

# Top Six Down Payment Mistakes

About to make a down payment on a home? Here's how to avoid the six most common down payment errors. Deciding how much of a down payment to make on a home is one of the most crucial steps in the mortgage process. The amount you pay up-front is a major factor in determining how much your monthly payments will be, which makes it a decision that could affect you for years to come. Here are six of the most common down payment mistakes home buyers make and advice on how to avoid making them yourself.

## **Mistake #1: Making too small a down payment**

While lenders do offer mortgages with down payments of less than 20 percent of a home's sale price, these loans require you to pay private mortgage insurance (PMI) -- an additional fee tacked on to your monthly payment to help protect the lender in case you should default on your loan.

In addition, low- and no-down-payment loans frequently carry higher interest rates and so can end up costing you considerably more over the life of your loan. Conversely, a down payment greater than 20 percent may earn you a more favorable interest rate if you have a less-than-stellar credit rating.

## **Mistake #2: Making too large a down payment**

While common sense dictates that the more you pay up front, the better off you'll be, that's not always the case. One mistake first-time homebuyers sometimes make is using such a large portion of their savings for their down payment that they end up not having enough left over to cover closing costs and other expenditures for their new home.

## **Mistake #3: Not making a down payment at all**

Some lenders offer mortgages that require no down payment but these loans can be risky. Paying no money down puts you in the position of having no equity in the home (i.e. you don't own any part of it). Should the value of your home fall, there is the risk that you could end up owing more to the lender than your house is worth. This situation could also make it difficult to refinance your mortgage in the future.

A no-down-payment mortgage may be an effective strategy in certain situations. However, you need to be economically responsible and financially sound to be able to handle the inherent risks involved.

No-down-payment loans often come with a higher interest rate than loans with a conventional down payment. As a result, your monthly payments will be higher, leaving you with less money available for bills and emergencies.

Since you'll be paying less than 20 percent of the home's purchase price, you will also have to pay PMI or be required to take out a second loan (known as a "piggyback loan"). Each of these options increases the monthly cost of owning the home.

## **Mistake #4: Paying with unseasoned funds**

In most cases, a down payment is a pretty substantial chunk of money, and not everyone has the

ready cash to cover it. A gift from a friend or family member can help, but don't think that just because you've come up with the full amount that you're necessarily in the clear.

All funds -- whether they're gifts from relatives, loans against an investment portfolio or your own savings -- that have been in your account for longer than two months are referred to as "seasoned," meaning that they're considered your money. If your bank statements indicate a large cash deposit that's less than two months old, your lender will need to know where those funds came from and whether they're gifts or loans. Gift-givers may be required to provide a letter to the lender indicating that they are in a financial position to offer the gift. Also, generally speaking, the larger your overall down payment amount, the less concerned the lender will be about where the money is coming from.

The lender wants assurances that the money you're putting towards your down payment is actually "yours," since it's assumed that if you're investing a significant portion of your own money into the down payment, you're less likely to default on your loan.

**Mistake #5: Neglecting to bring a cashier's check to closing**

Along with figuring out how much of a down payment you should make, you also need to ask your closing agent exactly how much you will be required to pay at closing. It's not enough to simply bring your personal checkbook to closing. You will need a cashier's check to pay the amount of your down payment and your closing costs. Find out ahead of time exactly what the final total will be and obtain a cashier's check for that amount.

**Mistake #6: Incorrectly assessing your debt comfort level**

No one knows better than you how much debt you can handle. Trust your instincts; if you'd rather pay as much as you can at the start and have the benefit of lower monthly payments, don't let anyone dissuade you from that. The worst thing you can do is lock yourself into a mortgage that ends up costing you more per month than you can comfortably afford to spend.