Homebuyer’s Must-know Terms

Don’t know your LTV from your DTI? Here are key terms you’re likely to hear during your homebuying journey—defined.

Adjustable-rate mortgage (ARM)

With ARM loans, interest rates can change after an initial fixed-rate period as they adjust based on the interest rate index the ARM is tied to (e.g., LIBOR, COFI, etc.). This loan type is less predictable than a traditional fixed-rate mortgage, but it can potentially yield lower interest rates during certain periods.

Annual income

Money you receive over the course of a year, whether it’s from wages or salary, alimony or child support, rental payments, commissions, investments, or other sources.

Appraisal

An appraisal is required to gather the estimated value of a piece of real estate. During the home sale, the mortgage lender sends out an appraiser to get a professional opinion of the value of the property. This helps the lender decide if the property is worth the amount of the loan the potential buyer is seeking.

Appraisal contingency

An appraisal contingency is a clause that allows a buyer to dissolve a purchase agreement if a home's appraised value is less than the sale price.

An appraiser hired by the buyer's lender evaluates the value of the home to ensure that the loan is secured by an appropriate home value. Lenders want to ensure they are not "over-paying" for a property.

As-is

A property marketed in "as is" condition usually indicates that the seller is unwilling to perform most if not all repairs. It could also mean that it is priced "as is," which is typically lower than market pricing in the area.

Finally, "as is" is in the condition at the time the offer was written, and should something happen to the property from the time the offer was written to the closing time which alters that condition, then that property is no longer "as is," as it was, and should be brought back to its original "as is" condition at the time of offer, at the cost of the seller. Or in the alternative, the seller should release the buyer from their obligation to purchase and refund the monies spent by the buyer, such as earnest money.

Backup offer

When a buyer is interested in purchasing a property that is already under contract with someone else, that buyer has an opportunity to submit a "backup offer" in case the first transaction falls apart. A backup offer must still be negotiated and any monies, such as earnest money, submitted to confirm it is the next offer in line. There can only be one backup offer legally, as you cannot have a backup to the backup.

Blind offer

When a buyer makes an offer on a property they haven't seen, even when it was possible to see it, that offer is considered a "blind offer". It is most commonly used in a highly competitive area and/or circumstance and used as an attempt to be first and win quickly.

Buyer's agent/listing agent

A buyer's agent, also known as a selling agent, is a licensed real estate professional whose job is to locate a buyer's next property and represent their interests by negotiating on behalf of that buyer to obtain the best price and purchasing scenario for that buyer as possible. This agent is a fiduciary for the buyer.

The listing agent, also known as the seller's agent, is a licensed real estate professional whose job is to market the seller's property and to represent the seller's best interest by negotiating on behalf of the seller to secure the best price and selling scenario as possible. This agent is a fiduciary for the seller.

Buyer and listing agent commissions are typically around 2- 3% of the contract price on each sale.

Comps

Short for "comparables." These are recently sold properties similar to the home you want, with approximately the same size, location, and amenities. They help an appraiser determine a property's fair market value.

Covenants, conditions & restrictions (CC&Rs)

Usually, these are the rules and regulations placed on real property by a homeowner's association (HOA), a neighborhood association, a developer, or a builder that sets forth any requirements and limitations of what a homeowner is allowed to do with the property. It may also include monthly and/or annual fees or special assessments.

Conventional sale

A conventional sale is when the property is owned outright (has no mortgage remaining) or the owner owes less on their mortgage than what the market indicates the owner could sell their property for. Such conventional sales are often smoother transactions than non-conventional sales, such as foreclosures, probate-related sales, and short sales.

Closing

Closing is when the home sale is considered final, which typically includes all parties' signatures on all required documents, all monies conveyed, and when a lender is involved, with full lender's approval. For some markets across the nation, recording the deed with the county clerk's office is the ultimate and final step of closing. Once all of these items are completed, then a buyer's access to the property is then provided, and the buyer is considered the new homeowner.

Closing costs

Closing costs are an assortment of fees, including fees charged by: a lender, the title company, attorneys, insurance companies, taxing authorities, homeowner's associations, real estate agents, and other closing settlement-related companies. They are typically 2 to 5 percent of your loan amount and are typically paid at the time of closing a real estate transaction.

Closing Disclosure (CD)

A document that provides key information about your loan, such as the interest rate, monthly payments, and closing costs. The lender must give you this document at least three business days before you close on the loan, and the information should match the Loan Estimate you received when you applied. You can find out more about what's on a closing disclosure from the Consumer Financial Protection Bureau.

Conforming loan

A mortgage loan that meets guidelines established by Fannie Mae and Freddie Mac and falls below a loan amount specified by the Federal Housing Finance Agency.

Contingencies

Conditions in a sales contract that must be satisfied before the home sale can occur. Some common contingencies: The appraised value must support the sales price, the house must pass inspection, and the borrower must be approved for a loan. Others might require a check for termites or the sale of the buyer's current home.

Days on market (DOM)

DOM is defined as the number of days from the date on which the property is listed for sale on the local real estate brokers' multiple listing service (MLS) to the date when the seller has signed a contract for the sale of the property with the buyer.

A related metric is the average DOM for homes sold in a market during a specified period. A low average DOM indicates a strong market that favors sellers. A high average DOM signals a weak market that favors buyers. Seasonality can also be a factor.

Homes generally appear to sell faster in Spring than Winter since you often have more people looking to purchase and sell during the more pleasant weather months rather than the colder, more uncomfortable weather months.

Debt-to-income ratio

Debt-to-income, or DTI, the ratio is a number used by mortgage lenders which is determined by the total of your debt expenses, plus your monthly housing payment, divided by your gross monthly income and multiplied by 100. This helps lenders determine affordability based on their available loan programs and allows them to estimate how much you can afford to pay monthly for a mortgage. Lenders typically look for borrowers who pay 28 percent or less of their total monthly income on housing and less than 36 percent of their income on debt payments. If either percentage is on the higher side, and you want to buy a home, you might need to adjust your budget.

Down payment

The amount of cash you can put toward the purchase price of a home. Down payments often range from 3 to 20 percent of the home price.

Due diligence

A due diligence period of time might be available in the purchase agreement, which is a time frame provided to a buyer to examine a property fully, often by hiring experts to inspect the property, perform tests, etc., so that a buyer may decide on how to proceed.

A buyer might also be afforded an opportunity to renegotiate the contract based on their findings or possibly even terminate within a specified time period, in order not to be considered in default of the contract. Due diligence allows a buyer to fully understand what they are buying.

Earnest money deposit (EMD)

An earnest money deposit (EMD), sometimes referred to as a "good faith deposit," is the initial funds that a buyer is asked to put down once a seller accepts the buyer's offer. It shows not only that the buyer is serious about buying but that they are also willing to put their money where their mouth is.

The amount of the EMD can vary between 1 to 5 percent of the sales price. The EMD is often held by an escrow company or as otherwise provided for under the purchase and sale agreement (PSA).

Escrow

Funds are deposited with a third party and held until a specific date is reached and/or a specific condition is met. For example, when you make an offer on a home, your earnest money deposit may be held in an escrow account until closing. Some lenders may require borrowers to establish an escrow account at closing comprised of future tax and insurance payments. The loan servicer then makes your property tax and insurance payments on your behalf.

Escrow holder

The escrow holder is the agent and depositary (impartial third-party) who collects the money, written instruments, documents, personal property, or other things of value to be held until the happening of specified events or the performance of described conditions, usually set forth in mutual, written instructions from the parties.

Equity

This is the investment a homeowner has in their home. To calculate equity, take the home's market value and subtract any mortgages or liens against the property. The amount left over is the amount of equity you have in the home.

If you buy a home worth $250,000 for $240,000, you gain what is known as instant equity because there is a $10,000 difference between the value and the cost. When you sell a home you bought for $250,000 for $260,000, you'll get to keep the equity in the home after the close, once all the expenses are paid.

It's important to build equity as homeowners can leverage this financial asset to obtain loans to help finance items such as home repairs or to pay off higher interest debt.

FHA loans

FHA loans are part of a group of loans that are insured by the federal government. This means that instead of actually lending money, the FHA insures banks and private lenders that they will cover losses they might incur in the event that the borrower does not repay the loan in full or timely.

FHA 203k rehab loan

This is a “fixer-upper” loan, which combines the mortgage loan with a loan to help pay for repairs or updates, such as structural repairs or energy-related updates. It is not intended to lend based on luxury upgrades such as adding a swimming pool or tennis courts.

Fixed-rate mortgage

With fixed-rate mortgages, your interest rate stays the same for the duration of the loan. They are often available as 10, 15, 20 & 30-year loans. The 15- and 30-year loans are by far the most popular type of home loans, accounting for about 75% of all U.S. residential mortgages, according to Mortgageloan.com.

Hard money loan

Hard money loans are a way to borrow without using traditional lenders. Hard money lenders finance the loan based on the property in question, not on your credit score, and typically require a large down payment and short repayment schedule, according to Nerdwallet.

Homeowner’s association (HOA)

A homeowner’s association is a private association that manages a planned community or condominium. When you purchase a property that is managed by an HOA, you agree to abide by the HOA’s rules and pay its monthly or annual HOA dues. If you fail to pay and/or comply, they often have the ability to file a lien against the property and/or foreclose on the property.

Home sale contingency

A home sale contingency is for a buyer to indicate to a seller that part of their condition to purchase the seller's property relies on the buyer's ability to finalize a close on their current property. This is often negotiated with a clause in a contract or with an addendum to a contract. An example of how such a contingency can be used would be if a buyer needs to sell their property in order to have the down payment required on the purchase of the new property or would rather use their sale proceeds instead of their savings to make the down payment.

Depending on the market, it could hamper negotiations with a seller when a contingency is part of the picture.

iBuyer

An iBuyer is a company that uses technology to make an offer on your home quickly or "instantly," as the term implies. iBuyers take on the burden of owning, marketing, and reselling your home. Depending on the service you choose, the benefit is the certainty of an all-cash offer and more control over when you move.

Inspection

An inspection happens when buyers pay a licensed professional inspector to visit the home and prepare a report on its condition and any needed repairs. The inspection often happens as part of the due diligence period, so buyers can fully assess if they want to buy a particular home as is or ask the seller to either complete or pay for certain repairs.

Inspection contingency

Also known as a “due diligence contingency,” the inspection contingency is a clause sometimes offered in a purchase agreement that grants buyers a predetermined amount of time during escrow to perform any necessary inspections.

Land lease

Traditionally, when you purchase a home, you own the home and the land the property is built on. There are some circumstances that involve a land lease, which means you would own the home while paying rent to the landowner for the land.

Loan contingency

A loan contingency is a clause or addendum (also known as a mortgage contingency) in an offer contract that allows a buyer to back out of a deal and keep their deposit if they are unable to secure a mortgage with specified terms during a fixed period of time.

Loan Estimate (LE)

A disclosure to help consumers understand the key loan terms and estimated costs of a mortgage. After a consumer submits six key elements—name, income, Social Security number, property address, estimated property value, and desired loan amount—the lender is required to provide this form. All lenders are required to use the same standard Loan Estimate form to make it easier for consumers to compare and shop for a mortgage. Learn more about loan estimates from the Consumer Financial Protection Bureau.

Loan-to-value ratio (LTV)

The total amount of your mortgage compared to the home's appraised value, expressed as a percentage. If your down payment is less than 20 percent of the purchase price, your LTV is above 80 percent, so you generally pay a higher interest rate on your mortgage and may need to pay private mortgage insurance (PMI).

Mortgage points (or discount points)

An amount paid to the lender, typically at closing, to lower (or buy down) the interest rate if the buyer chooses to do so. One discount point equals one percentage point of the loan amount. For example, 2 points on a $100,000 mortgage cost $2,000.

Mortgage pre-approval letter

Getting a mortgage pre-approval letter is important because it gives home buyers an idea of what they can afford. A mortgage pre-approval letter is issued by the lender and identifies the terms, loan type, and loan amount the buyer qualifies for after checking the buyer's debt-to-income ratios along with cash on hand and credit history.

Many sellers or their agents require a mortgage letter with any home offer that isn't all-cash since it acts as proof the buyer has been qualified to get financing.

Multiple listing service (or MLS)

An MLS is a database that allows real estate agents and broker members to access and add information about properties for sale in an area. When a home is listed for sale, it gets logged into the local MLS by a listing agent. Buyer's agents often check the MLS to see what's on the market and what similar homes have sold for. According to Inman.com, there are over 600 MLS organizations in the United States.

Natural hazards disclosure (NHD) report

A report required by most states that discloses if a property is located in an area that has a higher risk of natural hazards. The report is typically paid for by the seller and given to the buyer during escrow.

The following natural hazard zones are covered in a NHD report:

- Special flood hazard area
- Area of potential flooding
- Very high fire hazard severity zone
- Wildland area that may contain substantial forest fire risk and hazards
- Earthquake fault zone
- Seismic hazard zone

Offer/counter offer

Buyers make a formal offer on the home they want to purchase. The offer can be the full list price, or what you and your agent deem a fair market value.

The buyer's agent puts the offer in writing, asks you to sign it, and then submits it to the seller's agent. The seller might immediately accept it, in which case it becomes the parties' purchase contract or may make what's known as a counter offer. It's the art of negotiation, recorded in paperwork.

Option period (Texas only)

A termination option period (known as “option period”) is a form of a due diligence period, however, it is only available to a buyer who separately purchases this right for a negotiable amount of money and for a negotiable period of time.

When a buyer has purchased this right to terminate, they are strongly encouraged to get all of their inspections and other due diligence performed during this option time frame, although doing so during this timing is not required.

If the buyer chooses to terminate the contract within the option period, then the earnest money shall be released back to the buyer.

Origination fee

A fee from the lender that covers the expenses of processing a mortgage loan. It is usually a percentage of the amount loaned—often 1 percent. It can be expressed in the form of points or a flat fee.

PITI

An acronym for principal, interest, taxes, and insurance. Sometimes called your monthly housing expense, it includes your mortgage payment and a monthly portion of your real estate taxes and homeowners insurance.

PMI

An acronym for private mortgage insurance, which protects the lender against losses if you cannot repay your loan. Your lender may require it if your down payment is less than 20 percent.

The Affordable Loan Solution® mortgage offers eligible modest-income borrowers a down payment as low as 3 percent with lower-cost mortgage insurance.

Pre-approval

Getting pre-approved requires home buyers to fill out an application that allows a lender to determine their financial situation, including their debt-to-income ratio, ability to repay, and credit-worthiness. Once this is in hand, the lender can give the buyer a letter stating the exact loan amount they have been pre-approved for, along with the total sales price they are approved for.

The letter will usually indicate both the buyer's estimated down payment along with the potential interest rate. Because it is much more thorough than a pre-qualification letter, most sellers prefer to see a pre-approval letter with an offer.

Preliminary report

A preliminary report reveals any issues with a title that need to be dealt with by the seller in order to deliver a clear title. It gives details such as ownership history, liens, and easements. The title company gathers this report by searching existing property records at the county recorder's office.

This report is required for a title insurance company to issue a title insurance policy. Most lenders require borrowers to purchase title insurance coverage to protect their interest in a property. It's customary in many areas for a seller to pay for this policy, although it is a negotiable item.

Pre-qualification

A pre-qualification is a lender's estimate of the amount a home buyer can expect to be approved for during the loan process. Getting pre-qualified is a quick assessment by a lender of the buyer's financial situation based solely off of what a buyer tells a lender, and not based with any proof or verifications.

Principal

The principal balance of a mortgage loan is the amount of money owed to the lender, not including interest. Say you borrow $300,000. That's the principal of the loan, or what you borrowed to buy the home. Buyers pay the principal plus interest each month, although calculated on a daily basis for most loan type. Payments nearly always go toward interest first, then toward paying down the principal. After all, the interest is the reason the bank agrees to make the loan.

Probate sale

A probate sale happens when a homeowner dies without writing a will or leaving property to someone. In such situations, the probate court would authorize an estate attorney, or another representative, to hire a real estate agent to sell the home.

The total process will usually be a bit more complicated and, therefore, will take more time than a conventional sale.

Proof of funds

When you make an offer, sellers will require you to submit proof of funds. If you're buying a house with a mortgage, it shows them that you have the cash available for your down payment and closing costs. If you're paying all cash, your proof of funds shows you actually have the money.

The following documents qualify as proof of funds:

- Original or online bank statements with bank letterhead
- Copy of a money market account balance with the bank's logo or letterhead
- Certified financial statements, such as an income or cash flow statement that's been signed off on by an accountant
- An open equity line of credit

Purchase and sale agreement (PSA)

A purchase and sale agreement is commonly referred to as a written contract between the buyer and seller, which outlines the terms of the parties to sell and purchase real property.

When a home is "under contract," it usually signifies that the Buyer and Seller have formalized their commitment to sell and purchase the real property.

Real-estate owned (REO)

Real-estate owned is a designation given to properties that are owned by a lender due to an unsuccessful foreclosure sale at auction.

REO properties can sometimes present an opportunity for a buyer to be purchased for below market value as most banks would prefer to reinvest the proceeds rather than waste time marketing the property for an extended period.

Additionally, the bank will often market the property "as-is," meaning they are unwilling to make any repairs to the property, which can make financing tricky.

REALTOR®

An actively licensed real estate agent and REALTOR® are often used interchangeably, although not every real estate agent is a REALTOR®. A REALTOR® is a member of the National Association of REALTORS® (NAR).

A REALTOR® promises to uphold the Code of Ethics of the association and to hold each other accountable when serving the public, customers, clients, and each other, with a high standard of practice and care.

Rent-back

Rent-back, or leaseback, refers to an arrangement whereby the buyer, who is now the new homeowner, agrees to allow the seller, the now-tenant, to stay in the house beyond the close of escrow. The terms are negotiated prior to the situation occurring and will often involve a lease deposit, a daily rental rate, and a length of time allowable.

The rate can sometimes be determined by looking at the new homeowner’s monthly out-of-pocket for the mortgage as well as the possible inconvenience this may cause them in delaying their own move, all factoring into a daily rate.

Seller concession

Sellers may offer concessions to incentivize buyers to purchase the home or sweeten the deal.

Concessions are most readily seen as a contribution towards the buyer’s closing costs, up to certain limitations and approvals by a buyer’s lender, which ultimately leaves more money in a buyer’s pocket when all is said and done.

Seller disclosure

A seller’s disclosure is a disclosure by the seller of information about the property which could affect a buyer’s decision to purchase the property, all to the best of the seller’s knowledge.

A seller must also indicate items that are not specific to the property itself but related to a person’s enjoyment of the property, such as pest problems, property line disputes, knowledge of major construction projects in the area, military base-related noises or activities, association related assessments or legal issues, unusual odors caused by a nearby factory, or even recent deaths on the property as permitted by law.

Short sale

In a short sale, the property is being sold for less than the debt secured by the property. Short sales will require the approval of the seller’s lender(s) as the proceeds of the sale will be just “short” of the amount owed; most lenders’ processes of approving short sales are long and drawn out, requiring more time to close than a traditional sale.

Subject to inspection

Subject to inspection, or “submit offers subject to inspection”, means that the seller is not allowing the property to be viewed without an accepted offer. Some common reasons for this are privacy concerns of the occupants or uncooperative tenants.

The thought of buying a property sight unseen can be daunting for the traditional buyer, which can be used to your advantage as this will inevitably drive overall interest down.

It’s also not as bad as it seems as, under the standard purchase contract, you will have an inspection period, during which you can cancel the sale with no penalty.

Tenancy in common (TIC)

Tenancy in common describes a type of joint ownership of a property, whether a single-family property or a commercial building. The tenants in common all own the property, but in different ratios.

Depending on the property type will determine the ease or difficulty in securing financing. Also to note, tenants in common do not have the right to survivorship (the surviving owners do not get to split up the deceased tenant’s property interest), and instead, the deceased tenant’s ownership interest/percentage actually falls to their estate, as defined by their will or the governing law.

Termite report

Termites are small, pale, soft-bodied insects that feed on wood, and can be highly destructive. The WDI (wood-destroying insect) report, also known as the Termite Report, includes a diagram of the property and the location of active and/or previous WDI activity.

The report can also and sometimes include what may be necessary to resolve such possible infestations such as spraying or tenting. The WDI report will rarely, if ever, include the cost for such items, as that may be considered a conflict of interest.

Title insurance—Insurance that protects against issues, such as a tax lien or other legal claim, that would affect ownership of the property.

Title search

A title search examines public records for the history of the home, including sales, purchases, tax, and other types of liens.

Generally, a title examiner will conduct a search using title plants and sometimes the county records to see who is listed as the record owner of the property. Such information, along with any liens or encumbrances recorded against the property, will be listed in the Preliminary Report for the parties to review prior to closing escrow.

Trust sale

A trust sale means that the home is being sold by a trustee of a living trust – and not a private party. More often than not, this is because the original homeowner has passed away, or has placed their assets in a living trust.

The trustee may not be as emotionally attached to the property as a traditional owner, which could translate to them accepting a less attractive offer as the trustee may prefer to offload the property

Underwriting

The lender reviews submitted documents to verify the borrower’s finances and other factors related to the home, such as the title search and appraisal, then decides to approve or deny the loan.

VA Loan

A VA loan is a loan guaranteed by the government (Department of Veteran Affairs) and available to the military, active and retired, and even for some eligible spouses, at low-to-no-down payment scenarios with competitive rates and fees.