CLOSING HELP

(a.k.a. Seller Concessions)

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Title or ownership of real estate transfers at the time of successful settlement, sometimes referred to as "**closing**". Settlement or closing is normally the culmination of the effort of sellers, buyers, real estate agents, loan officers, underwriters, appraisers, inspectors (home, termite, roof, water and septic, etc.), insurance agents, settlement officers, and sometimes attorneys and others.

What is closing "**help**" then? It is money that the seller concedes from the proceeds of their sale that is credited to the buyers' closing costs at settlement. This concession is agreed to in the purchase agreement and is typically made based on the disclosure or pretext that the buyer would not otherwise have sufficient funds available to carry out the transaction.

Let's consider an example of a residential transaction for a buyer in Maryland and what their typical closing costs may be. The dollar amounts shown are purely fictional ballpark estimates of what actual costs will be in a real scenario. There are many variables, prorated costs, and other variations depending on location, date, vendors used, etc., etc.

Sale price:	$300,000
Down Payment:	$15,000 (5%)
Loan Amount:	$285,000
Closing help:	$9,000 (3%)
Loan term:	30 years
Interest Rate:	3.75%

Origination Charge: $1,000 (lender fee)

Credit Application Fee: $50

Underwriting Fee: $250

House Location Survey: $500

Appraisal Fee: $750

Flood Certification Fee: $100

Property Tax: $2,100 ($4,200 annually, $350/month – 6 months to escrow)

Transfer & Recordation Taxes: $2,250 (customary 50/50 split with seller)

Termite Inspection Fee: $200

Home Inspection Fee: $500

Recording Fees: $120 ($60 deed + $60 mortgage)

Title Insurance: $1,500

Broker Admin Fee: $400

Settlement Services: $500

(Closing Protection Letter, Document Processing/Prep Fee, Document Storage/Delivery Fee, Lender's Title Insurance, Settlement Fee, Title Binder Fee, Title Search Fee)

Homeowners Insurance: $600 ($100/month – 6 months to escrow)

HOA and/or Condo Fees: $100/month – sometimes more to escrow

Expenses shown in brown are closing costs that may be paid for by seller concession or closing help (a credit to the buyer and a debit to the seller on the closing/settlement statement, a.k.a. HUD-1). In this example, the total of these expenses is $10,920 – which is 3.64% of the sale price of $300,000. Therefore, since the closing help was $9,000, the buyer will have to come up with the difference of $1,920 + the down payment of $15,000.

Monthly Payment

Incidental to the discussion of closing help, here is a breakdown of the estimated monthly payment in this example:

Principal & Interest: $1,320 (PI)

Taxes & Insurance & Escrow*: $530 (TI)

Mortgage Insurance: $150 (I)

Estimated Total Monthly Payment $2,000 (PITII)

Generally speaking – when all is said and done, and depending on specific factors of loan amount, credit scores, interest rates, loan term, property taxes, homeowner insurance cost, mortgage insurance, etc. – total monthly payments (PITI) can be roughly guestimated at between $5 and $7 per thousand dollars of loan amount. In this example: $2,000 divided by $285,000 = $7.02/thousand. This example is designed to be on the high end of likely costs – worst case scenario (except for the interest rate).

*Escrow (as used here) refers to possible (or likely) required advance contribution of monies to pay property taxes and possibly other assessments, insurances and association dues. These obligations are managed and paid for by the loan servicing company. Depending on the amount of equity in the deal, borrowers may be able to petition the mortgage company to be allowed to pay for these expenses.

Limits on Closing Help

Home purchase closing costs vary from about two to five or six percent. As seen in the above example, that can be a significant amount of money to have available to purchase a home. The amount of closing help on any transaction is totally negotiable between the seller and buyer. In theory, it should be based on what the actual closing costs are likely to be – but not necessarily. If there had been a surplus of money in the above example, it could have been applied to the down payment for the benefit of the buyer. Again, all that is negotiable – but it does need to be negotiated and agreed to in advance and in writing.

All that said, there are limits imposed on the maximum amount of closing help based on the type of financing, e.g. conventional, Federal Housing Administration (FHA), Veterans Administration (VA), and United States Department of Agriculture (USDA). These limits are pretty generous.

With conventional loans, the individual lender will have their own guidelines or rules. Sometimes they may allow up to 10% closing help. Fannie Mae and Freddie Mac are the two rule makers for conventional loans. They set maximum seller paid closing costs.

For all FHA loans, the seller and other interested parties can contribute up to 6% of the sales price or toward closing costs, prepaid expenses, discount points, and other closing costs. If the appraised home value is less than the purchase price, the seller may contribute 6% of the value.

With VA loans, the seller may contribute up to 4% of the sale price, plus reasonable and customary loan costs. Total contributions may exceed 4% because standard closing costs do not count toward the total. According to VA guidelines, the 4% rule only applies to items such as:

- prepayment of property taxes and insurance
- appliances and other gifts from the builder
- discount points above 2% of the loan amount
- payoff of the buyer’s judgments and debts
- payment of the VA funding fee

USDA loan guidelines state that the seller may contribute up to 6% of the sales price toward the buyer’s reasonable closing costs.

So far, this discussion may seem to suggest that the amount of closing help is necessarily a percentage of the sale price. For the purpose of ensuring that the above limits are not exceeded, the percentage has to be calculated. But, the amount requested and agreed to can just be a simple flat sum of money – say, $5,000 – or any other amount mutually agreed upon. In the above example, that would happen to work out to 1.67% of the sale price – which would be fine.

Interested Party Contributions

Seller paid costs fall within a broader category of real estate related funds called interested party contributions or IPCs. These costs are contributions that incentivize the home buyer to buy that particular home. IPCs are OK up to a certain dollar amount, but above that they are not allowed.

Who is considered an interested party? Your real estate agent, the home builder, and of course the home seller. Even funds from down payment assistance programs are considered IPCs if the funds originate from the seller and run through a non-profit.

Anyone who might benefit from the sale of the home is considered an interested party, and their contribution to the buyer is limited.

Fannie Mae B3-4.1-02: Interested Party Contributions (IPCs) (06/28/2016)

https://www.fanniemae.com/content/guide/selling/b3/4.1/02.html

Overview

Interested party contributions (IPCs) are costs that are normally the responsibility of the property purchaser that are paid directly or indirectly by someone else who has a financial interest in, or can influence the terms and the sale or transfer of, the subject property.

Interested parties to a transaction include, but are not limited to, the property seller, the builder/developer, the real estate agent or broker, or an affiliate who may benefit from the sale of the property and/or the sale of the property at the highest price possible. A lender or employer is not considered an interested party to a sales transaction unless it is the property seller or is affiliated with the property seller or another interested party to the transaction. (For Fannie Mae's purposes, an affiliation exists when there is direct common ownership or control by the lender over the *interested party or vice versa, or when there is direct common ownership or control by a third party over both the lender and the interested party. A typical ongoing business relationship — for example, the relationship between a builder and a lender that serves as its financial institution — does not constitute an affiliation.)*

IPCs are either financing concessions or sales concessions. Fannie Mae considers the following to be IPCs:

- *funds that are paid directly from the interested party to the borrower;*
- *funds that flow from an interested party through a third-party organization, including nonprofit entities, to the borrower;*
- *funds that flow to the transaction on the borrower's behalf from an interested party, including a third-party organization or nonprofit agency; and*
- *funds that are donated to a third party, which then provides the money to pay some or all of the closing costs for a specific transaction.*

See B3-4.1-03, Types of Interested Party Contributions (IPCs), for more information.

Fannie Mae does not permit IPCs to be used to make the borrower's down payment, meet financial reserve requirements, or meet minimum borrower contribution requirements.

IPC Limits

The table below provides IPC limits for conventional mortgages.

IPCs that exceed these limits are considered sales concessions. The property's sales price must be adjusted downward to reflect the amount of contribution that exceeds the maximum, and the maximum LTV/CLTV ratios must be recalculated using the reduced sales price or appraised value.

Occupancy Type	*LTV/CLTV Ratio Maximum*	*IPC*
Principal residence or second home	*Greater than 90%*	*3%*[1]
	75.01% – 90%	*6%*
	75% or less	*9%*
Investment property	*All CLTV ratios*	*2%*

Lender Checklist for IPCs

The lender must ensure that all of the following requirements for an IPC are satisfied.

✓ ***Lender Checklist for IPCs***

- *Ensure that any and all IPCs have been identified and taken into consideration.*
- *Provide the appraiser with all appropriate financing data and IPCs for the subject property granted by anyone associated with the transaction.*
- *Ensure that the property value is adequately supported.*
- *Ensure that the LTV and CLTV ratios, after any IPCs are taken into consideration, remain within Fannie Mae's eligibility limits for the particular product.*
- *Ensure that mortgage insurance coverage, if applicable, has been obtained, based on the LTV ratio after any IPC adjustments have been made.*
- *Scrutinize all loan and sales contract documents, including but not limited to the sales contract, the loan estimate, the Uniform Residential Loan Application (Form 1003 or Form 1003(S)) (particularly Section VII, Details of Transaction), the appraisal report, and the settlement statement.*
- *Ensure that all elements of the settlement statement were taken into consideration during the underwriting process.*

- *Ensure that fees and expenses are consistent between all documents. Analyze any differences and review any discrepancies.*

Lender Incentives for Borrowers

Cash or Cash-like Incentives for all Transaction Types: The lender may provide the borrower with a cash or cash-like (e.g., a gift card) incentive that is not reflected on the settlement statement provided that

- *the amount of the incentive does not exceed $500, and*
- *no repayment is required.*

Because the lender is not typically a party to the sales transaction, these types of lender incentives are not considered IPCs and, as a result, are not included in the IPC limit calculation. Furthermore, these incentives are not considered cash out to the borrower and do not have to be included in the cash back to borrower at closing calculation.

Note: Documentation of compliance with this policy will not be required at the loan level. However, the lender must establish policies and/or procedures to ensure that the loans with these types of incentives that it delivers to Fannie Mae, whether or not the loans were originated by the lender, are in compliance with this policy.

Pay Down of Existing Mortgage Balance for Eligible Refinance Transactions: For DU Refi Plus and Refi Plus transactions, the lender may provide an incentive to the borrower in the form of a payment to pay off a portion of the mortgage loan being refinanced provided that

- *the amount of the incentive does not exceed $2,000,*
- *no repayment is required, and*
- *the payment is reflected on the settlement statement as a lender credit.*

Because these are refinance transactions, the incentive is not considered an IPC and, as a result, is not included in the IPC limit calculation. Furthermore, this incentive is not considered cash out to the borrower and it does not have to be included in the cash back to borrower at closing calculation.

Related Announcements

The table below provides references to the Announcements that have been issued that are related to this topic.

Announcements	Issue Date
Announcement SEL-2016–05	June 28, 2016
Announcement SEL-2014–07	June 24, 2014
Announcement SEL-2013–03	April 9, 2013
Announcement SEL-2010–06	April 30, 2010
Announcement 09-37	December 30, 2009

1 See B5-4-03, Loans Secured by HomePath Properties for an exception to this limit for principal residence transactions.

DISCLAIMER

John P. Hale is a licensed real estate agent in Maryland and Pennsylvania. He is affiliated with Coldwell Banker Residential Brokerage in Westminster, Maryland. John has been licensed since 2000 and also practiced in Tucson, Arizona for many years. Mr. Hale holds the following designations and certifications awarded by the National Association of REALTORS® (NAR) and other authorized institutions: ABR-Accredited Buyers Representative, AHWD-At Home With Diversity, CNE-Certified Negotiation Expert, CRMS-Certified Risk Management Specialist, CRS-Certified Residential Specialist, CTA-Certified Tourism Ambassador, e-PRO-Online Real Estate Practice, GRI-Graduate of Realtor Institute, MRE-Master of Real Estate, MREP-Mortgage Real Estate Professional, and MRP-Military Relocation Professional.

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