



The Federal Reserve Board

What you should know about Home Equity Lines of Credit

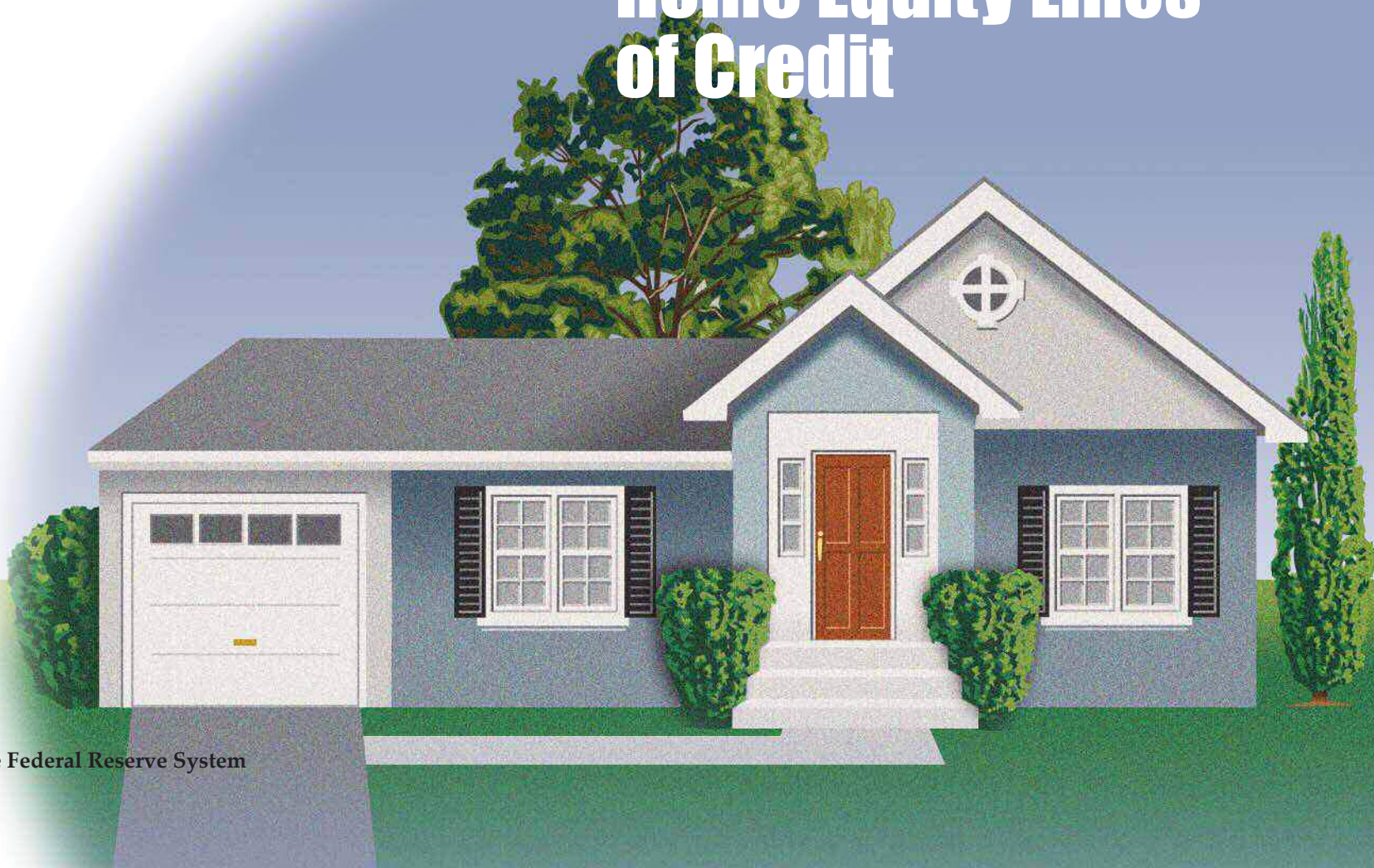


Table of contents

Home Equity Plan Checklist	2
What is a home equity line of credit?	3
What should you look for when shopping for a plan?	4
Costs of establishing and maintaining a home equity line	5
How will you repay your home equity plan?	6
Lines of credit vs. traditional second mortgage loans	8
What if the lender freezes or reduces your line of credit?	10
Glossary	A1
Where to go for help	A4
More resources	A7



If you are in the market for credit, a home equity plan is one of several options that might be right for you. Before making a decision, however, you should weigh carefully the costs of a home equity line against the benefits. Shop for the credit terms that best meet your borrowing needs without posing undue financial risks. And remember, failure to repay the amounts you've borrowed, plus interest, could mean the loss of your home.

Home Equity Plan Checklist

Ask your lender to help fill out this checklist.

Basic Features	Plan A	Plan B
Fixed annual percentage rate	%	%
Variable annual percentage rate	%	%
<ul style="list-style-type: none"> ■ Index used and current value 	%	%
<ul style="list-style-type: none"> ■ Amount of margin 		
<ul style="list-style-type: none"> ■ Frequency of rate adjustments 		
<ul style="list-style-type: none"> ■ Amount/length of discount (if any) 		
<ul style="list-style-type: none"> ■ Interest-rate cap and floor 		
Length of plan		
Draw period		
Repayment period		
Initial fees		
Appraisal fee		
Application fee		
Up-front charges, including points		
Closing costs		
Repayment Terms		
During the draw period		
Interest and principal payments		
Interest-only payments		
Fully amortizing payments		
When the draw period ends		
Balloon payment?		
Renewal available?		
Refinancing of balance by lender?		

What is a home equity line of credit?

A home equity line of credit is a form of revolving credit in which your home serves as collateral. Because a home often is a consumer's most valuable asset, many homeowners use home equity credit lines only for major items, such as education, home improvements, or medical bills, and choose not to use them for day-to-day expenses.

With a home equity line, you will be approved for a specific amount of credit. Many lenders set the credit limit on a home equity line by taking a percentage (say, 75%) of the home's appraised value and subtracting from that the balance owed on the existing mortgage. For example:

Appraised value of home	\$100,000
Percentage	x 75%
Percentage of appraised value	= \$ 75,000
Less balance owed on mortgage	– \$ 40,000
<hr/>	
Potential line of credit	\$ 35,000

In determining your actual credit limit, the lender will also consider your ability to repay the loan (principal and interest) by looking at your income, debts, and other financial obligations as well as your credit history.

Many home equity plans set a fixed period during which you can borrow money, such as 10 years. At the end of this "draw period," you may be allowed to renew the credit line. If your

plan does not allow renewals, you will not be able to borrow additional money once the period has ended. Some plans may call for payment in full of any outstanding balance at the end of the period. Others may allow repayment over a fixed period (the “repayment period”), for example, 10 years.

Once approved for a home equity line of credit, you will most likely be able to borrow up to your credit limit whenever you want. Typically, you will use special checks to draw on your line. Under some plans, borrowers can use a credit card or other means to draw on the line.

There may be other limitations on how you use the line. Some plans may require you to borrow a minimum amount each time you draw on the line (for example, \$300) or keep a minimum amount outstanding. Some plans may also require that you take an initial advance when the line is set up.

What should you look for when shopping for a plan?

If you decide to apply for a home equity line of credit, look for the plan that best meets your particular needs. Read the credit agreement carefully, and examine the terms and conditions of various plans, including the annual percentage rate (APR) and the costs of establishing the plan. Remember, though, that the APR for a home equity line is based on the interest rate alone and will not reflect closing costs and other fees and charges, so you’ll need to compare these costs, as well as the APRs, among lenders.

Variable interest rates

Home equity lines of credit typically involve variable rather than fixed interest rates. The variable rate must be based on a publicly available index (such as the prime rate published in some major

daily newspapers or a U.S. Treasury bill rate). In such cases, the interest rate you pay for the line of credit will change, mirroring changes in the value of the index. Most lenders cite the interest rate you will pay as the value of the index at a particular time, plus a “margin,” such as 2 percentage points. Because the cost of borrowing is tied directly to the value of the index, it is important to find out which index is used, how often the value of the index changes, and how high it has risen in the past. It is also important to note the amount of the margin.

Lenders sometimes offer a temporarily discounted interest rate for home equity lines—an “introductory” rate that is unusually low for a short period, such as 6 months.

Variable-rate plans secured by a dwelling must, by law, have a ceiling (or cap) on how much your interest rate may increase over the life of the plan. Some variable-rate plans limit how much your payment may increase and how low your interest rate may fall if the index drops.

Some lenders allow you to convert from a variable interest rate to a fixed rate during the life of the plan, or let you convert all or a portion of your line to a fixed-term installment loan.

Costs of establishing and maintaining a home equity line

Many of the costs of setting up a home equity line of credit are similar to those you pay when you get a mortgage. For example:

- A fee for a property appraisal to estimate the value of your home;
- An application fee, which may not be refunded if you are turned down for credit;

- Up-front charges, such as one or more “points” (one point equals 1 percent of the credit limit); and
- Closing costs, including fees for attorneys, title search, mortgage preparation and filing, property and title insurance, and taxes.

In addition, you may be subject to certain fees during the plan period, such as annual membership or maintenance fees and a transaction fee every time you draw on the credit line.

You could find yourself paying hundreds of dollars to establish the plan. And if you were to draw only a small amount against your credit line, those initial charges would substantially increase the cost of the funds borrowed. On the other hand, because the lender’s risk is lower than for other forms of credit, as your home serves as collateral, annual percentage rates for home equity lines are generally lower than rates for other types of credit. The interest you save could offset the costs of establishing and maintaining the line. Moreover, some lenders waive some or all of the closing costs.

How will you repay your home equity plan?

Before entering into a plan, consider how you will pay back the money you borrow. Some plans set a minimum monthly payment that includes a portion of the principal (the amount you borrow) plus accrued interest. But, unlike with typical installment loan agreements, the portion of your payment that goes toward principal may not be enough to repay the principal by the end of the term. Other plans may allow payment of *interest only* during the life of the plan, which means that you pay nothing toward the principal. If you borrow \$10,000, you will owe that amount when the payment plan ends.

Regardless of the minimum required payment on your home equity line, you may choose to pay more, and many lenders offer a choice of payment options. Many consumers choose to pay down the principal regularly as they do with other loans. For example, if you use your line to buy a boat, you may want to pay it off as you would a typical boat loan.

Whatever your payment arrangements during the life of the plan—whether you pay some, a little, or none of the principal amount of the loan—when the plan ends, you may have to pay the entire balance owed, all at once. You must be prepared to make this “balloon payment” by refinancing it with the lender, by obtaining a loan from another lender, or by some other means. If you are unable to make the balloon payment, you could lose your home.

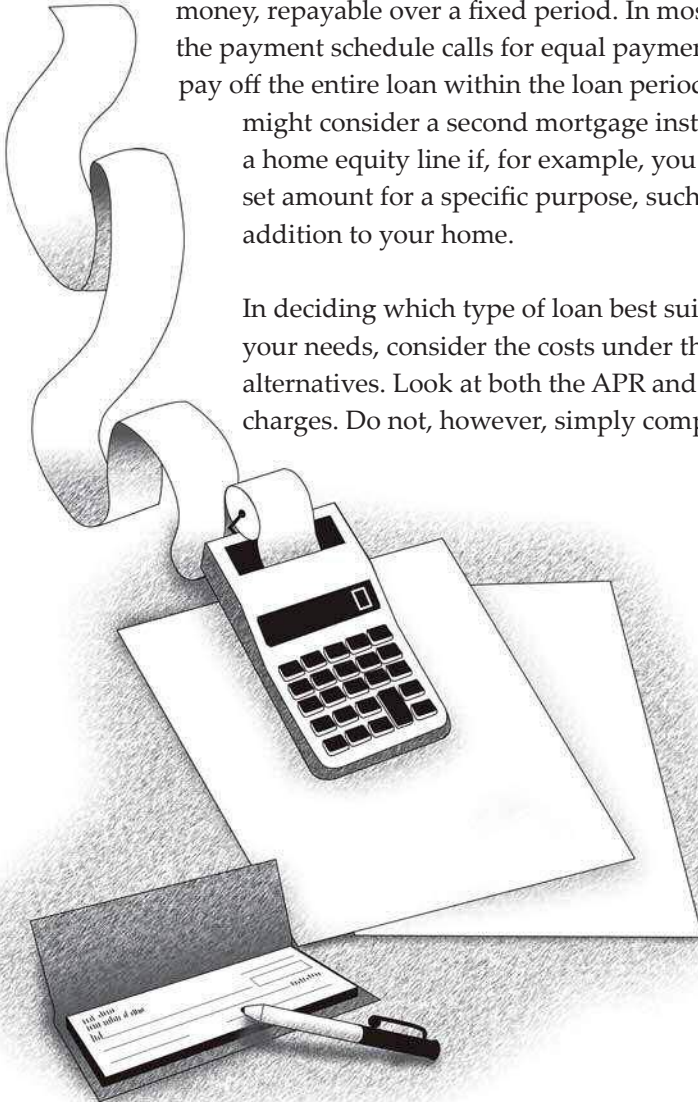
If your plan has a variable interest rate, your monthly payments may change. Assume, for example, that you borrow \$10,000 under a plan that calls for interest-only payments. At a 10% interest rate, your monthly payments would be \$83. If the rate rises over time to 15%, your monthly payments will increase to \$125. Similarly, if you are making payments that cover interest plus some portion of the principal, your monthly payments may increase, unless your agreement calls for keeping payments the same throughout the plan period.

If you sell your home, you will probably be required to pay off your home equity line in full immediately. If you are likely to sell your home in the near future, consider whether it makes sense to pay the up-front costs of setting up a line of credit. Also keep in mind that renting your home may be prohibited under the terms of your agreement.

Lines of credit vs. traditional second mortgage loans

If you are thinking about a home equity line of credit, you might also want to consider a traditional second mortgage loan. This type of loan provides you with a fixed amount of money, repayable over a fixed period. In most cases, the payment schedule calls for equal payments that pay off the entire loan within the loan period. You might consider a second mortgage instead of a home equity line if, for example, you need a set amount for a specific purpose, such as an addition to your home.

In deciding which type of loan best suits your needs, consider the costs under the two alternatives. Look at both the APR and other charges. Do not, however, simply compare



the APRs, because the APRs on the two types of loans are figured differently:

- The APR for a traditional second mortgage loan takes into account the interest rate charged plus points and other finance charges.
- The APR for a home equity line of credit is based on the periodic interest rate alone. It does not include points or other charges.

Disclosures from lenders

The federal Truth in Lending Act requires lenders to disclose the important terms and costs of their home equity plans, including the APR, miscellaneous charges, the payment terms, and information about any variable-rate feature. And in general, neither the lender nor anyone else may charge a fee until after you have received this information. You usually get these disclosures when you receive an application form, and you will get additional disclosures before the plan is opened. If any term (other than a variable-rate feature) changes before the plan is opened, the lender must return all fees if you decide not to enter into the plan because of the change.

When you open a home equity line, the transaction puts your home at risk. If the home involved is your principal dwelling, the Truth in Lending Act gives you 3 days from the day the account was opened to cancel the credit line. This right allows you to change your mind for any reason. You simply inform the lender in writing within the 3-day period. The lender must then cancel its security interest in your home and return all fees—including any application and appraisal fees—paid to open the account.

What if the lender freezes or reduces your line of credit?

Plans generally permit lenders to freeze or reduce a credit line if the value of the home “declines significantly” or, when the lender “reasonably believes” that you will be unable to make your payments due to a “material change” in your financial circumstances. If this happens, you may want to:

- **Talk with your lender.** Find out what caused the lender to freeze or reduce your credit line and what, if anything, you can do to restore it. You may be able to provide additional information to restore your line of credit, such as documentation showing that your house has retained its value or that there has not been a “material change” in your financial circumstances. You may want to get copies of your credit reports (go to the Federal Trade Commission’s website, at www.ftc.gov/freereports, for information about free copies) to make sure all the information in them is correct. If your lender suggests getting a new appraisal, be sure you discuss appraisal firms in advance so that you know they will accept the new appraisal as valid.
- **Shop around for another line of credit.** If your lender does not want to restore your line of credit, shop around to see what other lenders have to offer. You may be able to pay off your original line of credit and take out another one. Keep in mind, however, that you may need to pay some of the same application fees you paid for your original line of credit.

Glossary

Annual membership or maintenance fee

An annual charge for access to a financial product such as a line of credit, credit card, or account. The fee is charged regardless of whether or not the product is used.

Annual percentage rate (APR)

The cost of credit, expressed as a yearly rate. For closed-end credit, such as car loans or mortgages, the APR includes the interest rate, points, broker fees, and other credit charges that the borrower is required to pay. An APR, or an equivalent rate, is not used in leasing agreements.

Application fee

Fees charged when you apply for a loan or other credit. These fees may include charges for property appraisal and a credit report.

Balloon payment

A large extra payment that may be charged at the end of a mortgage loan or lease.

Cap (interest rate)

A limit on the amount that your interest rate can increase. Two types of interest-rate caps exist. *Periodic adjustment caps* limit the interest-rate increase from one adjustment period to the next. *Lifetime caps* limit the interest-rate increase over the life of the loan. By law, all adjustable-rate mortgages have an overall cap.

Closing or settlement costs

Fees paid when you close (or settle) on a loan. These fees may include application fees; title examination, abstract of title, title

insurance, and property survey fees; fees for preparing deeds, mortgages, and settlement documents; attorneys' fees; recording fees; estimated costs of taxes and insurance; and notary, appraisal, and credit report fees. Under the Real Estate Settlement Procedures Act, the borrower receives a good faith estimate of closing costs within three days of application. The good faith estimate lists each expected cost as an amount or a range.

Credit limit

The maximum amount that may be borrowed on a credit card or under a home equity line of credit plan.

Equity

The difference between the fair market value of the home and the outstanding balance on your mortgage plus any outstanding home equity loans.

Index

The economic indicator used to calculate interest-rate adjustments for adjustable-rate mortgages or other adjustable-rate loans. The index rate can increase or decrease at any time. *See also* Selected Index Rates for ARMs over an 11-year Period (www.federalreserve.gov/pubs/arms/arms_english.htm) for examples of common indexes that have changed in the past.

Interest rate

The percentage rate used to determine the cost of borrowing money, stated usually as a percentage of the principal loan amount and as an annual rate.

Margin

The number of percentage points the lender adds to the index rate to calculate the ARM interest rate at each adjustment.

Minimum payment

The lowest amount that you must pay (usually monthly) to keep your account in good standing. Under some plans, the minimum payment may cover interest only; under others, it may include both principal and interest.

Points (also called discount points)

One point is equal to 1 percent of the principal amount of a mortgage loan. For example, if a mortgage is \$200,000, one point equals \$2,000. Lenders frequently charge points in both fixed-rate and adjustable-rate mortgages to cover loan origination costs or to provide additional compensation to the lender or broker. These points usually are paid at closing and may be paid by the borrower or the home seller, or may be split between them. In some cases, the money needed to pay points can be borrowed (incorporated in the loan amount), but doing so will increase the loan amount and the total costs. Discount points (also called discount fees) are points that you voluntarily choose to pay in return for a lower interest rate.

Security interest

If stated in your credit agreement, a creditor's, lessor's, or assignee's legal right to your property (such as your home, stocks, or bonds) that secures payment of your obligation under the credit agreement.

Transaction fee

Fee charged each time a withdrawal or other specified transaction is made on a line of credit, such as a balance transfer fee or a cash advance fee.

Variable rate

An interest rate that changes periodically in relation to an index, such as the prime rate. Payments may increase or decrease accordingly.

Where to go for help

For additional information or to file a complaint about a bank, savings and loan, credit union, or other financial institution, contact one of the following federal agencies, depending on the type of institution.

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Federal Reserve Consumer Help P.O. Box 1200 Minneapolis, MN 55480	Federally insured state-chartered bank members of the Federal Reserve System	(888) 851-1920 www.federalreserveconsumerhelp.gov
Consumer Financial Protection Bureau (CFPB) P.O. Box 4503 Iowa City, IA 52244	Insured depository institutions and credit unions (and their affiliates) with assets greater than \$10 billion, and nondepository institutions such as mortgage originators, mortgage brokers and servicers, larger participants of other financial services products, private education loan providers, and payday lenders	(855) 411-2372 www.consumerfinance.gov
Office of the Comptroller of the Currency (OCC) Customer Assistance Unit 1301 McKinney Street Suite 3450 Houston, TX 77010	National banks and federally chartered savings banks/associations	(800) 613-6743 www.occ.treas.gov www.helpwithmybank.gov
Federal Deposit Insurance Corporation (FDIC) Consumer Response Center 1100 Walnut Street, Box #11 Kansas City, MO 64106	Federally insured state-chartered banks that are not members of the Federal Reserve System	(877) ASK-FDIC or (877) 275-3342 www.fdic.gov www.fdic.gov/consumers

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Federal Housing Finance Agency (FHFA) Consumer Communications Constitution Center 400 7th Street, S.W. Washington, DC 20024	Fannie Mae, Freddie Mac, and the Federal Home Loan Banks	(202) 649-3811 www. fa.gov www. fa.gov/Default.aspx?Page=369
National Credit Union Administration (NCUA) Consumer Assistance 1775 Duke Street Alexandria, VA 22314-3428	Federally chartered credit unions	(800) 755-1030 www.ncua.gov www.mycreditunion.gov
Federal Trade Commission (FTC) Consumer Response Center 600 Pennsylvania Avenue, N.W. Washington, DC 20580	Finance companies, retail stores, auto dealers, mortgage companies and other lenders, and credit bureaus	(877) FTC-HELP or (877) 382-4357 www. c.gov www. c.gov/bcp
Securities and Exchange Commission (SEC) Complaint Center 100 F Street, N.E. Washington, DC 20549-0213	Brokerage firms, mutual fund companies, and investment advisers	(202) 551-6551 www.sec.gov www.sec.gov/complaint/question.shtml
Farm Credit Administration Office of Congressional and Public Affairs 1501 Farm Credit Drive McLean, VA 22102-5090	Agricultural lenders	(703) 883-4056 www.fca.gov
Small Business Administration (SBA) Consumer Affairs 409 3rd Street, S.W. Washington, DC 20416	Small business lenders	(800) U-ASK-SBA or (800) 827-5722 www.sba.gov

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Commodity Futures Trading Commission (CFTC) 1155 21st Street, N.W. Washington, DC 20581	Commodity brokers, commodity trading advisers, commodity pools, and introducing brokers	(866) 366-2382 www.cftc.gov/Consumer-Protection
U.S. Department of Justice (DOJ) Criminal Division 950 Pennsylvania Avenue, N.W. Washington, DC 20530	Fair lending and fair housing issues	(202) 514-3301 www.justice.gov/criminal
Department of Housing and Urban Development (HUD) Office of Fair Housing/Equal Opportunity 451 7th Street, S.W. Washington, DC 20410	Fair lending and fair housing issues	(800) 669-9777 www.hud.gov/complaints

More resources

For more resources on mortgages and other financial topics, visit www.federalreserve.gov/consumerinfo.



The Federal Reserve Board

Consumer Handbook on Adjustable-Rate Mortgages

Interest Rate

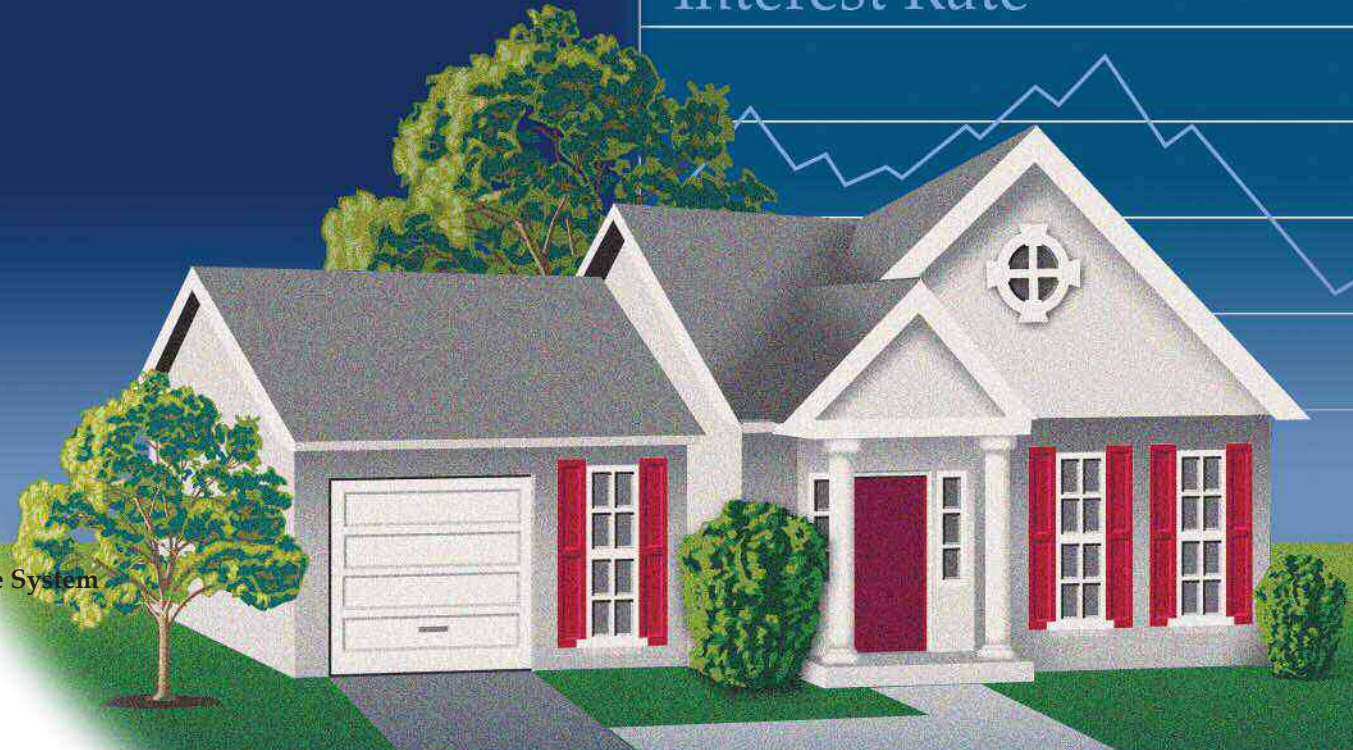


Table of contents

Mortgage shopping worksheet	2
What is an ARM?	4
How ARMs work: the basic features	6
Initial rate and payment	6
The adjustment period	6
The index	7
The margin	8
Interest-rate caps	10
Payment caps	13
Types of ARMs	15
Hybrid ARMs	15
Interest-only ARMs	15
Payment-option ARMs	16
Consumer cautions	19
Discounted interest rates	19
Payment shock	20
Negative amortization—when you owe more money than you borrowed	22
Prepayment penalties and conversion	24
Graduated-payment or stepped-rate loans	25
Where to get information	27
Disclosures from lenders	27
Newspapers and the Internet	28
Advertisements	28
Glossary	A1
Where to go for help	A6
More resources	A9

This information was prepared by the Board of Governors of the Federal Reserve System and the Office of Thrift Supervision in consultation with the following organizations:

AARP

American Association of Residential Mortgage Regulators

America's Community Bankers

Center for Responsible Lending

Conference of State Bank Supervisors

Consumer Federation of America

Consumer Mortgage Coalition

Consumers Union

Credit Union National Association

Federal Deposit Insurance Corporation

Federal Reserve Board's Consumer Advisory Council

Federal Trade Commission

Financial Services Roundtable

Independent Community Bankers Association

Mortgage Bankers Association

Mortgage Insurance Companies of America

National Association of Federal Credit Unions

National Association of Home Builders

National Association of Mortgage Brokers

National Association of Realtors

National Community Reinvestment Coalition

National Consumer Law Center

National Credit Union Administration



This handbook gives you an overview of ARMs, explains how ARMs work, and discusses some of the issues that you might face as a borrower. It

includes:

- ways to reduce the risks associated with ARMs;
- pointers about advertising and other sources of information, such as lenders and other trusted advisers;
- a glossary of important ARM terms; and
- a worksheet that can help you ask the right questions and figure out whether an ARM is right for you. (Ask lenders to help you fill out the worksheet so you can get the information you need to compare mortgages.)

An adjustable-rate mortgage (ARM) is a loan with an interest rate that changes. ARMs may start with lower monthly payments than fixed-rate mortgages, but keep in mind the following:

- Your monthly payments could change. They could go up—sometimes by a lot—even if interest rates don’t go up. See page 20.
- Your payments may not go down much, or at all—even if interest rates go down. See page 11.
- You could end up owing more money than you borrowed—even if you make all your payments on time. See page 22.
- If you want to pay off your ARM early to avoid higher payments, you might pay a penalty. See page 24.

You need to compare the features of ARMs to find the one that best fits your needs. The Mortgage Shopping Worksheet on page 2 can help you get started.

Mortgage shopping worksheet

Ask your lender or broker to help you fill out this worksheet.

Name of lender or broker and contact information
Mortgage amount
Loan term (e.g., 15 years, 30 years)
Loan description (e.g., fixed rate, 3/1 ARM, payment-option ARM, interest-only ARM)
Basic Features for Comparison
Fixed-rate mortgage interest rate and annual percentage rate (APR) (For graduated-payment or stepped-rate mortgages, use the ARM columns.)
ARM initial interest rate and APR How long does the initial rate apply? What will the interest rate be after the initial period?
ARM features How often can the interest rate adjust? What is the index and what is the current rate? (See chart on page 8.) What is the margin for this loan?
Interest-rate caps What is the periodic interest-rate cap? What is the lifetime interest-rate cap? How high could the rate go? How low could the interest rate go on this loan? What is the payment cap? Can this loan have negative amortization (that is, increase in size)? What is the limit to how much the balance can grow before the loan will be recalculated? Is there a prepayment penalty if I pay off this mortgage early? How long does that penalty last? How much is it? Is there a balloon payment on this mortgage? If so, what is the estimated amount and when would it be due? What are the estimated origination fees and charges for this loan?
Monthly Payment Amounts
What will the monthly payments be for the first year of the loan? Does this include taxes and insurance? Condo or homeowner's association fees? If not, what are the estimates for these amounts? What will my monthly payment be after 12 months if the index rate... ...stays the same? ...goes up 2%? ...goes down 2%? What is the most my minimum monthly payment could be after 1 year? What is the most my minimum monthly payment could be after 3 years? What is the most my minimum monthly payment could be after 5 years?

What is an ARM?

An adjustable-rate mortgage differs from a fixed-rate mortgage in many ways. Most importantly, with a fixed-rate mortgage, the interest rate stays the same during the life of the loan. With an ARM, the interest rate changes periodically, usually in relation to an index, and payments may go up or down accordingly.

To compare two ARMs, or to compare an ARM with a fixed-rate mortgage, you need to know about indexes, margins, discounts, caps on rates and payments, negative amortization, payment options, and recasting (recalculating) your loan. You need to consider the maximum amount your monthly payment could increase. Most importantly, you need to know what might happen to your monthly mortgage payment in relation to your future ability to afford higher payments.

Lenders generally charge lower initial interest rates for ARMs than for fixed-rate mortgages. At first, this makes the ARM easier on your pocketbook than would be a fixed-rate mortgage for the same loan amount. Moreover, your ARM could be less expensive over a long period than a fixed-rate mortgage—for example, if interest rates remain steady or move lower.

Against these advantages, you have to weigh the risk that an increase in interest rates would lead to higher monthly payments in the future. It's a trade-off—you get a lower initial rate with an ARM in exchange for assuming more risk over the long run. Here are some questions you need to consider:

- Is my income enough—or likely to rise enough—to cover higher mortgage payments if interest rates go up?
- Will I be taking on other sizable debts, such as a loan for a car or school tuition, in the near future?
- How long do I plan to own this home? (If you plan to sell soon, rising interest rates may not pose the problem they do if you plan to own the house for a long time.)
- Do I plan to make any additional payments or pay the loan off early?

Lenders and Brokers

Mortgage loans are offered by many kinds of lenders—such as banks, mortgage companies, and credit unions. You can also get a loan through a mortgage broker. Brokers “arrange” loans; in other words, they find a lender for you. Brokers generally take your application and contact several lenders, but keep in mind that brokers are not required to find the best deal for you unless they have contracted with you to act as your agent.

How ARMs work: the basic features

Initial rate and payment

The initial rate and payment amount on an ARM will remain in effect for a limited period—ranging from just 1 month to 5 years or more. For some ARMs, the initial rate and payment can vary greatly from the rates and payments later in the loan term. Even if interest rates are stable, your rates and payments could change a lot. If lenders or brokers quote the initial rate and payment on a loan, ask them for the annual percentage rate (APR). If the APR is significantly higher than the initial rate, then it is likely that your rate and payments will be a lot higher when the loan adjusts, even if general interest rates remain the same.

The adjustment period

With most ARMs, the interest rate and monthly payment change every month, quarter, year, 3 years, or 5 years. The period between rate changes is called the *adjustment period*. For example, a loan with an adjustment period of 1 year is called a 1-year ARM, and the interest rate and payment can change once every year; a loan with a 3-year adjustment period is called a 3-year ARM.

Loan Descriptions

Lenders must give you written information on each type of ARM loan you are interested in. The information must include the terms and conditions for each loan, including information about the index and margin, how your rate will be calculated, how often your rate can change, limits on changes (or *caps*), an example of how high your monthly payment might go, and other ARM features such as negative amortization.

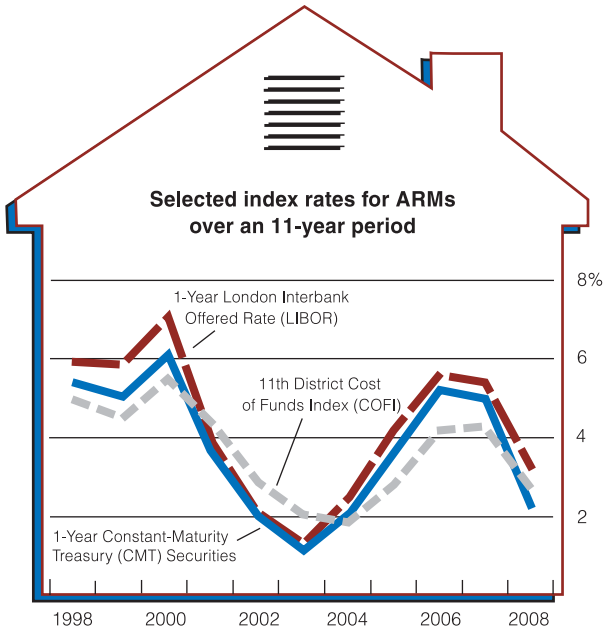
The index

The interest rate on an ARM is made up of two parts: the index and the margin. The index is a measure of interest rates generally, and the margin is an extra amount that the lender adds. Your payments will be affected by any caps, or limits, on how high or low your rate can go. If the index rate moves up, so does your interest rate in most circumstances, and you will probably have to make higher monthly payments. On the other hand, if the index rate goes down, your monthly payment could go down. Not all ARMs adjust downward, however—be sure to read the information for the loan you are considering.

Lenders base ARM rates on a variety of indexes. Among the most common indexes are the rates on 1-year constant-maturity Treasury (CMT) securities, the Cost of Funds Index (COFI), and the London Interbank Offered Rate (LIBOR). A few lenders use their own cost of funds as an index, rather than using other indexes. You should ask what index will be used, how it has fluctuated,

tuated in the past, and where it is published—you can find a lot of this information in major newspapers and on the Internet.

To help you get an idea of how to compare different indexes, the following chart shows a few common indexes over an 11-year period (1996–2008). As you can see, some index rates tend to be higher than others, and some change more often. But if a lender bases interest-rate adjustments on the average value of an index over time, your interest rate would not change as dramatically.



The margin

To set the interest rate on an ARM, lenders add a few percentage points to the index rate, called the *margin*. The amount of the margin may differ from one lender to another, but it is usually

constant over the life of the loan. The *fully indexed rate* is equal to the margin plus the index. If the initial rate on the loan is less than the fully indexed rate, it is called a *discounted index rate*. For example, if the lender uses an index that currently is 4% and adds a 3% margin, the fully indexed rate would be

Index	4%
+ Margin	3%
<hr style="width: 50%; margin-left: 0;"/>	<hr style="width: 50%; margin-left: 0;"/>
Fully indexed rate	7%

If the index on this loan rose to 5%, the fully indexed rate would be 8% (5% + 3%). If the index fell to 2%, the fully indexed rate would be 5% (2% + 3%).

Some lenders base the amount of the margin on your credit record—the better your credit, the lower the margin they add—and the lower the interest you will have to pay on your mortgage. In comparing ARMs, look at both the index and margin for each program.

No-Doc/Low-Doc Loans

When you apply for a loan, lenders usually require documents to prove that your income is high enough to repay the loan. For example, a lender might ask to see copies of your most recent pay stubs, income tax filings, and bank account statements. In a “no-doc” or “low-doc” loan, the lender doesn’t require you to bring proof of your income, but you will usually have to pay a higher interest rate or extra fees to get the loan. Lenders generally charge more for no-doc/low-doc loans.

Interest-rate caps

An interest-rate cap places a limit on the amount your interest rate can increase. Interest caps come in two versions:

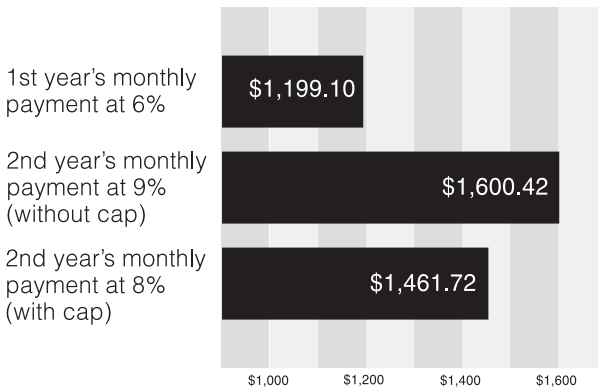
- *A periodic adjustment cap*, which limits the amount the interest rate can adjust up or down from one adjustment period to the next after the first adjustment, and
- *A lifetime cap*, which limits the interest-rate increase over the life of the loan. By law, virtually all ARMs must have a lifetime cap.

Periodic adjustment caps

Let's suppose you have an ARM with a periodic adjustment interest-rate cap of 2%. However, at the first adjustment, the index rate has risen 3%. The following example shows what happens.

Examples in This Handbook

All examples in this handbook are based on a \$200,000 loan amount and a 30-year term. Payment amounts in the examples do not include taxes, insurance, condominium or homeowner association fees, or similar items. These amounts can be a significant part of your monthly payment.



Difference in 2nd year between payment with cap and payment without = \$138.70 per month

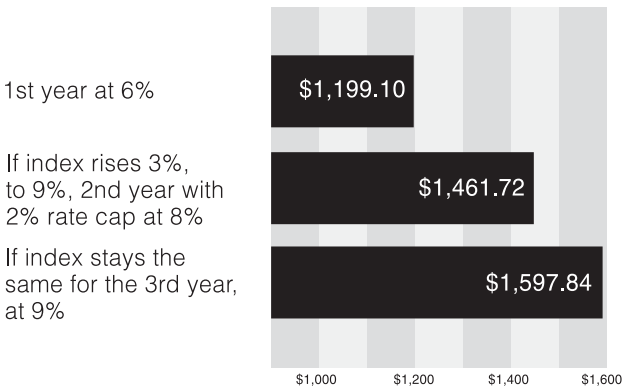
In this example, because of the cap on your loan, your monthly payment in year 2 is \$138.70 per month lower than it would be without the cap, saving you \$1,664.40 over the year.

Some ARMs allow a larger rate change at the first adjustment and then apply a periodic adjustment cap to all future adjustments.

A drop in interest rates does not always lead to a drop in your monthly payments. With some ARMs that have interest-rate caps, the cap may hold your rate and payment below what it would have been if the change in the index rate had been fully applied. The increase in the interest that was not imposed because of the rate cap might carry over to future rate adjustments. This is called *carryover*. So, at the next adjustment date, your payment might increase even though the index rate has stayed the same or declined.

The following example shows how carryovers work. Suppose the index on your ARM increased 3% during the first year.

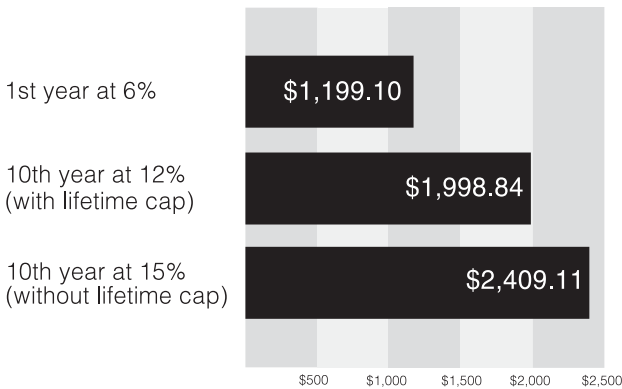
Because this ARM limits rate increases to 2% at any one time, the rate is adjusted by only 2%, to 8% for the second year. However, the remaining 1% increase in the index carries over to the next time the lender can adjust rates. So, when the lender adjusts the interest rate for the third year, even if there has been no change in the index during the second year, the rate still increases by 1%, to 9%.



In general, the rate on your loan can go up at any scheduled adjustment date when the lender’s standard ARM rate (the index plus the margin) is higher than the rate you are paying before that adjustment.

Lifetime caps

The next example shows how a lifetime rate cap would affect your loan. Let’s say that your ARM starts out with a 6% rate and the loan has a 6% lifetime cap—that is, the rate can never exceed 12%. Suppose the index rate increases 1% in each of the next 9 years. With a 6% overall cap, your payment would never exceed \$1,998.84—compared with the \$2,409.11 that it would have reached in the tenth year without a cap.

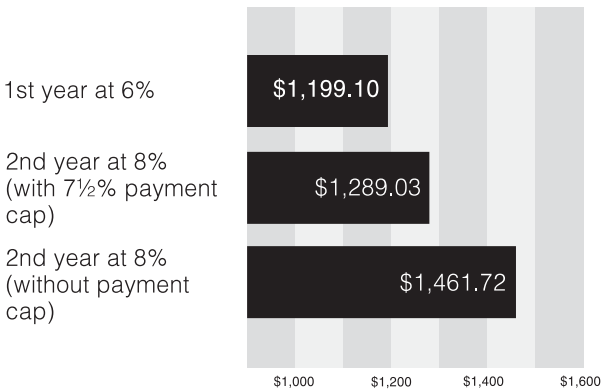


Payment caps

In addition to interest-rate caps, many ARMs—including payment-option ARMs (discussed on page 16)—limit, or cap, the amount your monthly payment may increase at the time of each adjustment. For example, if your loan has a payment cap of 7½%, your monthly payment won’t increase more than 7½% over your previous payment, even if interest rates rise more. For example, if your monthly payment in year 1 of your mortgage was \$1,000, it could only go up to \$1,075 in year 2 (7½% of \$1,000 is an additional \$75). Any interest you don’t pay because of the payment cap will be added to the balance of your loan. A payment cap can limit the increase to your monthly payments but also can add to the amount you owe on the loan. (This is called *negative amortization*, a term explained on page 22.)

Let’s assume that your rate changes in the first year by 2 percentage points, but your payments can increase no more than 7½% in any 1 year. The following graph shows what your monthly payments would look like.

While your monthly payment will be only \$1,289.03 for the



Difference in monthly payment = \$172.69

second year, the difference of \$172.69 each month will be added to the balance of your loan and will lead to negative amortization.

Some ARMs with payment caps do not have periodic interest-rate caps. In addition, as explained below, most payment-option ARMs have a built-in recalculation period, usually every 5 years. At that point, your payment will be recalculated (lenders use the term *recast*) based on the remaining term of the loan. If you have a 30-year loan and you are at the end of year 5, your payment will be recalculated for the remaining 25 years. The payment cap does not apply to this adjustment. If your loan balance has increased, or if interest rates have risen faster than your payments, your payments could go up a lot.

Types of ARMs

Hybrid ARMs

Hybrid ARMs often are advertised as 3/1 or 5/1 ARMs—you might also see ads for 7/1 or 10/1 ARMs. These loans are a mix—or a hybrid—of a fixed-rate period and an adjustable-rate period. The interest rate is fixed for the first few years of these loans—for example, for 5 years in a 5/1 ARM. After that, the rate may adjust annually (the 1 in the 5/1 example), until the loan is paid off. In the case of 3/1 or 5/1 ARMs:

- the first number tells you how long the fixed interest-rate period will be, and
- the second number tells you how often the rate will adjust after the initial period.

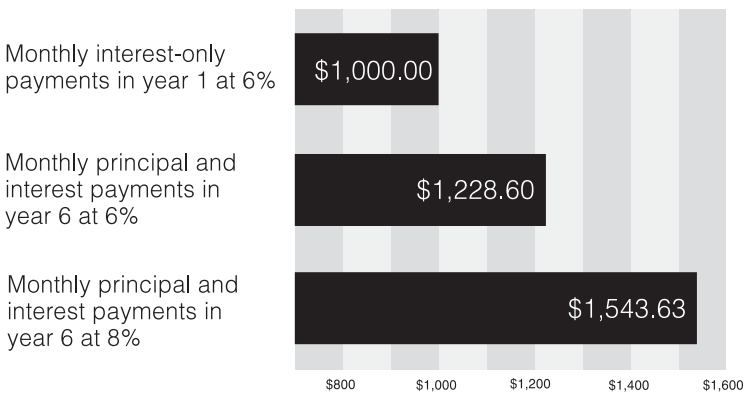
You may also see ads for 2/28 or 3/27 ARMs—the first number tells you how many years the fixed interest-rate period will be, and the second number tells you the number of years the rates on the loan will be adjustable. Some 2/28 and 3/27 mortgages adjust every 6 months, not annually.

Interest-only (I-O) ARMs

An interest-only (I-O) ARM payment plan allows you to *pay only the interest* for a specified number of years, typically for 3 to 10 years. This allows you to have smaller monthly payments for a period. After that, your monthly payment will increase—even if interest rates stay the same—because you must start paying back the principal as well as the interest each month.

For some I-O loans, the interest rate adjusts during the I-O period as well.

For example, if you take out a 30-year mortgage loan with a 5-year I-O payment period, you can pay only interest for 5 years and then you must pay both the principal and interest over the next 25 years. Because you begin to pay back the principal, your payments increase after year 5, even if the rate stays the same. Keep in mind that the longer the I-O period, the higher your monthly payments will be after the I-O period ends.



Payment-option ARMs

A payment-option ARM is an adjustable-rate mortgage that allows you to choose among several payment options each month. The options typically include the following:

- *a traditional payment of principal and interest*, which reduces the amount you owe on your mortgage. These payments are based on a set loan term, such as a 15-, 30-, or 40-year payment schedule.

- *an interest-only payment*, which pays the interest but does not reduce the amount you owe on your mortgage as you make your payments.
- *a minimum (or limited) payment* that may be less than the amount of interest due that month and may not reduce the amount you owe on your mortgage. If you choose this option, the amount of any interest you do not pay will be added to the principal of the loan, **increasing the amount you owe and your future monthly payments**, and increasing the amount of interest you will pay over the life of the loan. In addition, if you pay only the minimum payment in the last few years of the loan, you may owe a larger payment at the end of the loan term, called a *balloon payment*.

The interest rate on a payment-option ARM is typically very low for the first few months (for example, 2% for the first 1 to 3 months). After that, the interest rate usually rises to a rate closer to that of other mortgage loans. Your payments during the first year are based on the initial low rate, meaning that if you only make the minimum payment each month, it will not reduce the amount you owe and it may not cover the interest due. The unpaid interest is added to the amount you owe on the mortgage, and your loan balance increases. This is called *negative amortization*. This means that even after making many payments, you could owe more than you did at the beginning of the loan. Also, as interest rates go up, your payments are likely to go up.

Payment-option ARMs have a built-in recalculation period, usually every 5 years. At this point, your payment will be recalculated (or “recast”) based on the remaining term of the loan. If you have a 30-year loan and you are at the end of year 5, your payment will be recalculated for the remaining 25 years. If your

loan balance has increased because you have made only minimum payments, or if interest rates have risen faster than your payments, your payments will increase each time your loan is recast. At each recast, your new minimum payment will be a fully amortizing payment and any payment cap will not apply. This means that your monthly payment can increase a lot at each recast.

Lenders may recalculate your loan payments before the recast period if the amount of principal you owe grows beyond a set limit, say 110% or 125% of your original mortgage amount. For example, suppose you made only minimum payments on your \$200,000 mortgage and had any unpaid interest added to your balance. If the balance grew to \$250,000 (125% of \$200,000), your lender would recalculate your payments so that you would pay off the loan over the remaining term. It is likely that your payments would go up substantially.

More information on interest-only and payment-option ARMs is available in a Federal Reserve Board brochure, *Interest-Only Mortgage Payments and Payment-Option ARMs—Are They for You?* (available online at www.federalreserve.gov/consumerinfo/mortgages.htm).

Consumer cautions

Discounted interest rates

Many lenders offer more than one type of ARM. Some lenders offer an ARM with an initial rate that is lower than their fully indexed ARM rate (that is, lower than the sum of the index plus the margin). Such rates—called discounted rates, start rates, or teaser rates—are often combined with large initial loan fees, sometimes called *points*, and with higher rates after the initial discounted rate expires.

Your lender or broker may offer you a choice of loans that may include “discount points” or a “discount fee.” You may choose to pay these points or fees in return for a lower interest rate. But keep in mind that the lower interest rate may only last until the first adjustment.

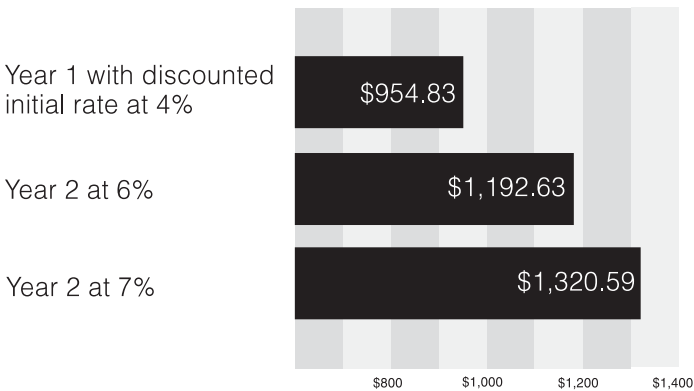
If a lender offers you a loan with a discount rate, don’t assume that means that the loan is a good one for you. You should carefully consider whether you will be able to afford higher payments in later years when the discount expires and the rate is adjusted.

Here is an example of how a discounted initial rate might work. Let’s assume that the lender’s fully indexed 1-year ARM rate (index rate plus margin) is currently 6%; the monthly payment for the first year would be \$1,199.10. But your lender is offering an ARM with a discounted initial rate of 4% for the first year. With the 4% rate, your first-year’s monthly payment would be \$954.83.

With a discounted ARM, your initial payment will probably remain at \$954.83 for only a limited time—and any savings during the discount period may be offset by higher payments over the remaining life of the mortgage. If you are considering a discount ARM, be sure to compare future payments with those for a fully indexed ARM. In fact, if you buy a home or refinance using a deeply discounted initial rate, you run the risk of payment shock, negative amortization, or prepayment penalties or conversion fees.

Payment shock

Payment shock may occur if your mortgage payment rises sharply at a rate adjustment. Let's see what would happen in the second year if the rate on your discounted 4% ARM were to rise to the 6% fully indexed rate.



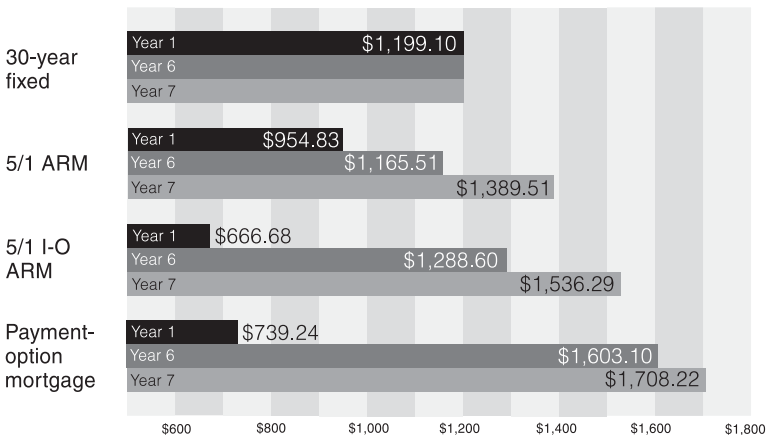
As the example shows, even if the index rate were to stay the same, your monthly payment would go up from \$954.83 to \$1,192.63 in the second year.

Suppose that the index rate increases 1% in 1 year and the ARM rate rises to 7%. Your payment in the second year would be \$1,320.59.

That’s an increase of \$365.76 in your monthly payment. You can see what might happen if you choose an ARM because of a low initial rate without considering whether you will be able to afford future payments.

If you have an interest-only ARM, payment shock can also occur when the interest-only period ends. Or, if you have a payment-option ARM, payment shock can happen when the loan is recast.

The following example compares several different loans over the first 7 years of their terms; the payments shown are for years 1, 6, and 7 of the mortgage, assuming you make interest-only payments or minimum payments. The main point is that, depending on the terms and conditions of your mortgage and changes in interest rates, ARM payments can change quite a bit over the life of the loan—so while you could save money in the first few years of an ARM, you could also face much higher payments in the future.



Negative amortization—When you owe more money than you borrowed

Negative amortization means that the amount you owe increases even when you make all your required payments on time. It occurs whenever your monthly mortgage payments are not large enough to pay all of the interest due on your mortgage—meaning the unpaid interest is added to the principal on your mortgage and you will owe more than you originally borrowed. This can happen because you are making only minimum payments on a payment-option mortgage or because your loan has a payment cap.

For example, suppose you have a \$200,000, 30-year payment-option ARM with a 2% rate for the first 3 months and a 6% rate for the remaining 9 months of the year. Your minimum payment for the year is \$739.24, as shown in the previous graph. However, once the 6% rate is applied to your loan balance, you are no longer covering the interest costs. If you continue to make minimum payments on this loan, your loan balance at the end of the first year of your mortgage would be \$201,118—or \$1,118 more than you originally borrowed.

Because payment caps limit only the amount of payment increases, and not interest-rate increases, payments sometimes do not cover all the interest due on your loan. This means that the unpaid interest is automatically added to your debt, and interest may be charged on that amount. You might owe the lender more later in the loan term than you did at the beginning.

A payment cap limits the increase in your monthly payment by deferring some of the interest. Eventually, you would have to

repay the higher remaining loan balance at the interest rate then in effect. When this happens, there may be a substantial increase in your monthly payment.

Some mortgages include a cap on negative amortization. The cap typically limits the total amount you can owe to 110% to 125% of the original loan amount. When you reach that point, the lender will set the monthly payment amounts to fully repay the loan over the remaining term. Your payment cap will not apply, and your payments could be substantially higher. You may limit negative amortization by voluntarily increasing your monthly payment.

Be sure you know whether the ARM you are considering can have negative amortization.

Home Prices, Home Equity, and ARMs

Sometimes home prices rise rapidly, allowing people to quickly build equity in their homes. This can make some people think that even if the rate and payments on their ARM get too high, they can avoid those higher payments by refinancing their loan or, in the worst case, selling their home. It's important to remember that home prices do not always go up quickly—they may increase a little or remain the same, and sometimes they fall. If housing prices fall, your home may not be worth as much as you owe on the mortgage. Also, you may find it difficult to refinance your loan to get a lower monthly payment or rate. Even if home prices stay the same, if your loan lets you make minimum payments (see *payment-option ARMs* on page 16), you may owe your lender more on your mortgage than you could get from selling your home.

Prepayment penalties and conversion

If you get an ARM, you may decide later that you don't want to risk any increases in the interest rate and payment amount. When you are considering an ARM, ask for information about any extra fees you would have to pay if you pay off the loan early by refinancing or selling your home, and whether you would be able to convert your ARM to a fixed-rate mortgage.

Prepayment penalties

Some ARMs, including interest-only and payment-option ARMs, may require you to pay special fees or penalties if you refinance or pay off the ARM early (usually within the first 3 to 5 years of the loan). Some loans have *hard prepayment penalties*, meaning that you will pay an extra fee or penalty if you pay off the loan during the penalty period for any reason (because you refinance or sell your home, for example). Other loans have *soft prepayment penalties*, meaning that you will pay an extra fee or penalty only if you refinance the loan, but you will not pay a penalty if you sell your home. Also, some loans may have prepayment penalties even if you make only a partial prepayment.

Prepayment penalties can be several thousand dollars. For example, suppose you have a 3/1 ARM with an initial rate of 6%. At the end of year 2 you decide to refinance and pay off your original loan. At the time of refinancing, your balance is \$194,936. If your loan has a prepayment penalty of 6 months' interest on the remaining balance, you would owe about \$5,850.

Sometimes there is a trade-off between having a prepayment penalty and having lower origination fees or lower interest rates.

The lender may be willing to reduce or eliminate a prepayment penalty based on the amount you pay in loan fees or on the interest rate in the loan contract.

If you have a hybrid ARM—such as a 2/28 or 3/27 ARM—be sure to compare the prepayment penalty period with the ARM’s first adjustment period. For example, if you have a 2/28 ARM that has a rate and payment adjustment after the second year, but the prepayment penalty is in effect for the first 5 years of the loan, it may be costly to refinance when the first adjustment is made.

Most mortgages let you make additional principal payments with your monthly payment. In most cases, this is not considered prepayment, and there usually is no penalty for these extra amounts. Check with your lender to make sure there is no penalty if you think you might want to make this type of additional principal prepayment.

Conversion fees

Your agreement with the lender may include a clause that lets you convert the ARM to a fixed-rate mortgage at designated times. When you convert, the new rate is generally set using a formula given in your loan documents.

The interest rate or up-front fees may be somewhat higher for a convertible ARM. Also, a convertible ARM may require a fee at the time of conversion.

Graduated-payment or stepped-rate loans

Some fixed-rate loans start with one rate for 1 or 2 years and then change to another rate for the remaining term of the loan. While

these are not ARMs, your payment will go up according to the terms of your contract. Talk with your lender or broker and read the information provided to you to make sure you understand when and by how much the payment will change.

Where to get information

Disclosures from lenders

You should receive information in writing about each ARM program you are interested in before you have paid a nonrefundable fee. It is important that you read this information and ask the lender or broker about anything you don't understand—index rates, margins, caps, and other ARM features such as negative amortization. After you have applied for a loan, you will get more information from the lender about your loan, including the APR, a payment schedule, and whether the loan has a prepayment penalty.

The APR is the cost of your credit as a yearly rate. It takes into account interest, points paid on the loan, any fees paid to the lender for making the loan, and any mortgage insurance premiums you may have to pay. You can compare APRs on similar ARMs (for example, compare APRs on a 5/1 and a 3/1 ARM) to determine which loan will cost you less in the long term, but you should keep in mind that because the interest rate for an ARM can change, APRs on ARMs cannot be compared directly to APRs for fixed-rate mortgages.

You may want to talk with financial advisers, housing counselors, and other trusted advisers. Contact a local housing counseling agency, call the U.S. Department of Housing and Urban Development toll-free at 800-569-4287, or visit www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm to find an agency near you.

Also, see our *Where to go for help* on page A6, for a list of federal agencies that can provide more information and assistance.

Newspapers and the Internet

When buying a home or refinancing your existing mortgage, remember to shop around. Compare costs and terms, and negotiate for the best deal. Your local newspaper and the Internet are good places to start shopping for a loan. You can usually find information on interest rates and points for several lenders. Since rates and points can change daily, you'll want to check information sources often when shopping for a home loan.

The Mortgage Shopping Worksheet on page 2 may also help you. Take it with you when you speak to each lender or broker, and write down the information you obtain. Don't be afraid to make lenders and brokers compete with each other for your business by letting them know that you are shopping for the best deal.

Advertisements

Any initial information you receive about mortgages probably will come from advertisements or mail solicitations from builders, real estate brokers, mortgage brokers, and lenders. Although this information can be helpful, keep in mind that these are marketing materials—the ads and mailings are designed to make the mortgage look as attractive as possible. These ads may play up low initial interest rates and monthly payments, without emphasizing that those rates and payments could increase substantially later. So, get all the facts.

Any ad for an ARM that shows an initial interest rate should also show how long the rate is in effect and the APR on the loan. If the APR is much higher than the initial rate, your payments may increase a lot after the introductory period, even if interest rates stay the same.

Choosing a mortgage may be the most important financial decision you will make. You are entitled to have all the information you need to make the right decision. Don't hesitate to ask questions about ARM features when you talk to lenders, mortgage brokers, real estate agents, sellers, and your attorney, and keep asking until you get clear and complete answers.

Glossary

Adjustable-rate mortgage (ARM)

A mortgage that does not have a fixed interest rate. The rate changes during the life of the loan based on movements in an index rate, such as the rate for Treasury securities or the Cost of Funds Index. ARMs usually offer a lower initial interest rate than fixed-rate loans. The interest rate fluctuates over the life of the loan based on market conditions, but the loan agreement generally sets maximum and minimum rates. When interest rates increase, generally your loan payments increase; and when interest rates decrease, your monthly payments may decrease.

Annual percentage rate (APR)

The cost of credit expressed as a yearly rate. For closed-end credit, such as car loans or mortgages, the APR includes the interest rate, points, broker fees, and other credit charges that the borrower is required to pay. An APR, or an equivalent rate, is not used in leasing agreements.

Balloon payment

A large extra payment that may be charged at the end of a mortgage loan or lease.

Buydown

When the seller pays an amount to the lender so that the lender can give you a lower rate and lower payments, usually for an initial period in an ARM. The seller may increase the sales price to cover the cost of the buydown. Buydowns can occur in all types of mortgages, not just ARMs.

Cap, interest rate

A limit on the amount that your interest rate can increase. The two types of interest rate caps are *periodic adjustment caps* and *lifetime caps*. *Periodic adjustment caps* limit the interest-rate increase from one adjustment period to the next. *Lifetime caps* limit the interest-rate increase over the life of the loan. All adjustable-rate mortgages have an overall cap.

Cap, payment

A limit on the amount that your monthly mortgage payment on a loan may change, usually a percentage of the loan. The limit can be applied each time the payment changes or during the life of the mortgage. Payment caps may lead to negative amortization because they do not limit the amount of interest the lender is earning.

Conversion clause

A provision in some ARMs that allows you to change the ARM to a fixed-rate loan at some point during the term. Conversion is usually allowed at the end of the first adjustment period. At the time of the conversion, the new fixed rate is generally set at one of the rates then prevailing for fixed-rate mortgages. The conversion feature may be available at extra cost.

Discounted initial rate (also known as a start rate or teaser rate)

In an ARM with a discounted initial rate, the lender offers you a lower rate and lower payments for part of the mortgage term (usually for 1, 3, or 5 years). After the discount period, the ARM rate will probably go up depending on the index rate. Discounts can occur in all types of mortgages, not just ARMs.

Equity

In housing markets, equity is the difference between the fair market value of the home and the outstanding balance on your mortgage plus any outstanding home equity loans. In vehicle leasing markets, equity is the positive difference between the trade-in or market value of your vehicle and the loan payoff amount.

Hybrid ARM

These ARMs are a mix—or a hybrid—of a fixed-rate period and an adjustable-rate period. The interest rate is fixed for the first several years of the loan; after that period, the rate can adjust annually. For example, hybrid ARMs can be advertised as 3/1 or 5/1—the first number tells you how long the fixed interest-rate period will be and the second number tells you how often the rate will adjust after the initial period. For example, a 3/1 loan has a fixed rate for the first 3 years and then the rate adjusts once each year beginning in year 4.

Index

The economic indicator used to calculate interest-rate adjustments for adjustable-rate mortgages or other adjustable-rate loans. The index rate can increase or decrease at any time. *See also* the chart on page 8, *Selected index rates for ARMs over an 11-year period*, for examples of common indexes that have changed in the past.

Interest

The rate used to determine the cost of borrowing money, usually stated as a percentage and as an annual rate.

Interest-only (I-O) ARM

Interest-only ARMs allow you to pay only the interest for a specified number of years, typically between 3 and 10 years. This arrangement allows you to have smaller monthly payments for a prescribed period. After that period, your monthly payment will increase—even if interest rates stay the same—because you must start paying back the principal and the interest each month. For some I-O loans, the interest rate adjusts during the I-O period as well.

Margin

The number of percentage points the lender adds to the index rate to calculate the interest rate of an adjustable-rate mortgage (ARM) at each adjustment.

Negative amortization

Occurs when the monthly payments in an adjustable-rate mortgage loan do not cover all the interest owed. The interest that is not paid in the monthly payment is added to the loan balance. This means that even after making many payments, you could owe more than you did at the beginning of the loan. Negative amortization can occur when an ARM has a payment cap that results in monthly payments that are not high enough to cover the interest due or when the minimum payments are set at an amount lower than the amount you owe in interest.

Payment-option ARM

An ARM that allows the borrower to choose among several payment options each month. The options typically include (1) a traditional amortizing payment of principal and interest, (2) an interest-only payment, or (3) a minimum (or limited) payment that may be less than the amount of interest due that month. If the borrower chooses the minimum-payment option, the amount

of any interest that is not paid will be added to the principal of the loan. *See also* Negative amortization on page A4.

Points (also called discount points)

One point is equal to 1 percent of the principal amount of a mortgage loan. For example, if the mortgage is \$200,000, one point equals \$2,000. Lenders frequently charge points in both fixed-rate and adjustable-rate mortgages to cover loan origination costs or to provide additional compensation to the lender or broker. These points usually are paid at closing and may be paid by the borrower or the home seller, or may be split between them. In some cases, the money needed to pay points can be borrowed (incorporated in the loan amount), but doing so will increase the loan amount and the total costs. Discount points (also called discount fees) are points that the borrower voluntarily chooses to pay in return for a lower interest rate.

Prepayment penalty

Extra fees that may be due if you pay off your loan early by refinancing the loan or by selling the home. The penalty is usually limited to the first 3 to 5 years of the loan's term. If your loan includes a prepayment penalty, make sure you understand the cost. Compare the length of the prepayment penalty period with the first adjustment period of the ARM to see if refinancing is cost-effective before the loan first adjusts. Some loans may have a prepayment penalty even if you make a partial prepayment. Ask the lender for a loan without a prepayment penalty and the cost of that loan.

Principal

The amount of money borrowed or the amount still owed on a loan.

Where to go for help

For additional information or to file a complaint about a bank, savings and loan, credit union, or other financial institution, contact one of the following federal agencies, depending on the type of institution.

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Federal Reserve Consumer Help P.O. Box 1200 Minneapolis, MN 55480	Federally insured state-chartered bank members of the Federal Reserve System	(888) 851-1920 www.federalreserveconsumerhelp.gov
Consumer Financial Protection Bureau (CFPB) P.O. Box 4503 Iowa City, IA 52244	Insured depository institutions and credit unions (and their affiliates) with assets greater than \$10 billion, and nondepository institutions such as mortgage originators, mortgage brokers and servicers, larger participants of other financial services products, private education loan providers, and payday lenders	(855) 411-2372 www.consumerfinance.gov
Office of the Comptroller of the Currency (OCC) Customer Assistance Unit 1301 McKinney Street Suite 3450 Houston, TX 77010	National banks and federally chartered savings banks/associations	(800) 613-6743 www.occ.treas.gov www.helpwithmybank.gov
Federal Deposit Insurance Corporation (FDIC) Consumer Response Center 1100 Walnut Street, Box #11 Kansas City, MO 64106	Federally insured state-chartered banks that are not members of the Federal Reserve System	(877) ASK-FDIC or (877) 275-3342 www.fdic.gov www.fdic.gov/consumers

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Federal Housing Finance Agency (FHFA) Consumer Communications Constitution Center 400 7th Street, S.W. Washington, DC 20024	Fannie Mae, Freddie Mac, and the Federal Home Loan Banks	(202) 649-3811 www.fhfa.gov www.fhfa.gov/Default.aspx?Page=369
National Credit Union Administration (NCUA) Consumer Assistance 1775 Duke Street Alexandria, VA 22314-3428	Federally chartered credit unions	(800) 755-1030 www.ncua.gov www.mycreditunion.gov
Federal Trade Commission (FTC) Consumer Response Center 600 Pennsylvania Avenue, N.W. Washington, DC 20580	Finance companies, retail stores, auto dealers, mortgage companies and other lenders, and credit bureaus	(877) FTC-HELP or (877) 382-4357 www.ftc.gov www.ftc.gov/bcp
Securities and Exchange Commission (SEC) Complaint Center 100 F Street, N.E. Washington, DC 20549-0213	Brokerage firms, mutual fund companies, and investment advisers	(202) 551-6551 www.sec.gov www.sec.gov/complaint/question.shtml
Farm Credit Administration Office of Congressional and Public Affairs 1501 Farm Credit Drive McLean, VA 22102-5090	Agricultural lenders	(703) 883-4056 www.fca.gov
Small Business Administration (SBA) Consumer Affairs 409 3rd Street, S.W. Washington, DC 20416	Small business lenders	(800) U-ASK-SBA or (800) 827-5722 www.sba.gov

Regulatory Agency	Regulated Entity(ies)	Telephone/Website
Commodity Futures Trading Commission (CFTC) 1155 21st Street, N.W. Washington, DC 20581	Commodity brokers, commodity trading advisers, commodity pools, and introducing brokers	(866) 366-2382 www.cftc.gov/Consumer-Protection
U.S. Department of Justice (DOJ) Criminal Division 950 Pennsylvania Avenue, N.W. Washington, DC 20530	Fair lending and fair housing issues	(202) 514-3301 www.justice.gov/criminal
Department of Housing and Urban Development (HUD) Office of Fair Housing/Equal Opportunity 451 7th Street, S.W. Washington, DC 20410	Fair lending and fair housing issues	(800) 669-9777 www.hud.gov/complaints

More resources

Looking for the Best Mortgage—Shop, Compare, Negotiate
(at www.federalreserve.gov/pubs/mortgage/mortb_1.htm)

*Interest-Only Mortgage Payments and Payment-Option
ARMs—Are They for You?*
(at www.federalreserve.gov/pubs/mortgage_interestonly/)

A Consumer's Guide to Mortgage Lock-Ins
(at www.federalreserve.gov/pubs/lockins/default.htm)

A Consumer's Guide to Mortgage Settlement Costs
(at www.federalreserve.gov/pubs/settlement/default.htm)

Know Before You Go . . . To Get a Mortgage: A Guide to Mortgage Products and a Glossary of Lending Terms
(at www.bos.frb.org/consumer/knowbeforeyougo/mortgage/mortgage.pdf)

Partners Online Mortgage Calculator
(at www.frbatlanta.org/partnerssoftwareonline/dsp_main.cfm)

For more information on mortgage and other financial topics, including interactive calculators, visit www.federalreserve.gov/consumerinfo.

ADJUSTABLE RATE MORTGAGE DISCLOSURE

This disclosure describes the features of the adjustable-rate mortgage (ARM) program you are considering. Information on other ARM programs is available upon request.

HOW YOUR INTEREST RATE AND PAYMENT ARE DETERMINED

Your interest rate will be based on an index rate plus a margin. However, the initial interest rate is not based on the margin and index used for later rate adjustments.

Your payment will be based on the interest rate, loan balance and loan term.

The interest rate after the initial five year period will be based on the weekly average yield on U.S. Treasury Securities adjusted to a constant maturity of 1 year plus our margin. The margin and initial rate are based on market conditions and certain creditworthiness factors. Many applicants have recently qualified for a margin of 2.75% and initial rate of 3.25%. Ask for our current initial interest rate, margin, index and interest rate.

Information about the index rate is published in the Federal Reserve Bulletin.

HOW YOUR INTEREST RATE CAN CHANGE

Your interest rate can change. Your interest rate is fixed for the first five years of the loan, but then can change annually on the month following the anniversary date of the loan and will be based on the index value 45 days prior to that date.

Your interest rate cannot increase or decrease more than 1 percentage point(s) at each adjustment, including the first adjustment after the initial period.

Over the term of the loan your interest rate will never be greater than 18% per year.

HOW YOUR PAYMENT CAN CHANGE

Your monthly payment can change annually. Payments may increase or decrease substantially based on changes in the interest rate.

For example, on a \$10,000, 15 year loan with an initial interest rate of 3.25% in effect in November 2013, the maximum amount that the interest rate can rise under this program is 10.00 percentage point(s) to 13.25%, and the monthly payment can rise from a first year payment of \$70.27 to a maximum of \$91.02 in the fifteenth year.

To see what your payments would be, divide your mortgage amount by \$10,000; then multiply the monthly payment by that amount. (For example, the monthly payment for a mortgage amount of \$60,000 would be: $60,000/10,000 = 6$; $6 \times 70.27 = \$421.62$ per month.)

You will be notified in writing at least 60, but not more than 120 calendar days before the due date of a payment at a new level. This notice will contain information about your interest rates, payment amount and loan balance.



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IMPORTANT TERMS of our MANUFACTURED HOME SECURED (NOT INVOLVING REAL PROPERTY) LINES OF CREDIT

THIS DISCLOSURE CONTAINS INFORMATION ABOUT OUR MANUFACTURED HOME SECURED (NOT INVOLVING REAL PROPERTY) LINES OF CREDIT. ALL TERMS ARE THE SAME EXCEPT FOR WHERE OTHERWISE INDICATED. YOU SHOULD READ IT CAREFULLY AND KEEP THIS COPY FOR YOURSELF.

Availability of Terms

All terms described below are subject to change. If these terms change (other than the Annual Percentage Rate), and you decide, as a result, not to enter into an agreement with us, you are entitled to a refund of any fees you paid to us or anyone else in connection with your application.

Security Interest

We will take a lien on your manufactured home ("Security Property"). You could lose your manufactured home if you do not meet certain obligations in your Agreement with us.

Possible Actions

Termination

If you fail to meet the terms of repayment, or if you act or fail to act in a way that adversely affects our security interest or other rights in the Security Property, or if you have committed fraud or made a material misrepresentation in connection with the Account, we may, subject to the governing law, terminate the plan, require payment in full of the entire outstanding balance in a single payment or cause the Security Property to be sold and the proceeds of such sale to be applied to your obligation to us. You agree to pay any reasonable costs of protecting, retaking, repairing or selling the Security Property.

Suspension

Your right to request additional advances may be suspended, or your maximum credit limit reduced, at our option, in the following instances: (1) you fail to make the scheduled payments due to us; (2) you fail to make timely payments to the holders of liens senior to ours; (3) you fail to pay any taxes prior to delinquency; (4) you fail to maintain the required property insurance; (5) the value of the Security Property declines significantly below the appraised value upon which we relied in approving your application; (6) we reasonably believe that your ability to meet your payment obligations is impaired because of a material change in your financial circumstances; (7) governmental action precludes our imposing the interest rate provided herein or adversely affects the priority of our security interest such that the value of our interest is less than 120.00% of your maximum credit limit; (8) for variable rate credit, the maximum interest rate under the plan is reached; or (9) government regulatory authorities find that further advances under this plan constitute an unsafe and unsound practice. When the condition which caused the suspension of advances or reduction of your maximum credit limit no longer exists, the original terms of your Agreement will be reinstated. You understand that if your right to request additional advances is suspended or your maximum credit limit is reduced, you still owe us whatever sums you have already borrowed, all other charges under your Agreement and applicable Finance Charges.

Home Equity Plans

We offer two (2) Manufactured Home Line of Credit plans: (i) our Variable Rate Plan that has an introductory rate period; and (ii) our Fixed Rate Plan that does not have an introductory rate. Not all applicants may qualify for all Plans.

Minimum Payment Requirements

Fixed Rate Plan

You can obtain credit advances for 24 months⁽¹⁾ (the draw period). During the draw period, your minimum periodic payment will be established and fixed at the time of each advance to the amount necessary to amortize your then outstanding account balance by the agreement maturity date, subject to the lesser of \$50.00 or your account balance. After the draw period ends, you will no longer be able to obtain credit advances and you must repay your outstanding account balance (the repayment period). The length of the repayment period will depend on the date and the amount of your last advance but in no event will exceed 156 months⁽²⁾. During the repayment period, your minimum periodic payment will be calculated in the same manner as the draw period.

(1) This represents a draw period length that we have recently used

(2) This represents a repayment period that we have recently used

Variable Rate Plan

You can obtain credit advances for 24 months⁽³⁾ (the draw period). During the draw period, your minimum periodic payment will be established at the time of each advance, and any subsequent change in interest rate, to the amount necessary to amortize your then outstanding account balance by the agreement maturity date, subject to the lesser of \$50.00 or your account balance. After the draw period ends, you will no longer be able to obtain credit advances and you must repay your outstanding account balance (the repayment period). The length of the repayment period will depend on the date and the amount of your last advance but in no event will exceed 156 months⁽⁴⁾. During the repayment period, your minimum periodic payment will be calculated in the same manner as the draw period.

(3) This represents a draw period length that we have recently used

(4) This represents a repayment period that we have recently used

Minimum Payment Example

Fixed Rate Plan

If you made only the minimum payments and took no other credit advances, it would take 180 months to pay off a credit advance of \$10,000.00 at an **ANNUAL PERCENTAGE RATE** of 11.00%⁽⁵⁾. During that period you would make 24 monthly payments of \$113.67, followed by 155 payments of \$113.67, and a final payment of \$114.67.

(5) This represents an interest rate we have recently used

Variable Rate Plan

If you made only the minimum payments and took no other credit advances, it would take 180 months to pay off a credit advance of \$10,000.00 at an **ANNUAL PERCENTAGE RATE** of 9.50%⁽⁶⁾. During that period you would make 24 monthly payments of \$104.43, followed by 155 payments of \$104.43, and a final payment of \$105.43.

(6) This represents an interest rate we have recently used

Fees and Charges

To open a line of credit you must pay us a \$300.00 origination fee FINANCE CHARGE. You will also have to pay certain fees to third parties. The fees you will have to pay to third parties generally total from \$_____ - \$_____. If you ask, we will give you an itemization of the fees you will have to pay to third parties.

Minimum Draw and Balance Requirements

The initial credit advance must be equal to or greater than \$_____. Each subsequent credit advance must be equal to or greater than \$_____.

Insurance

You must carry insurance on the property that secures this plan. As a condition of obtaining credit, we will not require you to provide such insurance in an amount that exceeds the replacement value of the Security Property.

Tax Deductibility

You should consult a tax advisor regarding the deductibility of interest and charges for the line of credit.

Variable Rate Plan**Plan Description**

The variable rate plan's Annual Percentage Rate (corresponding to the periodic rate), and the amount of your regularly scheduled payments during the repayment period can change as a result. The Annual Percentage Rate includes only interest and no other costs. The Annual Percentage Rate is based on the value of an index. The index is the highest Prime Rate as published in the Money Rates Section of The Wall Street Journal in effect on the day the introductory rate period expires, and subsequently on the last calendar day of each month of each year. To determine the Annual Percentage Rate that will apply to your line of credit, we add a margin to the value of the index. Ask us for the current index value, margin, and annual percentage rate. After you open a line of credit, rate information will be provided in periodic statements that we send you.

Introductory Rate

For the 60-month period immediately following the date of agreement, the Annual Percentage Rate that will apply to your account will be an introductory rate. The introductory rate will be 9.50%⁽⁷⁾. Upon the expiration of the introductory rate period, your account will be subject to the variable rate provisions described herein. The introductory Annual Percentage Rate is not based on the index and margin used for later adjustments.

(7) This represents an initial introductory rate we have recently used

Rate Changes

Your Annual Percentage Rate can change on the day the introductory rate period expires, and monthly thereafter. There is no limit on the amount by which the interest rate can change during any one-year period other than the maximum and minimum annual percentage rates that can apply at any time to this Account.

The minimum **ANNUAL PERCENTAGE RATE** at any time is 4.00%. The maximum **ANNUAL PERCENTAGE RATE** at any time is 18.00%.

Maximum Rate and Payment Examples

If you had an outstanding balance of \$10,000.00 during the draw period, the Minimum Payment at the maximum **ANNUAL PERCENTAGE RATE** of 18.00% would be \$161.06. This Annual Percentage Rate could be reached during the 61st month of the draw period.

If you had an outstanding balance of \$10,000.00 during the repayment period, the Minimum Payment at the maximum **ANNUAL PERCENTAGE RATE** of 18.00% would be \$180.19. This Annual Percentage Rate could be reached during the 1st month of the repayment period.

Historical Example

The following table shows how the Annual Percentage Rate and the monthly payments for a single \$10,000.00 credit advance would have changed based on changes in the index since 2008. The index is from The Wall Street Journal and is calculated on the first business day of August of each year. While only one payment amount per year is shown, payments may have varied during the year. The table assumes that no additional credit advances were taken, that only the minimum payments were made, and that the rate remained constant during the year. It does not necessarily indicate how the index or your payments will change in the future.

Year	Index	Margin ⁽⁸⁾	ANNUAL PERCENTAGE RATE	Payment Period	Minimum Payment
2008	5.00	4.00	9.50% ⁽⁹⁾	DRAW	\$104.43
2009	3.25	4.00	9.50% ⁽⁹⁾	DRAW	\$104.43
2010	3.25	4.00	9.50% ⁽⁹⁾	REPAYMENT	\$104.43
2011	3.25	4.00	9.50% ⁽⁹⁾	REPAYMENT	\$104.43
2012	3.25	4.00	9.50% ⁽⁹⁾	REPAYMENT	\$104.43
2013	3.25	4.00	7.25%	REPAYMENT	\$94.74
2014	3.25	4.00	7.25%	REPAYMENT	\$94.74
2015	3.25	4.00	5.25%	REPAYMENT	\$88.00
2016	3.50	4.00	7.50%	REPAYMENT	\$94.71
2017	4.25	4.00	6.25%	REPAYMENT	\$91.43
2018	5.00	4.00	9.00%	REPAYMENT	\$97.58
2019	5.25	4.00	9.25%	REPAYMENT	\$98.05
2020	3.25	4.00	7.25%	REPAYMENT	\$95.21
2021	3.25	4.00	7.25%	REPAYMENT	\$95.21
2022	5.50	4.00	9.50%	REPAYMENT	\$96.35

(8) This represents a margin which we have used recently

(9) This represents an introductory rate which we have used recently



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 (707) 527-6216 • Fax: (707) 527-6835

What you should know about home equity lines of credit:

This disclosure was initially prepared by the Board of Governors of the Federal Reserve System. The Consumer Financial Protection Bureau (CFPB) has made technical updates to the disclosure to reflect new mortgage rules under Title XIV of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). A larger update of this disclosure is planned in the future to reflect other changes under the Dodd-Frank Act and to align with other CFPB resources and tools for consumers as part of the CFPB's broader mission to educate consumers. Consumers are encouraged to visit the CFPB's website at consumerfinance.gov/owning-a-home to access interactive tools and resources for mortgage shoppers, which are expected to be available beginning in 2014.

Table of Contents

Table of Contents	1
1. Introduction	1
1.1 Home equity plan checklist	1
2. What is a home equity line of credit?	2
2.1 What should you look for when shopping for a plan?	2
2.2 Costs of establishing and maintaining a home equity line	3
2.3 How will you repay your home equity plan?	3
2.4 Line of credit vs. traditional second mortgage loans	3
2.5 What if the lender freezes or reduces your line of credit?	4
Appendix A:	5
Defined terms	5
Appendix B:	6
More information	6
Appendix C:	7
Contact information	7

Introduction

If you are in the market for credit, a home equity plan is one of several options that might be right for you. Before making a decision, however, you should weigh carefully the costs of a home equity line against the benefits. Shop for the credit terms that best meet your borrowing needs without posing undue financial risks. And remember, failure to repay the amounts you've borrowed, plus interest, could mean the loss of your home.

1.1 Home equity plan checklist

Ask your lender to help you fill out this worksheet.

Basic features for comparison	Plan A	Plan B
Fixed annual percentage rate	%	%
Variable annual percentage rate	%	%
• Index used and current value	%	%
• Amount of margin		
• Frequency of rate adjustments		
• Interest rate cap and floor		
Length of plan		
Draw Period		
Repayment period		
Initial fees		
Appraisal fee		
Application fee		
Up-front charges, including points		
Closing Costs		

Home equity plan checklist (continued)

Repayment terms	Plan A	Plan B
During the draw period		
Interest and principal payments		
Interest-only payments		
Fully amortizing payments		
When the draw period ends		
Balloon payment?		
Renewal available?		
Refinancing of balance by lender?		

2. What is a home equity line of credit?

A home equity line of credit is a form of revolving credit in which your home serves as collateral. Because a home often is a consumer's most valuable asset, many homeowners use home equity credit lines only for major items, such as education, home improvements, or medical bills, and choose not to use them for day-to-day expenses.

With a home equity line, you will be approved for a specific amount of credit. Many lenders set the credit limit on a home equity line by taking a percentage (say, 75 percent) of the home's appraised value and subtracting from that the balance owed on the existing mortgage. For example:

Appraised value of home	\$100,000
Percentage	x 75%
Percentage of appraised value	= \$ 75,000
Less balance owed on mortgage debt	- \$ 40,000
<hr/>	
Potential line of credit	\$ 35,000

In determining your actual credit limit, the lender will also consider your ability to repay the loan (principal and interest) by looking at your income, debts, and other financial obligations as well as your credit history.

Many home equity plans set a fixed period during which you can borrow money, such as 10 years. At the end of this "draw period," you may be allowed to renew the credit line. If your plan does not allow renewals, you will not be able to borrow additional money once the period has ended. Some plans may call for payment in full of any outstanding balance at the end of the period. Others may allow repayment over a fixed period (the "repayment period"), for example, 10 years.

Once approved for a home equity line of credit, you will most likely be able to borrow up to your credit limit whenever you want. Typically, you will use special checks to draw on your line. Under some plans, borrowers can use a credit card or other means to draw on the line.

There may be other limitations on how you use the line. Some plans may require you to borrow a minimum amount each time you draw on the line (for example, \$300) or keep a minimum amount outstanding. Some plans may also require that you take an initial advance when the line is set up.

2.1 What should you look for when shopping for a plan?

If you decide to apply for a home equity line of credit, look for the plan that best meets your particular needs. Read the credit agreement carefully, and examine the terms and conditions of various plans, including the annual percentage rate (APR) and the costs of establishing the plan. Remember, though, that the APR for a home equity line is based on the interest rate alone and will not reflect closing costs and other fees and charges, so you'll need to compare these costs, as well as the APRs, among lenders.

2.1.1 Variable interest rates

Home equity lines of credit typically involve variable rather than fixed interest rates. The variable rate must be based on a publicly available index (such as the prime rate published in some major daily newspapers or a U.S. Treasury bill rate). In such cases, the interest rate you pay for the line of credit will change, mirroring changes in the value of the index. Most lenders cite the interest rate you will pay as the value of the index at a particular time, plus a "margin," such as 2 percentage points. Because the cost of borrowing is tied directly to the value of the index, it is important to find out which index is used, how often the value of the index changes, and how high it has risen in the past. It is also important to note the amount of the margin.

Lenders sometimes offer a temporarily discounted interest rate for home equity lines—an "introductory" rate that is unusually low for a short period, such as six months.

Variable-rate plans secured by a dwelling must, by law, have a ceiling (or cap) on how much your interest rate may increase over the life of the plan. Some variable-rate plans limit how much your payment may increase and how low your interest rate may fall if the index drops.

Some lenders allow you to convert from a variable interest rate to a fixed rate during the life of the plan, or let you convert all or a portion of your line to a fixed-term installment loan.

2.2 Costs of establishing and maintaining a home equity line

Many of the costs of setting up a home equity line of credit are similar to those you pay when you get a mortgage. For example:

- A fee for a property appraisal to estimate the value of your home;
- An application fee, which may not be refunded if you are turned down for credit;
- Up-front charges, such as one or more "points" (one point equals 1 percent of the credit limit); and
- Closing costs, including fees for attorneys, title search, mortgage preparation and filing, property and title insurance, and taxes.

In addition, you may be subject to certain fees during the plan period, such as annual membership or maintenance fees and a transaction fee every time you draw on the credit line.

You could find yourself paying hundreds of dollars to establish the plan. And if you were to draw only a small amount against your credit line, those initial charges would substantially increase the cost of the funds borrowed. On the other hand, because the lender's risk is lower than for other forms of credit, as your home serves as collateral, annual percentage rates for home equity lines are generally lower than rates for other types of credit. The interest you save could offset the costs of establishing and maintaining the line. Moreover, some lenders waive some or all of the closing costs.

2.3 How will you repay your home equity plan?

Before entering into a plan, consider how you will pay back the money you borrow. Some plans set a minimum monthly payment that includes a portion of the principal (the amount you borrow) plus accrued interest. But, unlike with typical installment loan agreements, the portion of your payment that goes toward principal may not be enough to repay the principal by the end of the term. Other plans may allow payment of only the interest during the life of the plan, which means that you pay nothing toward the principal. If you borrow \$10,000, you will owe that amount when the payment plan ends.

Regardless of the minimum required payment on your home equity line, you may choose to pay more, and many lenders offer a choice of payment options. However, some lenders may require you to pay special fees or penalties if you choose to pay more, so check with your lender. Many consumers choose to pay down the principal regularly as they do with other loans. For example, if you use your line to buy a boat, you may want to pay it off as you would a typical boat loan.

Whatever your payment arrangements during the life of the plan-whether you pay some, a little, or none of the principal amount of the loan-when the plan ends, you may have to pay the entire balance owed, all at once. You must be prepared to make this "balloon payment" by refinancing it with the lender, by obtaining a loan from another lender, or by some other means. If you are unable to make the balloon payment, you could lose your home.

If your plan has a variable interest rate, your monthly payments may change. Assume, for example, that you borrow \$10,000 under a plan that calls for interest-only payments. At a 10 percent interest rate, your monthly payments would be \$83. If the rate rises over time to 15 percent, your monthly payments will increase to \$125. Similarly, if you are making payments that cover interest plus some portion of the principal, your monthly payments may increase, unless your agreement calls for keeping payments the same throughout the plan period.

If you sell your home, you will probably be required to pay off your home equity line in full immediately. If you are likely to sell your home in the near future, consider whether it makes sense to pay the up-front costs of setting up a line of credit. Also keep in mind that renting your home may be prohibited under the terms of your agreement.

2.4 Line of credit vs. traditional second mortgage loans

If you are thinking about a home equity line of credit, you might also want to consider a traditional second mortgage loan. This type of loan provides you with a fixed amount of money, repayable over a fixed period. In most cases, the payment schedule calls for equal payments that pay off the entire loan within the loan period. You might consider a second mortgage instead of a home equity line if, for example, you need a set amount for a specific purpose, such as an addition to your home.

In deciding which type of loan best suits your needs, consider the costs under the two alternatives. Look at both the APR and other charges. Do not, however, simply compare the APRs, because the APRs on the two types of loans are figured differently:

- The APR for a traditional second mortgage loan takes into account the interest rate charged plus points and other finance charges.
- The APR for a home equity line of credit is based on the periodic interest rate alone. It does not include points or other charges.

2.4.1 Disclosures from lenders

The federal Truth in Lending Act requires lenders to disclose the important terms and costs of their home equity plans, including the APR, miscellaneous charges, the payment terms, and information about any variable-rate feature. And in general, neither the lender nor anyone else may charge a fee until after you have received this information. You usually get these disclosures when you receive an application form, and you will get additional disclosures before the plan is opened. If any term (other than a variable-rate feature) changes before the plan is opened, the lender must return all fees if you decide not to enter into the plan because of the change. Lenders are also required to provide you with a list of homeownership counseling organizations in your area.

When you open a home equity line, the transaction puts your home at risk. If the home involved is your principal dwelling, the Truth in Lending Act gives you three days from the day the account was opened to cancel the credit line. This right allows you to change your mind for any reason. You simply inform the lender in writing within the three-day period. The lender must then cancel its security interest in your home and return all fees-including any application and appraisal fees-paid to open the account.

The Home Ownership and Equity Protection Act of 1994 (HOEPA) addresses certain unfair practices and establishes requirements for certain loans with high rates and fees, including certain additional disclosures. HOEPA now covers some HELOCs. You can find out more information by contacting the CFPB at the website address and phone number listed in the Contact information appendix, below.

2.5 What if the lender freezes or reduces your line of credit?

Plans generally permit lenders to freeze or reduce a credit line if the value of the home "declines significantly" or when the lender "reasonably believes" that you will be unable to make your payments due to a "material change" in your financial circumstances. If this happens, you may want to:

- **Talk with your lender.** Find out what caused the lender to freeze or reduce your credit line and what, if anything, you can do to restore it. You may be able to provide additional information to restore your line of credit, such as documentation showing that your house has retained its value or that there has not been a "material change" in your financial circumstances. You may want to get copies of your credit reports (go to the CFPB's website at consumerfinance.gov/askcfpb/5/can-i-review-my-credit-report.html for information about how to get free copies of your credit reports) to make sure all the information in them is correct. If your lender suggests getting a new appraisal, be sure you discuss appraisal firms in advance so that you know they will accept the new appraisal as valid.
- **Shop around for another line of credit.** If your lender does not want to restore your line of credit, shop around to see what other lenders have to offer. If another lender is willing to offer you a line of credit, you may be able to pay off your original line of credit and take out another one. Keep in mind, however, that you may need to pay some of the same application fees you paid for your original line of credit.

APPENDIX A:

Defined terms

This glossary provides general definitions for terms commonly used in the real estate market. They may have different legal meanings depending on the context.

DEFINED TERM

ANNUAL MEMBERSHIP OR MAINTENANCE FEE	An annual charge for access to a financial product such as a line of credit, credit card, or account. The fee is charged regardless of whether or not the product is used.
ANNUAL PERCENTAGE RATE (APR)	The cost of credit, expressed as a yearly rate. For closed-end credit, such as car loans or mortgages, the APR includes the interest rate, points, broker fees, and other credit charges that the borrower is required to pay. An APR, or an equivalent rate, is not used in leasing agreements.
APPLICATION FEE	Fees charged when you apply for a loan or other credit. These fees may include charges for property appraisal and a credit report.
BALLOON PAYMENT	A large extra payment that may be charged at the end of a mortgage loan or lease.
CAP (INTEREST RATE)	A limit on the amount that your interest rate can increase. Two types of interest-rate caps exist. Periodic adjustment caps limit the interest-rate increase from one adjustment period to the next. Lifetime caps limit the interest-rate increase over the life of the loan. By law, all adjustable-rate mortgages have an overall cap.
CLOSING OR SETTLEMENT COSTS	Fees paid when you close (or settle) on a loan. These fees may include application fees; title examination, abstract of title, title insurance, and property survey fees; fees for preparing deeds, mortgages, and settlement documents; attorneys' fees; recording fees; estimated costs of taxes and insurance; and notary, appraisal, and credit report fees. Under the Real Estate Settlement Procedures Act, the borrower receives a good faith estimate of closing costs within three days of application. The good faith estimate lists each expected cost as an amount or a range.
CREDIT LIMIT	The maximum amount that may be borrowed on a credit card or under a home equity line of credit plan.
EQUITY	The difference between the fair market value of the home and the outstanding balance on your mortgage plus any outstanding home equity loans.
INDEX	The economic indicator used to calculate interest-rate adjustments for adjustable-rate mortgages or other adjustable-rate loans. The index rate can increase or decrease at any time. See also Selected index rates for ARMs over an 11-year period (consumerfinance.gov/f/201204_CFPB_ARMs-brochure.pdf) for examples of common indexes that have changed in the past.
INTEREST RATE	The percentage rate used to determine the cost of borrowing money, stated usually as a percentage of the principal loan amount and as an annual rate.
MARGIN	The number of percentage points the lender adds to the index rate to calculate the adjustable-rate-mortgage interest rate at each adjustment.
MINIMUM PAYMENT	The lowest amount that you must pay (usually monthly) to keep your account in good standing. Under some plans, the minimum payment may cover interest only; under others, it may include both principal and interest.
POINTS (ALSO CALLED DISCOUNT POINTS)	One point is equal to 1 percent of the principal amount of a mortgage loan. For example, if a mortgage is \$200,000, one point equals \$2,000. Lenders frequently charge points in both fixed-rate and adjustable-rate mortgages to cover loan origination costs or to provide additional compensation to the lender or broker. These points usually are paid at closing and may be paid by the borrower or the home seller, or may be split between them. In some cases, the money needed to pay points can be borrowed (incorporated in the loan amount), but doing so will increase the loan amount and the total costs. Discount points (also called discount fees) are points that you voluntarily choose to pay in return for a lower interest rate.
SECURITY INTEREST	If stated in your credit agreement, a creditor, lessor, or assignee's legal right to your property (such as your home, stocks, or bonds) that secures payment of your obligation under the credit agreement. The property that secures payment of your obligation is referred to as "collateral."
TRANSACTION FEE	Fee charged each time a withdrawal or other specified transaction is made on a line of credit, such as a balance transfer fee or a cash advance fee.
VARIABLE RATE	An interest rate that changes periodically in relation to an index, such as the prime rate. Payments may increase or decrease accordingly.

APPENDIX B:

More information

For more information about mortgages, including home equity lines of credit, visit consumerfinance.gov/mortgage. For answers to questions about mortgages and other financial topics, visit consumerfinance.gov/askcfpb. You may also visit the CFPB's website at consumerfinance.gov/owning-a-home to access interactive tools and resources for mortgage shoppers, which are expected to be available beginning in 2014.

Housing counselors can be very helpful, especially for first-time home buyers or if you're having trouble paying your mortgage. The U.S. Department of Housing and Urban Development (HUD) supports housing counseling agencies throughout the country that can provide free or low-cost advice. You can search for HUD-approved housing counseling agencies in your area on the CFPB's web site at consumerfinance.gov/find-a-housing-counselor or by calling HUD's interactive toll-free number at 800-569-4287.

The company that collects your mortgage payments is your loan servicer. This may not be the same company as your lender. If you have concerns about how your loan is being serviced or another aspect of your mortgage, you may wish to submit a complaint to the CFPB at consumerfinance.gov/complaint or by calling (855) 411-CFPB (2372).

When you submit a complaint to the CFPB, the CFPB will forward your complaint to the company and work to get a response. Companies have 15 days to respond to you and the CFPB. You can review the company's response and give feedback to the CFPB.

APPENDIX C:

Contact Information

For additional information or to submit a complaint, you can contact the CFPB or one of the other federal agencies listed below, depending on the type of institution. If you are not sure which agency to contact, you can submit a complaint to the CFPB and if the CFPB determines that another agency would be better able to assist you, the CFPB will refer your complaint to that agency and let you know.

Regulatory Agency	Regulated Entity(ies)	Contact Information
Consumer Financial Protection Bureau (CFPB) P.O. Box 4503 Iowa City, IA 52244	Insured depository institutions and credit unions with assets greater than \$10 billion (and their affiliates), and non-bank providers of consumer financial products and services, including mortgages, credit cards, debit collection, consumer reports, prepaid cards, private education loans, and payday lending.	(855) 411-CFPB (2372) www.consumerfinance.gov www.consumerfinance.gov/complaint
Board of Governors of the Federal Reserve System (FRB) Consumer Help P.O. Box 1200 Minneapolis, MN 55480	Federally insured state-chartered bank members of the Federal Reserve System	(888) 851-1920 www.federalreserveconsumerhelp.gov
Office of the Comptroller of the Currency (OCC) Customer Assistance Group 1301 McKinney Street Suite 3450 Houston, TX 77010	National banks and federally chartered savings banks/associations	(800) 613-6743 www.occ.treas.gov www.helpwithmybank.gov
Federal Deposit Insurance Corporation (FDIC) Consumer Response Center 1100 Walnut Street, Box #11 Kansas City, MO 64106	Federally insured state-chartered banks that are not members of the Federal Reserve System	(877) ASK-FDIC or (877) 275-3342 www.fdic.gov www.fdic.gov/consumers
Federal Housing Finance Agency (FHFA) Consumer Communications Constitution Center 400 7th Street, S.W. Washington, DC 20024	Fannie Mae, Freddie Mac, and the Federal Home Loan Banks	Consumer Helpline (202) 649-3811 www.fhfa.gov www.fhfa.gov/Default.aspx?Page=369 ConsumerHelp@fhfa.gov
National Credit Union Administration (NCUA) Consumer Assistance 1775 Duke Street Alexandria, VA 22314-3428	Federally chartered credit unions	(800) 755-1030 www.ncua.gov www.mycreditunion.gov
Federal Trade Commission (FTC) Consumer Response Center 600 Pennsylvania Avenue, N.W. Washington, DC 20580	Finance companies, retail stores, auto dealers, mortgage companies and other lenders, and credit bureaus	(877) FTC-HELP or (877) 382-4357 www.ftc.gov www.ftc.gov/bcp
Securities and Exchange Commission (SEC) Complaint Center 100 F Street, N.E. Washington, DC 20549-0213	Brokerage firms, mutual fund companies, and investment advisers	(202) 551-6551 www.sec.gov www.sec.gov/complaint/select.shtml
Farm Credit Administration Office of Congressional and Public Affairs 1501 Farm Credit Drive McLean, VA 22102-5090	Agricultural lenders	(703) 883-4056 www.fca.gov
Small Business Administration (SBA) Consumer Affairs 409 3rd Street, S.W. Washington, DC 20416	Small business lenders	(800) U-ASK-SBA or (800) 827-5722 www.sba.gov
Commodity Futures Trading Commission (CFTC) 1155 21st Street, N.W. Washington, DC 20581	Commodity brokers, commodity trading advisers, commodity pools, and introducing brokers	(866) 366-2382 www.cftc.gov/ConsumerProtection/index.htm
U.S. Department of Justice (DOJ) Civil Rights Division 950 Pennsylvania Avenue, N.W. Housing and Civil Enforcement Section Washington, DC 20530	Fair lending and housing issues	(202) 514-4713 TTY-(202) 305-1882 FAX-(202) 514-1116 To report an incident of housing discrimination: 1-800-896-7743 fairhousing@usdoj.gov
Department of Housing and Urban Development (HUD) Office of Fair Housing/Equal Opportunity 451 7th Street, S.W. Washington, DC 20410	Fair lending and housing issues	(800) 669-9777 www.hud.gov/complaints



1194 Montgomery Drive
 Santa Rosa, California 95405
 (707) 527-6216

Home Equity Early Disclosure

IMPORTANT TERMS OF OUR HOME EQUITY LINE OF CREDIT PLAN

This disclosure contains important information about our Home Equity Line of Credit Plan. You should read it carefully and keep a copy for your records.

AVAILABILITY OF TERMS: All of the terms described below are subject to change. If these terms change (other than the annual percentage rate) and you decide, as a result, not to enter into an agreement with us, you are entitled to a refund of any fees that you pay to us or anyone else in connection with your application.

SECURITY INTEREST: We will take a security interest in your home. You could lose your home if you do not meet the obligations in your agreement with us.

POSSIBLE ACTIONS: We can terminate your line, require you to pay us the entire outstanding balance in one payment, and charge you certain fees, if (1) you engage in fraud or material misrepresentation in connection with the plan; (2) you do not meet the repayment terms of this plan, or (3) your action or inaction adversely affects the collateral or our rights in the collateral.

We can refuse to make additional extensions of credit or reduce your credit limit if (1) any reasons mentioned above exist; (2) the value of the dwelling securing the line declines significantly below its appraised value for purposes of the line; (3) we reasonably believe that you will not be able to meet the repayment requirements due to a material change in your financial circumstances; (4) you are in default of a material obligation of the agreement; (5) government action prevents us from imposing the annual percentage rate provided for in the agreement; (6) the priority of our security interest is adversely affected by government action to the extent that the value of the security interest is less than 120 percent of the credit line; (7) a regulatory agency has notified us that continued advances would constitute an unsafe and unsound business practice, or (8) the maximum annual percentage rate is reached.

MINIMUM PAYMENT REQUIREMENTS: You can obtain credit advances for 10 years. This period is called the "draw period." At our option, we may renew or extend the draw period. After the draw period ends the repayment period will begin. The length of the repayment period will depend on the balance at the time of the last advance you obtain before the draw period ends. You will be required to make monthly payments during both the draw and repayment periods. At the time you obtain a credit advance a payoff period of 360 monthly payments will be used to calculate your payment. The payoff period will always be the shorter of the payoff period for your outstanding balance or the time remaining to the maturity date. Your payment will be set to repay the balance after the advance, at the current annual percentage rate, within the payoff period. Your payment will remain the same unless you obtain another credit advance. Your payment may also change if the annual percentage rate increases or decreases. Each time the annual percentage rate changes, we will adjust your payment to repay the balance within the original payoff period. Your payment will include any

amounts past due and any amount by which you have exceeded your credit limit, and all other charges.

MINIMUM PAYMENT EXAMPLE: If you made only the minimum monthly payment and took no other credit advances it would take 30 years to pay off a credit advance of \$10,000 at an **ANNUAL PERCENTAGE RATE** of 6.125%. During that period, you would make 359 payments of \$60.78 and one (1) final payment of \$60.13.

FEES AND CHARGES: In order to open, use and maintain a line of credit plan, you must pay the following fees to us:

- Loan Processing Fee: \$1,500.00 (Due at closing)
- Flood Zone Determination Fee: \$29.00 (Due at closing)
- Check Printing Charge: \$14.00 (Due when checks are ordered)

You must pay certain fees to third parties to open the plan. These fees generally total between \$400.00 and \$10,000.00. If you ask, we will provide you with an itemization of the fees you will have to pay third parties.

PROPERTY INSURANCE: You must carry insurance on the property that secures this plan. If the property is located in a Special Flood Hazard Area we will require you to obtain flood insurance if it is available.

REFUNDABILITY OF FEES: If you decide not to enter into this plan within three business days of receiving this disclosure and the home equity brochure, you are entitled to a refund of any fee you may have already paid.

TAX DEDUCTIBILITY: You should consult a tax advisor regarding the deductibility of interest and charges for the plan.

ADDITIONAL HOME EQUITY PLANS: Please ask us about our other available home equity line of credit plans.

ANNUAL PERCENTAGE RATE AND VARIABLE RATE FEATURE: A fixed annual percentage rate will be used for the first 5 years of the plan. An **ANNUAL PERCENTAGE RATE** of 6.00% is representative of the fixed rate we have offered with this plan. Please ask us for the current fixed rate under this plan. This plan also contains a variable rate feature beginning with the sixth year and the annual percentage rate (corresponding to the periodic rate) and the minimum payment may change as a result. The annual percentage rate includes only interest and no other costs. The annual percentage rate is based on the value of an index. The index is the weekly average yield on the United States Treasury Securities, adjusted to the Constant Maturity of (5) Five Years. A source of information about the index can be found at the Federal Reserve Economic Data website. We will use the most recent index value available to us as of 15 days before the date of any annual percentage rate adjustment. To determine the annual percentage rate that will apply to your account, we add a margin to the value of the Index. If the rate is not already rounded we then round up to the next



0.125%. Ask us for the current index value, margin and annual percentage rate. After you open a plan, rate information will be provided on periodic statements that we send you.

RATE CHANGES: The annual percentage rate can change every five (5) years on the anniversary date of opening your plan. The rate cannot increase or decrease more than 2.0 percentage points at each adjustment. The **ANNUAL PERCENTAGE RATE** cannot increase more than 6.0 percentage points above the initial rate or the maximum permitted by law, whichever is less. However, under no circumstances will your **ANNUAL PERCENTAGE RATE** go below 4.0% at any time during the term of the plan.

MAXIMUM RATE AND PAYMENT EXAMPLES: If you had an outstanding balance of \$10,000, the minimum payment at the maximum

ANNUAL PERCENTAGE RATE of 12.0% would be \$102.90. This annual percentage rate could be reached at the time of the 61st payment.

HISTORICAL EXAMPLE: The following table shows how the annual percentage rate and the minimum payments for a single \$10,000 credit advance would have changed based on changes in the index over the past 15 years. The index values are as of the first week ending in July of each year. While only one payment per year is shown, payments may have varied during each year. The table assumes that no additional credit advances were taken, that only the minimum payments were made, and that the rate remained constant during each year. It does not necessarily indicate how the index or your payments will change in the future.

U.S. TREASURY SECURITIES (5-YEAR) INDEX TABLE

Year (as of the first week ending in July)	Index (Percent)	Margin ⁽¹⁾ (Percent)	ANNUAL PERCENTAGE RATE	Monthly Payment (Dollars)
2008.....	3.320	3.000	6.000 ⁽²⁾	\$59.99
2009.....	2.500	3.000	6.000 ⁽²⁾	\$59.99
2010.....	1.800	3.000	6.000 ⁽²⁾	\$59.99
2011.....	1.670	3.000	6.000 ⁽²⁾	\$59.99
2012.....	0.670	3.000	6.000 ⁽²⁾	\$59.99
2013.....	1.450	3.000	4.500	\$51.74
2014.....	1.680	3.000	4.500 ⁽³⁾	\$51.74
2015.....	1.650	3.000	4.500 ⁽³⁾	\$51.74
2016.....	1.010	3.000	4.500 ⁽³⁾	\$51.74
2017.....	1.940	3.000	4.500 ⁽³⁾	\$51.74
2018.....	2.730	3.000	5.750	\$57.42
2019.....	1.780	3.000	5.750 ⁽³⁾	\$57.42
2020.....	0.290	3.000	5.750 ⁽³⁾	\$57.42
2021.....	0.880	3.000	5.750 ⁽³⁾	\$57.42
2022.....	3.110	3.000	5.750 ⁽³⁾	\$57.42

⁽¹⁾ This is a margin we have used recently; your margin may be different.

⁽²⁾ This **ANNUAL PERCENTAGE RATE** reflects a fixed rate that we have provided recently, your plan may reflect a different amount.

⁽³⁾ This **ANNUAL PERCENTAGE RATE** is the same as the previous rate since the rate can only change every 60 months.





P.O. Box 2507, Santa Rosa, CA 95405
(707) 527-6216 • Fax: (707) 527-6835

RIGHT TO RECEIVE A COPY OF APPRAISALS

Lender: **Sonoma Federal Credit Union**

Date: _____

NOTICE TO FIRST-LIEN DWELLING-SECURED CREDIT APPLICANTS:

We may order an appraisal to determine the property's value and charge You for this appraisal. We will promptly give You a copy of any appraisal, even if Your loan does not close.

You can pay for an additional appraisal for Your own use at Your own cost.

Other than as prohibited by law, We may charge You a reasonable fee to reimburse Us for the appraisal costs that We incur in connection with such appraisal or other written valuation. We will not however, charge You for any photocopy costs, postage costs, administrative costs, or other costs We incur in providing the copy(ies).

To obtain additional information on Your right to receive a copy of appraisals, including the amount of the reasonable fee that We may require You to pay, please contact Us at _____.