The Homebuyer Financial Guide

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Introduction

Congratulations! You have taken the first step in getting your finances in order with the goal of buying your first home, building or buying your dream home or investing in real estate.

At Prosperwell Financial, our mission is to coach, mentor and inspire you to achieve financial independence and happiness and we would love to help you with your investing and financial planning. In addition to helping you with your financial planning, we are here to help you with any of the following:

- A complimentary asset allocation review of any investments. You can send us your investment account statements and we will give you an analysis and our opinion at no cost.
- Analyzing your insurance such as Life, Disability and Long-Term Care Insurance. We can review your current policies or get you quotes for a new policy. We can also help you analyze the proper amount of insurance.
- Send us your Social Security statement for a Social Security Analysis.
- Establishing a college savings account for your child or grandchild.
- Setting up a 401(k), Simple IRA or SEP IRA for your business.
- Discuss available options for your old 401(k) accounts.
- Charitable Giving and Donor Advised Funds.

If you have any questions about the information in this packet, would like a second opinion on your investments or would like to start planning for your future, please call us at 763-231-9510 or reach out via our website at www.prosperwell.com.

Sincerely,

Nicole

Nicole N. Middendorf, CDFA
CEO, Prosperwell Financial
Wealth Advisor, RJFS

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Buying a Home Checklist

- ☐ Determine how much you can afford
- ☐ Set a budget
- ☐ Save for a down payment
- ☐ Find a Real Estate Agent you trust
- ☐ Get a mortgage pre-approval and choose a lender
- ☐ Find the perfect home for you
- ☐ Make a smart purchase offer
- ☐ Schedule a home inspection and appraisal
- ☐ Prepare for closing
- ☐ Close on your new home

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How Much Can You Afford?

If you have the desire to buy a home, you want to make sure that you can truly afford that home. First, you need to know that you can afford it from a monthly cash flow standpoint. Second, you need to be sure that purchasing a new home makes sense with your financial plan.

At a minimum, when you buy a home, you want to put at least 20% down as your down payment. Although there are loan options that do not require this, it is not recommended to go any lower on your down payment. The down payment is money you need to have set aside in cash. You do NOT want to borrow this money from your retirement savings.

The reason you want to put the 20% down on your home, is not only so that you have equity from the beginning, but also so you do not need to pay PMI. PMI is Private Mortgage Insurance. This is an extra cost and it is required when putting any less down than 20% when taking out your mortgage. This expense is unnecessary and if you have PMI, it means you truly cannot afford that home. Instead you should be looking to purchase a more affordable home, or waiting to save more money to hit the 20% mark by cutting your expenses.

In addition, you will want to establish a budget and make sure that you can afford not only the monthly mortgage payment, but also the utilities, property taxes, repairs and maintenance of that home. A good way of figuring out if this amount each month is manageable, is to estimate the costs and put that money away for six months into a savings account prior to buying the home.

Buying a home is a large purchase and there are several other factors to consider such as:

1. Job Security. This is extremely important. Just because you graduated from college and got a job does not necessarily mean you have job security.
2. Low Debt. When applying for a mortgage, lenders will access your ability to pay the loan based on your debt-to-income ratio. If you have excessive debt due to student loans, credit cards, personal loans, you are more likely to receive a higher interest rate and are faced with the possibility of not being approved for the loan.
3. Be realistic with what you can afford. What you want and what you can afford might be two different things. Be realistic and set your priorities before you begin shopping for your new home.
4. Budgeting. Develop a budget and stick to it before making the purchase. You want to make sure you can stick to your monthly allocations beforehand because it will likely only get harder once you buy the home.

Buying a home can be an exciting time, but you want to do it when you are financially prepared. If you are ready to start looking for homes and would like a referral to a realtor and/or mortgage broker, please let us know.

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Debt and Cash Flow

Budgeting. That dreaded word. Most of the American population does not have a budget. Budgeting is not fun but something that we believe is extremely important. When you have a budget, you spend money on the things you truly need and want. You spend money consciously and truly where you want your money to go.

Do you often wonder where all your money goes? Having a budget and tracking where your money goes can be very beneficial to achieving your financial goals. We often do not realize how all of the little things add up. A coffee here and a dinner there all add up and take away from money you could be saving. Have you ever had a $20, $50, or $100 bill in your pocket and a couple days (or hours) later it is gone and you don’t have anything to show for it? Tracking what you spend for a month or couple of weeks could be an eye-opening experience. You might see some things that you don’t necessarily need and could eliminate from your monthly expenses. All those little amounts combined could be saved and put toward achieving your financial goals for the future. So, this month try to track your spending and see if you need everything you buy.

There is truly a difference between a want and a need. You want to really stop and ponder before you buy something and determine if it is a want or a need. We have a budget worksheet that we have developed over the years to help you with your budget. The easiest way is to take this budget worksheet and to start from today forward and truly write down everything you spend.

On the following pages, we have developed a budget worksheet for you. On of the best ways to develop a budget to track all your expenses for the current month. Set a timer for 15 minutes and work on it for 15 minutes at a time. When it is complete, send it to us and we can give you some ideas as well as to where you can cut back on your expenses. Completing this budget worksheet is the first step in awareness of where you are spending money and you may be able to find areas to cut back.

One tip that I love to share with homebuyers is to pretend you have the house now. So, if right now your current rent or mortgage is $2,000 a month and the new house would be $3,000, pretend you already are in that home. So, you would pay your current payment, but add that extra $1,000 each month to your savings. Do this for six months to see how it works and if you can in fact afford the home. The worst-case scenario is that you have an extra $6,000 in your savings at the end of the six months.

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Budget Worksheet

Expenses:

Living Expenses:

Mortgage/Rent: ________________
Heloc: ________________
2nd Property: ________________
Investment Prop: ________________
Home Insurance: ________________
Property Taxes: ________________
Assessment: ________________
Condo Fees: ________________
Dining Out: ________________
Lunch at Work: ________________
Groceries: ________________
Bedding/Linens: ________________
Pet Expenses: ________________
Postage: ________________
________________ ________________
________________ ________________

Home Maintenance Expenses:

Furniture: ________________
Interior Repairs: ________________
Home Supplies: ________________
House Cleaning: ________________
Decorating: ________________
Lawn Mowing: ________________
Landscaper: ________________
Snow Blowing: ________________
Furnace Filters: ________________
Garbage: ________________
Security System: ________________
Water Softener Salt: ________________
Tree Trimming: ________________
Spring/Fall Cleanup: ________________
House Painting: ________________
Gardening: ________________
Plumber: ________________
Room Maintenance: ________________
Irrigation: ________________
Pest Maintenance: ________________
Water System: ________________
________________ ________________
________________ ________________

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Personal Expenses:

Clothing: ________________
Hosiery: ________________
Shoes: ________________
Haircuts: ________________
Beauty Salon: ________________
Jewelry: ________________
Beauty Supplies: ________________
Massage: ________________
Manicure/Pedicure: ________________
Alterations/Repairs: ________________
Dry Cleaning: ________________
Spousal Maintenance: ________________
Personal Trainer: ________________
________________ ________________
________________ ________________

Utilities:

Electricity: ________________
Gas: ________________
Water: ________________
Phone: ________________
Cable TV: ________________
Cell Phone: ________________
Long Distance: ________________
Pager: ________________
Voicemail: ________________
DSL/Internet: ________________
Sewer/Septic: ________________
Firewood: ________________
________________ ________________
________________ ________________

Transportation:

Car Loan/Lease: ________________
Gas: ________________
Car Insurance: ________________
Vehicle Tabs: ________________
Car Washes: ________________
Oil Changes: ________________
Parking: ________________
Maintenance: ________________

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Repairs: ________________
Bus Pass: ________________
Bikes: ________________
Car Savings: ________________
________________ ________________
________________ ________________

Medical:

Doctor Visits: ________________
Health Insurance: ________________
Eyeglasses/contacts: ________________
Dental: ________________
Medications: ________________
Medicare Supplements: ________________
LTC Insurance: ________________
Life Insurance: ________________
Disability Insurance: ________________
Vitamins: ________________
Non-Reimbursable: ________________
________________ ________________
________________ ________________

Recreation:

Hobbies: ________________
Relaxation: ________________
Sport Activities: ________________
Vacation: ________________
Theatre: ________________
Sports Events: ________________
Movies: ________________
Entertainment: ________________
Home Entertaining: ________________
Boat Expenses: ________________
Boat Insurance: ________________
Watercraft Expenses: ________________
Watercraft Insurance: ________________
Pool Expenses: ________________

Memberships:

AAA: ________________
Golf Club: ________________
Country Club: ________________
Sam's Club: ________________
Costco: ________________
Golf League: ________________
Bowling League: ________________

Other Leagues: ________________
Health/Fitness Club: ________________
Fish/Hunt Licenses: ________________
Union Dues: ________________
________________ ________________
________________ ________________

Debit/Credit Cards:

________________ ________________
________________ ________________
________________ ________________
________________ ________________
________________ ________________

Savings:

401k/457/403b: ________________
Roth/Traditional IRA: ________________
Deferred Comp: ________________
Liquid Money: ________________
VUL Insurance: ________________
Annuity: ________________
Spending Money: ________________
529/Ed IRA/UTMA: ________________
________________ ________________
________________ ________________

Miscellaneous:

School Expenses: ________________
Paper/copies: ________________
Laundry: ________________
Cards/Gifts: ________________
Donations: ________________
Travel: ________________
Cigarettes: ________________
Alcohol: ________________
Magazines: ________________
Books: ________________
Accountant Fees: ________________
Financial Fees: ________________
Attorney Fees: ________________
Income Taxes: ________________
Safe Deposit Box: ________________

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Newspapers: _______________
Agent Fees: _______________
Promotion Fees: _______________
_______________ _______________
_______________ _______________

Kids Expenses:

Clothing: _______________
Shoes: _______________
Food: _______________
Transportation: _______________
School Expenses: _______________
Cell Phone: _______________
Lunch Money: _______________
Personal Supplies: _______________
Haircuts: _______________
Babysitter: _______________
Nanny: _______________
Child Support: _______________
Day Care: _______________
Diapers: _______________
Diaper Service: _______________
Medical: _______________
Summer Camp: _______________
Activities: _______________
Lessons: _______________
Parenting Consultant: _______________
Supervision: _______________
Allowance: _______________
_______________ _______________
_______________ _______________

TOTALS:

Total Income: _______________
Total Expenses: _______________
Income minus Expenses: _______________

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Everything You Need to Know About A Mortgage

Typically, when buying a home, it will involve a mortgage. Here are five tips to help guide you through the process of applying for a mortgage:

1. Getting Pre-qualified
   When looking for a mortgage, you want to research rates and terms that various lenders offer. Once you have settled on a mortgage broker, the first step is to get pre-qualified (or pre-approved) for the mortgage. This will give you an estimate of how much you will be approved of in order to make your home purchase. However, this does not guarantee that the lender will grant you the loan. It is not uncommon for someone to get pre-qualified for a certain amount but then does not get final approval. Also, just because you pre-qualify for a certain amount, does not mean that you can afford that amount. Keep in mind that before making an offer on a home, you will need to be pre-qualified. Many times, the pre-approval letter will need to accompany your written offer on the home.

2. A general guide is that when you are looking at a conventional mortgage, your monthly housing expenses which consist of the mortgage payment, real estate taxes and homeowner's insurance should not exceed 28 percent of your gross monthly income.

3. Applying for a Mortgage
   When going through the approval process, your lender will need a lot of information from you (and your spouse if applicable) to determine your eligibility of the loan. You will want to organize and collect:
   1. Bank statements for the last 3 months minimum.
   2. Investment statements for the last 3 months minimum.
   3. Pay stubs, W-2 withholding forms or other proof of employment and income.
   4. Tax Returns and/or Balance sheets.
   5. Information on your debt (student loans, vehicle, personal loans, credit cards, etc).

4. Types of Mortgages
   There are a variety of different types of mortgages. The type of mortgage that is right for you will depend on several factors, this is something that your mortgage broker will help you determine. The following are some popular types of mortgages available:
   1. Conventional fixed rate mortgage. With this type of mortgage, your interest rate will not change over the life of your loan. Typically they range from 10-30 years.
   2. Adjustable rate mortgages (ARM). With an ARM, your interest rate will periodically adjust.
   3. Government mortgages (FHA or VA mortgage loans). These loans have specific guidelines that you must have in order to use them.
   4. Hybrid adjustable rate mortgage (ARM). This mortgage will have an initial fixed rate period followed by an adjustable rate period.
   5. Jumbo loans. This is a home loan for an amount that exceeds the "conforming loan limit."

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Real Estate Investing

Investing in real estate goes well beyond buying a home; for we all need a place to live. I would not classify home ownership as investing. In fact, did you know that there are twenty-two different types of real estate? You could purchase a duplex, commercial building, second home, apartment complex or a REIT, etc. If your allocation makes sense to add real estate, you could look at a REIT.

What is a REIT? It stands for Real Estate Investment Trust. A REIT lets you invest in real estate as part of a group. It's a trust that owns a variety of buildings and various different types of real estate without you as an individual owning one particular building. Instead, you own pieces of a lot of different types of real estate.

Investing in real estate, or REITs, involves special risks such as potential illiquidity and may not be suitable for all investors. Illiquidity is where your money is not accessible. It is tied up and the money is not liquid and so you cannot get at the money. There is no assurance the investment objectives of REITs will be attained.

If you want to own the actual property, it is recommended to look at a 100 properties before you find that diamond in the rough. Historically, you earn 3-4% on Real Estate. That is simply inflation. But you can buy a property as an investment to increase your cash flow. For example, if you buy a $200,000 duplex to start with a 15-year mortgage and 20% down payment. This would mean you need $40,000 in cash to buy the house and assuming you have a 4% interest rate, your mortgage payment each month would be $1,184 plus the cost of homeowner's insurance and property taxes if you escrow. For if you make your payments then after 15 years this property will be paid for. Those that are living in it will continue to pay rent to you. But now with the house paid for you can get some income. You will continue pay for the maintenance and taxes of the property but the rest of the cashflow is now your income.

You then can let that income accumulate in a savings account and build up more cash so that you have more money for another down payment and you can buy another property. You can keep doing this to build your net worth.

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Real Estate Extras

In 1997, the tax code changed relating to home ownership. A married couple can exclude up to $500,000 of capital gain on a home sale and a single person can exclude up to $250,000 as long you have lived in the home for two out of the last five years. (Your capital gain is the bottom line profit you end up with after realtor fees, any improvements you have made to your home, after any liabilities and any other house expenses.) What this means is that if you take the house as part of the divorce and sell it one year later with a gain on your home sale of over $250,000 you will pay capital gains taxes.

On the other hand, if you sold the house pursuant to the divorce and had a capital gain of less than $500,000 there would have been no taxable gain. Let's look at a hypothetical example. Let's say you bought a house in 1975 for $200,000 and today it is worth $600,000 and you are selling the house as part of the divorce while you are married. You will have a gain of $400,000. So if you sell the house while being married you would not have to pay capital gains taxes for you have an exclusion of gain up to $500,000 as a married couple. Whereas, if you took the house as part of the divorce and sold it a year later as a single person you only have an exclusion of $250,000. So you would have to pay capital gains taxes on the difference of your gain of $400,000 (assuming the house 1 year later was still worth $400,000) and subtracting your $250,000 exclusion which would leave you with a gain of $150,000.

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Conclusion

Congratulations! Buying a new home or another property is big step for your financial future. We highly encourage you to keep on this path and re-evaluate your budget, cash flow and financial plan as your situation changes.

At Prosperwell Financial, we believe that life is not just about money, but instead it is about doing things that truly make you happy and living your life to the fullest. Our mission is to coach, mentor and inspire you to achieve financial independence and happiness. We would love the opportunity to work with you to help you achieve your goals, work towards what makes you happy and help you live your very best life.

If you are interested in meeting with one of our Wealth Advisors to help you get started on investing, rolling over your 401(k) or to get a second opinion on your investments, we would be happy to offer you a complimentary consultation. You can call our office at 763-231-9510 to schedule.

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