

# Buying a home with a low down payment

Looking for a mortgage that doesn't require a 20 percent down payment? Here are some options.

You've found a home you'd love to own, and you're ready to buy. But you don't have a 20 percent down payment. Don't worry; there are several low-down-payment alternatives.

## **Private mortgage insurance**

It's possible to get a mortgage with a down payment of as little as 3 percent by taking out private mortgage insurance (PMI). This insurance protects the lender in case you default on your mortgage payments by ensuring that the outstanding balance will be paid off.

The cost of PMI varies but, in general, it's about one-half of one percent of the mortgage amount per year, or \$500 for a \$100,000 loan. The good news is that once you've paid down your mortgage to the point where you achieve 20 percent equity in your home, most lenders will allow you to cancel the insurance. You may also be able to drop it if an updated appraisal indicates your equity has increased sufficiently due to an increase in the value of your home.

PMI can sometimes be financed through your mortgage loan (often called a self-insured mortgage). You will likely have to pay a higher interest rate, but the payments are usually tax-deductible as mortgage interest.

## **FHA loans**

A second option is to apply for an FHA mortgage. These loans, designed for those with less-than-perfect credit, are insured by the Federal Housing Administration and also allow a down payment as low as 3 percent.

The down payment can be a gift from a family member, government agency or non-profit organization. However, there is a limit to the amount you can borrow, which varies depending on your location. You will also be required to take out FHA mortgage insurance. In most cases, this insurance costs 1.5 percent of the loan amount on closing, plus 0.5 percent per year -- the amount can be rolled into your mortgage.

On a \$100,000 mortgage, the 1.5 percent upfront FHA mortgage insurance payment would be \$1,500 which, wrapped into a fixed, 30-year mortgage at 8 percent, would come to an additional \$11.01 per month. The 0.5 percent annual premium would be \$500 per year or \$41.67 per month.

Government-insured loans are also available for those with military service under the Veterans Administration (VA) loans program, and for rural residents under the Rural Development Housing and Community Facilities program.

## **Piggyback loans**

Also called a second trust loan or second mortgage, a piggyback loan is a second loan that closes at the same time as your first mortgage. The idea is to combine this loan with your down payment in order to reach the 20 percent needed for a conventional mortgage.

The most common piggyback loan is an 80/10/10: your mortgage equals 80 percent of the purchase price, and your second trust loan and down payment each equal 10 percent. There are also 80/15/5 loans, which require you to put down only 5 percent.

With this arrangement, you'll have two loans to pay each month. And the interest rate on the second trust loan will likely be higher than that of your first mortgage. In addition, paying the closing costs on another loan will add to your upfront expenses. But your total payments may be less than they would be if you were paying for PMI. Plus, the interest on a piggyback loan may be tax-deductible, though you should consult a tax advisor about your situation.