to seven years. Although the balance of the loan is due at the end of the term; the debt is not cleared with a final installment payment. Some people view the balloon loan as a poor choice because the borrower must be disciplined enough to plan for a large-sum payment at maturity (or be prepared to refinance their loan or move from the property). While the disadvantage of having to come up with a large sum of money at the end of a rather short loan term is obvious, there are advantages to securing a balloon loan. One major advantage is that balloon loans often carry low interest payments, allowing the borrower to hold onto more cash over the loan term. The borrower can use the cash as she sees fit, perhaps even investing it in the hopes of earning more than what is required to repay the loan. This loan type is also good if you know you are only going to live in the home for less than the specified loan term (again, which is typically five or seven years).

Sub-Prime Loan

If you cannot qualify for a mortgage loan or you are having difficulty obtaining credit through the normal channel, then a sub-prime loan may be your next option. Although given the current market this area of lending is volatile, it is still available through certain lenders. A sub-prime loan is a loan that is typically given to people with a bad credit record. The interest rate on a sub-prime loan is likely to be higher than an interest rate you would expect on a loan from a bank. Many people will use a sub-prime loan when they cannot get credit to help repair their credit rating. Lenders of this type of loan usually finance the loan through a third party, so the lending rules are slightly more flexible. This type of loan is good for repairing credit records but you may not wish to repay the loan over a long period. You might take out a loan over five years and then circumstances may change and you can pay it back sooner. If you think this may be the case, ask about the lenders early repayment terms. With that said, you want to be mindful when investigating this type of loan as it is often considered high-risk. Also, be sure to read the section on Predatory Lending which is explained later in this module, as this type of lending is often found in the sub-prime market.

Loan Options (cont'd)

Now that you are more familiar with the different types of mortgages, below is a comparison chart to help you determine which loan is best for you.

HOME LOAN COMPARISON CHART

Loan Type	Loan Features	Perfect if You:
Fixed-Rate Loan (e.g., 30, 20, 15, or 10 years)	• Fixed interest rate and monthly payment over the entire term of the loan • Higher interest rate and monthly payment than adjustable rate loans	• Don't plan to sell or refinance for 10 years or more • Prefer the security of having the same monthly payment with no pressure to refinance later
ARM Loan (e.g., 1, 3, 5, 7, or 10 years)	• Lower starting interest rate and monthly payment than fixed-rate loans • May eventually go higher than a fixed-rate loan	• Want the lowest possible interest rate and monthly payment • Are comfortable with changing interest rates and monthly payments
Balloon Loan (e.g., 5 or 7 years)	• Lower starting interest rate and monthly payment than fixed-rate loans • Full balance of loan is due at end of term (five to seven years)	• Plan to only live in your home for a short time but want a stable interest rate
Sub-Prime Loans (e.g., 2, 3, 15, or 30 years)	• May contain a prepayment penalty	• Want a home, but don't qualify for the lowest rate and best terms and can afford paying more for the loan

Regardless of which type of loan you apply for, make sure you research home mortgages carefully. Some websites (such as, www.mortgageloan.com) will compare mortgages for you, but consider working with a loan consultant (loan representative from a bank) before applying for a mortgage online. The loan consultant can discuss your options and any problems that might affect your eligibility for an online mortgage.

While there are many factors to consider, most borrowers make the choice based on the monthly payment that is most comfortable. The longer the repayment term of the loan, the less the monthly payment will be. The drawback to this is that over the life of the loan, the borrower will pay more in interest with a longer term than with a shorter term.

Loan Options (cont'd)

Mortgage Features

In addition to the various loan types available, the following features can be applicable to any loan type. The two most common are reviewed below.

Prepayment Penalties

A prepayment penalty is a monetary penalty should a borrower payoff a loan earlier than was originally agreed. Banks enforce a prepayment penalty to guarantee they make a certain amount of money from loaning money to a borrower. Many lending institutions attach a prepayment penalty to a loan because loan refinancing has become relatively commonplace. If a consumer takes out a loan, pays on it for a period of time, and then refinances at a lower interest rate, she saves money. The lending institution that provided the original loan, however, loses out on the money that would have been earned from interest payments.

The specifics of a pre-payment penalty vary from one lender to another. One type of pre-payment penalty is referred to as a soft prepay. This type of pre-payment penalty is waived if the source of the original loan, such as a home, is sold. In this case, the penalty is only enforced if the loan is refinanced. This type of pre-payment penalty is considered to be an incentive for customers who do not plan on refinancing, while still protecting the original lending institution.

Negative Amortization

Negative Amortization (Neg Am) may be helpful to first time buyers who can't afford huge upfront mortgage payments. With Neg Am, initial payments do not even cover the full cost of interest accrued on the loan. The remaining unpaid interest is added to the money owed on the house, so the loan increases in size (instead of decreasing).

While this may be attractive to buyers at first, Neg Am loans only allow below interest rate payments for a short period of time, and eventually, payments must increase to cover the full cost of interest, which is now higher than it would have been in the onset since the total amount owed is higher. Interest on Neg Am loans is almost always given at an adjustable rate. Payments on this type of loan don't necessarily go up dramatically. Some Neg Am loans are graduated, meaning over time, your payments will gradually increase until you are paying at least the interest, and often some of the principal too.

Loan Options (cont'd)

Now that you know all about the different types of loans available (both unsecured and secured), below is some final information to further educate you about the loan financing industry. While most lenders are respectable, there are some lenders that are not (including mortgage lenders) and they may charge excessively high interest rates and unreasonable terms.

Predatory Lending

Predatory lending is the practice of using unfair, deceptive and abusive tactics in lending money. Dishonest lenders take advantage of borrowers who are less knowledgeable about lending practices, getting them to agree to loan terms that are not only less than desirable, but also financially damaging.

Predatory lenders also target borrowers who are so desperate to obtain loans that they will agree to nearly anything. Often, people with poor credit are primary targets for lenders who engage in predatory lending practices. Individuals with low incomes are often targets, as well as women, senior citizens and minorities. However, individuals from all backgrounds, income levels and walks of life can be victims of predatory lending.

Predatory Lending and Mortgage Lending

Predatory lending is not limited to short-term lending. It is all too common among dishonest mortgage lenders. These mortgage lenders offer loans at very high interest rates, requiring borrowers to agree to terms that are unfair and damaging.

For example, a predatory lender may include unfair pre-payment penalties or balloon payments in a loan agreement. Often these terms are hidden within very technical language, making it difficult for the borrower to fully understand what she is agreeing to.

To avoid falling victim to predatory lending, avoid lenders that advertise guaranteed loan approval. Also, be wary of loans advertised through telemarketers or traveling salespeople. Thoroughly research the lending company you are considering to learn if it has been accused of predatory lending.

Also, read all loan agreements carefully before you sign and make sure there are no blank spaces on your loan document. Consider consulting with a lawyer before you sign any loan documents, especially mortgage loans.

Loan Application Process

Why do some people get loans approved without any problem, while others struggle through the process? What do lenders look at when they evaluate you?

Getting your loan approved depends on how your financial background matches the lender's criteria. Although the criteria may change from lender to lender, the following guidelines are often used to evaluate loan applications.

- **Employment History:** Depending on the type of loan, most lenders look for one to two consecutive years of employment within the same industry. This shows employment stability and that you do not hop from one job to another. Employment history helps lenders evaluate your ability to generate income and repay a loan.

- **Credit History:** You must demonstrate that you can manage credit responsibly. Lenders look for a history of on-time payments. Too much debt on credit cards, or maxed-out credit lines, indicates that you may be unable to pay or manage your debt. Pay down any short-term debt at least six months before applying for a new loan. A good rule is that you should not owe more than 30 percent of the card limit (e.g. if your limit is $1,000 you should not owe a balance over $300).

- **Outstanding Liabilities:** How big a loan can you comfortably repay? The size of your income dictates the amount of liability you can support. Your total monthly payments for debts (including credit card debt, car loans, student loans, existing mortgages or child support) should not exceed 42 percent of your monthly earnings.

- **Cash and Asset Reserves:** Lenders may request information about your cash available (checking and savings). This is particularly important if you apply for a mortgage loan, as lenders may require that cash and liquid assets be available to pay at least two monthly mortgage payments.

Loan Application Process (cont'd)

Before visiting a lending institution, you should take advantage of numerous online mortgage calculators. These mortgage calculators also make it possible to determine how much you can afford in a mortgage loan, as well as how much monthly payments will be for specific mortgage loan amounts. Although the information on these calculators is not as accurate as the information provided by a lender, it does provide you with ballpark figures.

Prequalification Process

Loan prequalification is a process that pre-approves a homebuyer for a specific loan amount when purchasing a home. A loan pre-qualification can aid a homebuyer in the purchase of a home because it gives the buyer a clearer picture of how much money can be spent toward the purchase of the home. It can also make your offer on a property more appealing to the seller if they know you are prequalified.

The loan prequalification process is a simple one. First, the loan officer asks the homebuyer several questions, some of which may require documented proof. For example, the loan officer will ask the homebuyer to provide proof of income and debt in order to determine a debt to income ratio.

In order to determine this ratio, the loan officer needs to know the homebuyer's outstanding debts, assets, credit, and employment status. After evaluating all of this information, the loan officer is able to provide the homebuyer with an estimate of how much money he or she can spend toward the purchase of a new home.

Loan Approval Process

As valuable as loan prequalification letters can be, they are not a guarantee of a loan.

The actual loan approval process is a long and sometimes tedious one, even if the homebuyer's income and credit history is impeccable.

After prequalification (and finding a home you'd like to purchase), the next step is to apply for a mortgage loan. A mortgage application is a type of loan application. When a person wants to buy real estate, he applies for a mortgage from lending institution.

The application asks a number of important questions about the applicant's identity, employment history, income, monthly expenses, and debts. It also asks for information about the house the person wants to buy and the amount he wants to borrow.

The physical application form is only one part of the mortgage application process. A big part of this process is checking the borrower's credit by ordering a credit report through a credit bureau.

Loan Application Process (cont'd)

Checking Your Credit Report

The purpose of this check is to find out whether or not the borrower has a history of paying his bills on time. No matter how good an applicant looks on a loan application, she stands to be rejected if her credit history is poor. There are some mortgage lenders that grant loans to people with imperfect credit, but the terms of such loans may be less optimal than those offered to borrowers with good credit.

Before submitting a mortgage application, many home loan experts recommend that borrowers check their credit files for inaccuracies. If the wrong information is listed, a borrower can contact the credit bureau to learn the process for having it changed.

To have the best chance of securing a home mortgage loan, provide accurate information.

Checking Other Documentation

Besides the credit check, another important part of a mortgage application is the documentation a borrower provides. A bank or mortgage company is unlikely to take a borrower's word for her income, expenses, and employment. The borrower may need to provide tax returns, bank records, and proof of income. These types of documents may be required not only of the primary borrower, but also of anyone else whose name is included as a co-borrower or co-signer on the mortgage application.

Sometimes a mortgage lender will reject an application. Some of the reasons an application may be rejected include a low down-payment, poor credit history, and insufficient income to cover the amount of mortgage the borrower is seeking.

Home Ownership

For many people, the process of acquiring a home requires obtaining a mortgage. One of the best places to begin your quest for mortgage advice is to talk with your banker. Banks make a wide range of loans, and many of them have a great deal of expertise when it comes to helping you evaluate your circumstances and identify mortgage packages that are right for you. Your banker can help you understand how the mortgage works, what type of commitments you are making, and how a particular type of mortgage would provide the most benefit in your case.

Along with bankers, consulting a mortgage broker is also a great way to acquire current and reliable mortgage advice. Brokers of this type are sometimes connected with loan agencies or other types of financial institutions. However, a mortgage broker may also be involved in the buying and selling of mortgages. The depth of knowledge that the broker must have in order to conduct business on this level includes a firm grasp on what types of mortgages are likely to be the most stable over the next several years. That is something you need to know if you want to purchase a home in the near future.

Real estate professionals also tend to have a working knowledge of mortgages and can be a great source of mortgage advice. Realtors have a vested interest in helping clients get financing from the right lender, as it means they earn a sale and the resulting commission. In order to help people obtain financing, a realtor is often able to assess the financial condition of a potential buyer and create a match with the right type of lender.

All these financial professionals can provide you with mortgage advice that has to do with just about every aspect of the process. They can help you better understand the difference between a fixed rate and variable rate mortgage, obtaining a mortgage from a loan company instead of a bank, what type of references you must normally supply as part of the application process, and even advice on calculating what type of monthly mortgage payment you can reasonably manage. Seeking solid mortgage advice before purchasing a home can help you avoid mistakes that could prove to be costly in the long run.

Owning a home is a dream for many. To make this dream a reality, ask tough questions, set goals and plan carefully. The more you know about owning a home, the more likely you are to fulfill your goal.

Home Ownership (cont'd)

Ask yourself these questions:

- ❒ Do you have a steady income and a stable job?
- ❒ Do you plan to stay in the same city or state for at least three to five years?
- ❒ Do you have a budget? Do you stick to it?
- ❒ Do you have a good credit or non-traditional credit history (including payments to landlords, utilities, cable, insurance, etc.)?
- ❒ Do you have savings for a down payment and closing costs? Have you researched programs that offer down payments and closing costs for survivors of domestic violence?
- ❒ Have you tried to pre-qualify for a home mortgage?
- ❒ Can you pay off most of your current debt before you buy a home?
- ❒ Have you looked at low- and moderate-income mortgage programs?
- ❒ Have you taken homebuyer education classes?

Can you afford to buy a home? Most lenders require a down payment, usually three to 20 percent of the home mortgage. A three to five percent down payment is standard for many first-time homebuyer programs.

Most people can comfortably repay a mortgage that is 2.5 times their total annual income (before deductions). If you make $30,000 a year, you can qualify for a $75,000 mortgage. You still must have the down payment, closing and inspection costs, and a good credit rating.

Although you may qualify for a large mortgage with some lenders, you may be unable to meet the monthly payments, and you could lose your home. Review your finances and estimated monthly expenses carefully. Do not take on a mortgage unless you can comfortably make the monthly payments.

Closing Costs

Closing or settlement costs are fees you pay when you finalize the details of your home mortgage with a financial institution.

Closing costs include a title search, which will prove that no one else owns or has a lien on the property. Once this is proven, you must purchase title insurance. You may also have to pay for a land survey, termite inspection and homeowner's insurance. Ask your banker to explain the closing costs before you sign any papers. Watch for hidden fees and be sure to comparison shop.

Home Ownership (cont'd)

Owning a home is a good way to build wealth and protect your family's future. It offers security and stability. The equity in your home can help pay education expenses, finance a small business, buy a car or take care of unexpected emergencies like illness or unemployment.

However, as you learned earlier, some lenders will loan you money even if you do not have good credit. These lenders, called predatory lenders, offer loans with high interest rates, fees and repayment terms. If you can't afford to repay the loan, you may lose your home in foreclosure. Some tips:

- ❒ **Get help before you sign.** If you're concerned about becoming a victim of predatory lending, have a counselor or attorney review the loan documents before you sign them.
- ❒ **Read the fine print.** Watch for balloon payments, high interest rates and fees, and credit life insurance.
- ❒ **Shop around.** Comparison shop to get a loan with the best terms and fees. If you don't understand loan terms, ask a housing counselor to review the documents for you.
- ❒ **Avoid high-pressure sales.** Ignore high-pressure sales tactics and be leery of advertising that promises "No credit? No problem!"
- ❒ **Review total costs.** A low monthly payment isn't always a deal. Look at the total cost of the loan.
- ❒ **Watch what you sign.** Never sign a blank document or any document the lender promises to fill in later.

In general, the best advice we could share is to read and gain knowledge in regard to your finances, especially when it comes to the important decisions in your life, such as loans and your housing arrangements.

Although this module provides a great start, it does not address every topic available regarding financial management. As mentioned previously, contact your local domestic violence program to learn about these topics or call the National Domestic Violence Hotline 1-800-799-7233.