

What New Homebuyers Need to Know

REAL ESTATE, US, MORTGAGE, HOME, LOAN, RATES, CREDIT SCORE, BROKER, HOUSE, FINANCE.

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So you've decided to buy a house, but you're not sure if your finances are quite up to speed. Even if you hope to buy six months from now, there are numerous improvements and adjustments to be made in the interim, prior to taking on a mortgage.

First-time home buying is well documented as an arduous process, and much of that can be attributed to the sheer number of new and unexpected issues. Therefore, the more you know, the better you're likely to fare. Here, briefly, are some aspects buyers should consider when shoring up finances to buy a house. **Knowing is half the battle.** To start, learn as much as possible about the process that will soon temporarily take over your existence. When Corinne Weiner and her fiancé recently bought a home in upstate New York, she says it was one of the most stressful experiences of her life, "but that was mostly because we had a completely incompetent 'team' between the brokers and the bank. So advice number one: get references on those people." She also recommends a book by CNBC's own Suze Orman, "The Money Book for the Young, Fabulous, and Broke" which breaks down the house-buying process in simple terms, and has exercises to make sure buyers can handle the responsibility.

While you've got the researching cap on, Cathi Brese Doebler, author of "Ditch the Joneses, Discover Your Family" recommends shopping around to see which banks give the best rates. "Also, ask people you trust who have mortgages which banks they use and what they think of their experience having a mortgage through that bank."

What can you realistically afford? To determine your price range, use the online calculators, then see if the bank agrees by trying to get pre-approved. "this will bring you back down to Earth so that you can begin shopping in the appropriate price range," says Gail Cunningham, Vice President of Public Relations for the National Foundation for Credit Counseling.

Doebler offers this clever and helpful challenge: "Months before you buy a home, begin putting the amount of money that you will have to use for a house payment into a separate bank account. Save that money rather than spending it for those months, and see how you do at managing your other bills with only the money that is left."

Don't forget to take taxes into account when calculating, cautions Doebler. She also advises not to leave out the not-too-distant future in these estimates. If children come into the picture, can you still afford this house on what might become a single income?

Lynn Ballou, CFP, Principal of Ballou Plum Wealth Advisors, points out other costs that might be overlooked by unsuspecting homebuyers during the initial stages: homeowner's dues ("in our area, \$250 a month is pretty average") utilities including the cable for TV and internet, water and garbage, property insurance ("In California, a \$1 million umbrella policy can run you \$200 - \$350 per year"), moving, furnishing, and maintenance of the home.

Oh yeah? Prove it! When Andy Payment of Atlanta, Georgia applied for a mortgage, it was an ordeal. He recalls several back-and-forths with the lender to demonstrate that they had the money to put down on the home and pay the mortgage in the short term.

Among the hoops they had to jump through: Hold the down payment (5%, in his case) plus closing costs in a savings account for more than two months and provide bank statements to demonstrate that it was earned and not gifted. "We didn't realize this was necessary, so only sent statements for our checking/savings accounts (vs. 401(k), stock, other liquid assets)." He also had to hold two months of mortgage payments in savings to demonstrate we could pay the actual mortgage.

How's that credit score looking? Six months is a good amount of time to start preparing your finances in anticipation of buying a home, Cunningham says, because it takes time to clear up old forgotten debt and have it cycle through to the credit report and score.

First she recommends that the buyer should get credit reports from all three bureaus, to avoid any surprises, and review them all for inaccuracies, which must then be disputed.

"Make sure that any old negative information that should have rolled off, has. Pay off any lingering old bills that you've forgotten about. If you're behind on any payments, get caught up."

Next, check your credit score, which you'll want to nudge up to as high a number as possible. This is where paying down your debt comes in, aiming for an amount that doesn't equal more than 30 percent of your line of credit. Cunningham offers the tried and true credit score advice: "Make sure that you have at least three open and active lines of credit. You need this many for the credit score to have enough data to crunch. The model also likes for you to have a good mix of credit. For instance, an open-ended account (general purpose card), a closed-end account (car payment), and a personal loan. This demonstrates that you can handle multiple types of credit responsibly."

Finally, here's a piece of less traditional credit wisdom, courtesy of Chip Poli, owner of Poli Mortgage Group, Inc. "Credit reporting sites supply a score calculated by something called 'VantageScore' and it trends much higher than the FICO scoring used by the mortgage industry. Consult with your loan officer and find out what your true credit score is. It's vital to start the prequalification process early."

How much can you pay up front? “One obvious tip: start saving,” says Cunningham. “Even if you qualify for a low down-payment loan, the lender will still want to see that you have significant savings. This is a further protection for them against loss, and demonstrates that you can weather a financial hiccup if one should come along.”

The more money you can put down as a down payment, the lower your mortgage will be. “I personally cleaned out my IRA for the down payment (as long as it's under 10K you don't get penalized) because I'm young and can boost it up again,” says Weiner.

Now, sit. Stay! Part of proving your mortgage-worthiness is demonstrated stability, so prospective home buyers should plan to stay put in their current living situation and job. “I can't tell you how much hassle I got because I switched jobs a few times in the past two years,” says Weiner, who had changed careers and moved during that time. “I actually had to write a letter to the underwriters explaining why I changed jobs so much!” Fortunately, homebuyers of the future now have plenty to keep them occupied while staying put.

Note: An earlier version of this article stated your mortgage rate would be lower with higher down payments. It has been corrected.