7 Terms Every Homebuyer Should Know

When buying a home, understanding your contract is one of the most important protections you have to ensure you make an informed decision. While the terms used may change from place to place, seven common terms are particularly important for you to understand.

1. Good-faith estimate. The good-faith estimate is not part of the purchase contract, but is still important. The good-faith estimate has a twofold purpose, it gives buyers a snapshot of their estimated costs for closing services, the down payment and prepaid items like homeowners association dues, homeowners insurance and property taxes. In addition, buyers can use the estimate to hold their lenders to the amount promised in certain categories of costs.

2. Good Funds. The law requires escrow to comply with the “Good Funds Law” (AB512). The funds may be a wire transfer. Wire Transfers must be from a FDIC insured bank – A wire transfer is the best choice to insure funds or closing escrow are good funds. These funds are electronically transferred into the escrow trust account from the client’s bank account. Other forms are a Cashier’s check which must be issued from a California Bank. However, once a cashier’s check has been deposited for closing, the amount does not become “Good Funds” until it has been paid by the issuing financial institution. Personal checks are not considered “Good Funds” and cannot be used for closing purposes. Finally, the payment of a Money Order cannot be tracked and does not constitute “Good Funds”. Escrow does not, under any circumstance, accept Money Orders

3. Contingency. A contingency is a clause in a contract that sets the conditions under which the contract can be voided and the deposit returned to the buyer. Contingencies are negotiable. So if you believe you need more time for an inspection or to obtain financing, you can write that into your offer.

4. Disclosure/disclaimer. Rules vary from state to state about what homeowners need to disclose to potential buyers, but most states require sellers to complete a form that tells buyers what they know about their property. California sellers must disclose anything that affects the 'value and desirability' of the property.

5. Earnest-money deposit. Buyers usually attach a check for their earnest-money deposit to their offer. The check is put into escrow once the contract has been approved by all parties and is used as part of the down payment at settlement.

6. Escrow. Escrow is handled by a title company or an escrow company. An escrow account includes the buyer's deposit and all the financial portions of the purchase transaction before, during and after the settlement. The escrow company will pay off all the liens on the property after settlement and will record the transaction at the local courthouse or county office. The term escrow also refers to prepaid amounts for homeowners insurance and property taxes that you pay with your mortgage bill each month. Your lender will keep these funds in an escrow account until the bills are due.

7. Title Insurance. There are two types of title insurance: Owner's title insurance, and Lenders title insurance, also called a Loan Policy. An Owner's Policy fully protects the buyer should a covered title problem arise with the title that was not found during the title search. The Owner's Policy protects you for as long as you or your heirs have an interest in the property. Most lenders usually require a Loan Policy when they issue you a loan. The Loan Policy is usually based on the dollar amount of your loan and it only protects the lender's interests in the property should a problem with the title arise. It does not protect the buyer. The policy amount decreases each year and eventually disappears as the loan is paid off.

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