10 Questions to Ask a Mortgage Lender

The thought of buying a home spurs hopes and dreams—and lots of questions. Many of the questions center around the scariest part of home buying: the mortgage.

You and your mortgage are going to be together for a long time, so the more you know about it at the outset, the better. Here are some questions to ask a lender before you apply for your mortgage. Some of these will help you choose a lender in the first place; others will help you gather information you should know before filling out a mortgage application.

1. What's the lender's history?

The first quandary for the prospective home buyer is figuring out which lender to use. The mortgage field has many players: credit unions, banks, savings and loans, mortgage brokers, finance companies, and Internet-based enterprises.

Scores of companies are dangling low-rate mortgages in front of consumers. Don't bite on rate alone. Find out how long the lender has been in operation and what kind of service reputation it's established. Check if it's registered as a financial institution in your state. Getting your mortgage from the credit union means you'll be able to work with someone you know you can trust to look out for your best interests and provide good service throughout the life of the mortgage.

2. How much are the closing costs?

When comparing lenders, remember that interest rate is only *part* of the mortgage costs. You'll also pay closing costs, due at the closing, the process that makes the house officially yours. A major portion of the closing costs is what's known as "points"—various one-time fees the lender charges. One point is equal to one percent of the mortgage amount. Find out how many points the lender charges.

Ask if you have the option of paying fewer or no points in return for a higher interest rate on the loan. That will increase your monthly payments, but require you to come up with less cash at closing. Points are just part of the closing costs, so ask the lender for a preliminary estimate of what all your closing costs will be. (The law requires most lenders to give you a written estimate of closing costs within three days of accepting your mortgage application).

3. What other fees must I pay up front?

Be sure you get the full story on fees. Some lenders won't tell you about all the fees unless you ask for specifics. For instance, if the lender quotes an "application fee," ask what that entails. Is it just for the application? Are there separate fees for obtaining your credit report and appraising the house, or is that included in the application fee? Are there any extra "processing" or "document preparation" fees? You don't want surprises later.

4. How big a down payment must I pay?

Five percent down is a common minimum today, but some special programs require less. You'll have to determine what you can afford. Ask your lender to show you how different down payment amounts will affect the size of your monthly house payments.

5. What will private mortgage insurance cost?

With most loans, if you make a down payment of less than 20% of the home's cost, your lender will require private mortgage insurance (PMI). It's a protection for the lender in case you default on your loan. How much will PMI cost? How will you pay it (usually added in with the monthly payment)? Will you have to pay the full first-year's premium at closing? The law makes it easier to drop PMI once your equity level reaches 22% of the value of your home, if you're current on payments (with some exceptions).

6. How much can I afford to borrow?

Your lender can help you figure out how much your mortgage amount could be, and therefore what price range of homes to look at. This is known as prequalification— not the same as approval or preapproval—and it's wise to do it before you start house shopping. The prequalification gives you some idea of what size mortgage you'll be eligible for, based on preliminary information you give the lender about income, assets, and past debts. The lender will confirm that information later, after you've applied for the loan, plus check into your job and credit history, before granting loan approval.

7. Should I go with a fixed-rate or adjustable rate mortgage (ARM)?

With a fixed-rate mortgage your interest rate stays the same throughout the life of the mortgage. It's usually the best choice if you plan to stay in your house for a long time. Ask the lender to show you what the monthly payments and total interest would be for a fixed-rate mortgage for different loan periods, such as 15, 20, or 30 years.

If you expect to sell your house in a few years, an ARM may be right for you. With an ARM, the interest rate starts out lower than with a fixed-rate mortgage, making monthly payments smaller now, and changes at set intervals. Ask the lender:

- How often can the ARM rate change?
- How much can it change at each adjustment and over the full term of the loan?
- What's the interest rate tied to (known as the index, such as the Treasury bill rate)?
- What is the margin (the amount the ARM rate may exceed the index rate)?
- How much will the payment become at the first adjustment?
- Can you convert the ARM to a fixed-rate mortgage later? When? Is there a conversion fee? Will you have to pay for another appraisal?

8. Can I lock in a rate?

Locking in a rate means that a lender promises to hold a rate for you, even if rates climb before your application process is complete. Ask when the lock-in takes effect: upon application or approval? How long does the lock-in last?

9. When is the mortgage payment due each month?

When is a payment considered late? What is the penalty? Inquire about payment methods. Many lenders will give you a slightly lower rate if you pay by automatic deduction from your account, rather than by coupon.

10. Is there a prepayment penalty?

You may want to pay extra on your mortgage principal when you're able to, to pay off your mortgage sooner than the full term of the loan. Find out if there's a penalty for doing so.