



**SELECT PORTFOLIO
MANAGEMENT, INC.**
Integrated Wealth Management
A Registered Investment Advisor



White Paper

Home Ownership:

Alternative Ways to Fund Your Down Payment

www.selectportfolio.com • Toll Free 800.445.9822 • Tel 949.975.7900 • Fax 949.900.8181

Securities offered through Securities Equity Group Member FINRA, SIPC, MSRB

Table of Contents

Alternative Ways to Fund Your Down Payment	3
How much money will you need for a down payment?	3
Funding alternatives	3
Disclosures	6

Alternative Ways to Fund Your Down Payment

How much money will you need for a down payment?

It used to be that most lenders would require a down payment equal to at least 20 percent of a home's purchase price. Today, however, there's good news for homebuyers who have little money saved for a down payment. Many lenders have relaxed their requirements and are approving loans with lower down payments. In addition, there are numerous private and government-sponsored low down payment mortgage programs, such as those offered by Fannie Mae, Freddie Mac, the Federal Housing Administration, and the Department of Veterans Affairs.

However, if you've done all you can to save for a down payment and it's still not enough, don't worry-- you have other options. The following are some alternative methods you can use to help fund your down payment.

Caution: Keep in mind that if your down payment is less than 20 percent, you may have to pay private mortgage insurance (PMI), which can equal .5 to 1.25 percent of your total loan amount at closing.

Funding alternatives

Rent with option to buy

A rent with option to buy (also known as a lease with option to purchase, lease purchase, or lease option) allows you to rent a home for a certain period of time (e.g., three years) while a portion of your rental payments accumulate and are credited toward your down payment. At the end of the lease term, you have the option to purchase the home for a specified price. If you choose not to exercise the purchase option, it usually expires. These arrangements often require you to pay a nonrefundable fee (referred to as an option fee), which can be as much as 2 to 3 percent of the purchase price.

Shared equity financing

A shared equity arrangement can be structured in many ways. However, it typically involves an investor who supplies all or a portion of the down payment on the home. The investor may also take a partial ownership interest in the house and make part of each monthly mortgage payment. Meanwhile, you live in the home, make the payments on the mortgage, and pay fair market rent to the investor for the portion of the home that he or she owns. At a point in time that is specified in the equity-sharing agreement (e.g., after the home is sold or after a certain time period), the investor is entitled to receive the money for the down payment back, plus a share of any appreciation that has occurred.

Borrow from the cash value of a life insurance policy

If you have accumulated a substantial cash value in your life insurance policy, you may be able to borrow from it in order to raise funds for a down payment. You may be able to borrow up to 90 percent of your policy's cash value, and the interest rate is usually substantially lower than rates for bank loans and credit cards. However, any outstanding loan balance will be subtracted from your death benefit when you die, reducing the amount your beneficiaries will receive upon your death.

Borrow against your assets/convert assets to cash

Another option is to borrow against your assets (e.g., personal property, fixed-income investments) to raise money for a down payment. When you borrow against an asset, the asset becomes collateral for a loan. You still own the asset, but the lender takes a security interest in it. If you fail to repay the loan as promised, the lender has the right to take legal action to acquire the asset and sell it to repay your outstanding debt.

You may also want to sell, redeem, or otherwise liquidate an asset in order to come up with a source of funds for a down payment. While you can easily determine the value of certain assets, such as fixed-income investments, placing a value on other types of assets (e.g., personal property) requires some additional research. So, you may want to enlist the services of a qualified appraiser to help you estimate the asset's value.

Caution: Liquidating assets can have tax ramifications. See Income from Sale or Exchange of Property.

Gifts

Most mortgage lenders allow gifts to be used for part of the down payment on a home. However, lenders often require borrowers to contribute some of their own money toward a down payment in addition to any gifts. You'll also need to submit a letter to your lender that proves that the money is a gift rather than a loan, and that you are not expected to repay the funds. You may also have to submit documentation, such as bank statements, showing the funds withdrawn from your benefactor's account and deposited into your account.

Borrow from an employer-sponsored retirement plan

If you participate in an employer-sponsored retirement plan, one way to come up with money for a down payment is to borrow the money from your plan. Many employer-sponsored retirement plans (e.g., 401(k) plan) allow you to borrow against the funds in your account. Depending on the rules established by your employer, you may be able to borrow against your own contributions and the earnings on this money. You may also be able to borrow against contributions made by your employer if you are vested in those dollars. Interest rates on these types of loans are generally only one or two points above the prime rate. Although loans from retirement plans generally must be paid back within

five years, the repayment period can be longer if funds are used to purchase a primary residence. Many plans carry restrictions, so consult your plan administrator for more details.

Caution: If you leave your employer before you repay a loan from an employer-sponsored retirement plan, the balance of your plan loan will typically be due immediately. If it's not repaid on time, the loan balance will be deemed a distribution for tax purposes, and you may be subject to the 10 percent penalty tax.

Withdraw from a traditional IRA

You can withdraw funds from your traditional IRA and use them for a down payment. However, all or part of a distribution from a traditional IRA must be included in taxable income in the year received. While funds distributed prior to age 59½ are generally subject to a premature distribution penalty, an exception applies when the distribution is used within 120 days to pay the costs of acquiring, constructing, or reconstructing the principal residence of a first-time homebuyer. There is a \$10,000 lifetime limit on distributions covered by the first-time homebuyer exception, however.

Withdraw from an employer-sponsored retirement plan

If your plan allows, you may be able to take a distribution from your employer-sponsored retirement plan and use the funds for a down payment. You'll want to consult your plan administrator to find out what options, if any, are available to you. Before you withdraw from an employer-sponsored plan, however, keep in mind that distributions from an employer-sponsored plan generally must be included in taxable income in the year received. In addition, a 10 percent federal penalty tax may be assessed on distributions made before age 59½. See Premature Distribution Penalty for more information.

Caution: Taking money out of your retirement plan to apply to the purchase of a home should be done only after careful consideration--it is generally not recommended.

Disclosures

This material does not constitute the rendering of investment, legal, tax or insurance advice or services. It is intended for informational use only and is not a substitute for investment, legal, tax, and insurance advice.

State, national and international laws vary, as do individual circumstances; so always consult a qualified investment advisor, attorney, CPA, or insurance agent on all investment, legal, tax, or insurance matters.

The effectiveness of any of the strategies described will depend on your individual situation and on a number of other factors. After reviewing your personal situation, we may recommend that you not use any strategy in this document but instead consider various other strategies available through our practice.

Securities offered through Securities Equity Group, member FINRA, SIPC, MSRB

Copyright 2006 Forefield, Inc. All rights reserved.