Important Things To Avoid Before Buying a Home

Don't Move Money Around

When a lender reviews your loan package for approval, one of the things they are concerned about is the source of funds for your down payment and closing costs. Most likely, you will be asked to provide statements for the last two or three months on any of your liquid assets. This includes checking accounts, savings accounts, money market funds, certificates of deposit, stock statements, mutual funds, and even your company 401K and retirement accounts.

If you have been moving money between accounts during that time, there may be large deposits and withdrawals in some of them.

The mortgage underwriter (the person who actually approves your loan) will probably require a complete paper trail of all the withdrawals and deposits. You may be required to produce cancelled checks, deposit receipts, and other seemingly inconsequential data, which could get quite tedious.

Perhaps you become exasperated at your lender, but they are only doing their job correctly. To ensure quality control and eliminate potential fraud, it is a requirement on most loans to completely document the source of all funds. Moving your money around, even if you are consolidating your funds to make it "easier," could make it more difficult for the lender to properly document.

So leave your money where it is until you talk to a loan officer.

Oh…don't change banks, either.

The Effect of Changing Jobs

For most people, changing employers will not really affect your ability to qualify for a mortgage loan, especially if you are going to be earning more money. For some homebuyers, however, the effects of changing jobs can be disastrous to your loan application.

How Changing Jobs Affects Buying a Home

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Salaried Employees

If you are a salaried employee who does not earn additional income from commissions, bonuses, or over-time, switching employers should not create a problem. Just make sure to remain in the same line of work. Hopefully, you will be earning a higher salary, which will help you better qualify for a mortgage.

Hourly Employees

If your income is based on hourly wages and you work a straight forty hours a week without over-time, changing jobs should not create any problems.

Commissioned Employees

If a substantial portion of your income is derived from commissions, you should not change jobs before buying a home. This has to do with how mortgage lenders calculate your income. They average your commissions over the last two years.

Changing employers creates an uncertainty about your future earnings from commissions. There is no track record from which to produce an average. Even if you are selling the same type of product with essentially the same commission structure, the underwriter cannot be certain that past earnings will accurately reflect future earnings.

Changing jobs would negatively impact your ability to buy a home.

Bonuses

If a substantial portion of your income on the new job will come from bonuses, you may want to consider delaying an employment change. Mortgage lenders will rarely consider future bonuses as income unless you have been on the same job for two years and have a track record of receiving those bonuses. Then they will average your bonuses over the last two years in calculating your income.

Changing employers means that you do not have the two-year track record necessary to count bonuses as income.

Part-Time Employees

If you earn an hourly income but rarely work forty hours a week, you should not change jobs. There would be no way to tell how many hours you will work each week on the new job, so no way to accurately calculate your income. If you remain on the old job, the lender can just average your earnings.

Over-Time

Since all employers award overtime hours differently, your overtime income cannot be determined if you change jobs. If you stay on your present job, your lender will give you credit for overtime income. They will determine your overtime earnings over the last two years, then calculate a monthly average.

Self-Employment

If you are considering a change to self-employment before buying a new home, ***don't do it.*** Buy the home first.

Lenders like to see a two-year track record of self-employment income when approving a loan. Plus, self-employed individuals tend to include a lot of expenses on the Schedule C of their tax returns, especially in the early years of self-employment. While this minimizes your tax obligation to the IRS, it also minimizes your income to qualify for a home loan.

If you are considering changing your business from a sole proprietorship to a partnership or corporation, you should also delay that until you purchase your new home.

No Major Purchase of Any Kind

Review the article title "Don’t Buy a Car," and apply it to any major purchase that would create debt of any kind. This includes furniture, appliances, electronic equipment, jewelry, vacations, expensive weddings…

…and automobiles, of course.

Don't Buy a Car

When an individual’s income starts growing and they manage to set aside some savings, they commonly experience what may be considered an innate instinct of modern civilized mankind.

The desire to spend money.

Since North Americans have a special love affair with the automobile, this becomes a high priority item on the shopping list. Later, other things will be added and one of those will probably be a house.

However, by the time home ownership has become more than a distant and hopeful dream, you may have already bought the car.

It happens all the time, sometimes just before you contact a lender to get pre-qualified for a mortgage.

As part of the interview, you may tell the loan officer your price target. He will ask about your income, your savings and your debts, then give you his opinion. "If only you didn’t have this car payment," he might begin, "you would certainly qualify for a home loan to buy that house."

Debt-to-Income Ratios and Car Payments

When determining your ability to qualify for a mortgage, a lender looks at what is called your "debt-to-income" ratio. A debt-to-income ratio is the percentage of your gross monthly income (before taxes) that you spend on debt. This will include your monthly housing costs, including principal, interest, taxes, insurance, and homeowner’s association fees, if any. It will also include your monthly consumer debt, including credit cards, student loans, installment debt, and….

…car payments.

How a New Car Payment Reduces Your Purchase Price

Suppose you earn $5000 a month and you have a car payment of $400. At current interest rates (approximately 8% on a thirty-year fixed rate loan), you would qualify for approximately $55,000 less than if you did not have the car payment.

Even if you feel you can afford the car payment, mortgage companies approve your mortgage based on their guidelines, not yours. Do not get discouraged, however. You should still take the time to get pre-qualified by a lender.

However, if you have not already bought a car, remember one thing. Whenever the thought of buying a car enters your mind, think ahead. Think about buying a home first. Buying a home is a much more important purchase when considering your future financial well being.