Wise Advice from The Loan Goddess

"Low Down" Loans

Whenever your down payment is less than 20% of the purchase price, you, the borrower, must compensate the lender for their additional risk. Given that unpleasant reality, there are several methods now available in an ever changing mortgage market for you to choose from.

Mortgage Insurance ("MI" or "PMI")

The most important thing to remember about MI is that it is NOT tax deductible. The insurance is designed to provide extra protection for the **lender** if a borrower defaults on a mortgage loan, which already is secured by a Trust Deed or lien on the property. PMI is an actual company name, but they are not the only company offering mortgage insurance, MGIC and GE are two others. MI is not related to credit life insurance, which pays off a mortgage on behalf of a homeowner's family in the event of the homeowner's death. Paying mortgage insurance is the traditional method, and it allows borrowers to lock in comparatively low loan rates, but you must remember to consider the cost of monthly MI when you budget the actual housing payments. As the equity builds in your house (to over 20%), you can ask to have the MI removed after at least two years have passed.

Lender Paid MI or TAMI "Tax Advantaged Mortgage Insurance"

Another way to pay for the MI is to have it included in your interest rate. Although this results in a higher note rate, you are only making one payment, and of course the interest portion of every payment is tax deductible. The negative aspect is that you cannot eliminate the "Lender Paid Mortgage Insurance add-on" without refinancing. For this illustration, let's use 6.25% as our Base Rate assumption, bearing in mind that mortgage rates fluctuate, and this is by no means a price quote.

5% Down = Base Rate Plus .875%	Total: 7.125%
10% Down = Base Rate Plus .625%	Total: 6.875%
15% Down = Base Rate Plus .375%	Total: 6.625%
20% Down = Base Rate	Total: 6.250%

Piggy Back Mortgage

This alternative to the unpopular MI, known as a "piggyback" loan, stacks a small second mortgage on top of a primary or first mortgage. These loans are most commonly designed with an 80% primary loan, 10% second loan and a 10% down payment, or "80-10-10s". But variations, such as 75%-20%-5%, are possible, and in fact Fannie Mae may limit the first mortgage to a 75% LTV. There are three types of second loans that you can piggyback, each of which carries different payment schedules. First type has a fixed rate and a fixed term – such as a 15 due in 15 or a 20 due in 20. The interest rate is higher than the primary mortgage's – typically between 7% and 10%, depending on the borrower's credit rating. The second type is a fixed-rate "balloon" mortgage. In this case, monthly payments are low because they are based upon a 30 year amortization period, but the balance must be paid off in full after a specified term, often 15 years. The third type is referred to as "HELOC" or Home Equity Line of Credit. This is a very flexible borrowing tool. Typically the first 10 years, known as the "draw period" require payments of interest only, and then you have 15 years to pay the entire principal back, a 25 year term in all. Interest is charged only on the amount you have "drawn", so if you pay it down, you can borrow back the money later. However, HELOC's could have a new rate for you every month – they are based upon the Prime Rate, plus a margin. That means your rate changes every time the Prime Rate is changed, and the lifetime cap is usually 18%.

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