

What Do Loans Really Cost?

By David Reed



Thanks to the Internet, you have choices homeowners could have only dreamed of just a few years ago.

Way back in 1993, if you wanted to search for mortgage rates you could pick up the Sunday paper and glean old data in the real estate section. Or you could get a couple of referrals from your real estate agent for lenders in your area.

But now, your choices are virtually endless. Thanks to the Internet you can now choose from over 100s of lenders all offering the same program and all with different rate programs and combination of fees and points. And as most consumers are now finding out, this new Internet blessing has also borne a new problem, mass confusion.

Go ahead. Log on leading mortgage sites or call a few lenders and check-out the 30-year fixed rate offerings for your city and state.. Depending on where you live, you'll now see about 25 or more lenders all offering a 30-year fixed. Most everyone will show a different annual percentage rate or "APR."

Why is that? How can lenders offer the same exact program with the same nominal rate -- say 7 percent, but have APR numbers all over the map? Pretty confusing, isn't it.

Figuring The APR (Annual Percentage Rate)

Correctly defined as "the cost of money borrowed expressed as an annual rate," the APR is part of the federal Truth in Lending law. When mortgage companies advertise their nominal interest rates, they must also state the mortgage amount along with the annual percentage rate.

In addition, to arrive at an APR, the lender must take into consideration other required lender fees needed to close the loan. Such fees commonly include points and origination fees, application or underwriting fees, prepaid interest and other lender charges. The result is that two lenders with the same interest rate for the same loan may have wildly different APRs. While the APR is certainly intended to be a consumer's tool, it can be difficult for borrowers to make meaningful comparisons.

For instance, suppose a loan officer provides an

array of mortgage choices. He or she gives quotes for a 30-year fixed rate loan, 15-year financing and a 5/1 adjustable-rate mortgage (ARM). Now you're challenged not only to compare APRs from different lenders, but to also compare APRs from different loan programs. The way to end the confusion is to follow three basic steps.

- Decide beforehand, absolutely, your desired loan program for the purpose of comparing lender costs. You can repeat this exercise if you decide later to consider another loan program.
- Ask for a specific rate, say 7.00%, require a predetermined "lock" period, perhaps of 30 days, and provide a specific closing date, say the 20th of the month. (When loans close on different days the APR will change because of daily interest costs.)

- Make sure all lenders are counting the same factors. Did the lender count escrow fees when calculating the APR? Did they count PMI costs? How was the APR for an adjustable-rate mortgage determined? ARMS should use the fully indexed rate (index plus margin) and not just the start rate. Escrow fees, PMI costs, and the fully indexed rate for ARMS are all APR requirements.

Then specifically ask the lender for all lender charges associated with the requested loan such as points, origination, charges, and document fees. Don't worry about title or attorney charges, as those won't change should you simply pick one lender over another, just be concerned with lender fees. Conversely, you can also ask for a rate quote with no points -- what lenders call "par" pricing -- or for quotes with just 1 point. Whatever you're willing to pay, make certain your quotes are for the exact same program -- say a 30-year fixed rate loan with 10 percent down, FHA financing, a VA loan, or whatever program you want to compare.

Now you have rate quotes from different lenders with the same terms and conditions. And, finally, you can use the APR to do what it was supposed to do, help borrowers compare like loans from different lenders.

So go ahead, log onto the Internet, dial that 800 number, or call local lenders, or speak with your broker. It's easy now.