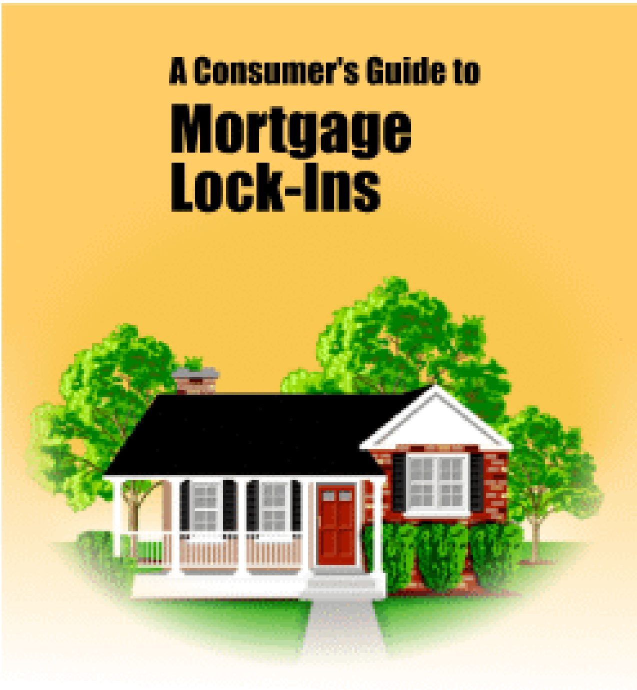
The Federal Reserve Board



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When you’re looking for a mortgage, you’re likely to shop among lenders for the most favorable interest rate, and the lowest points and other up-front charges. When you find the most favorable terms and the lender that you want, you’ll apply to that lender. But when you get to settlement, will you actually receive the terms you applied or bargained for? Or will you find that the rate has changed -- and that your costs have gone up?

Lock-ins on rates and points might offer you a way to ensure that what you shop for is what you get. This brochure explains what these arrangements mean.

All About Lock-Ins

In most cases, the terms you are quoted when you shop among lenders only represent the terms available to borrowers settling their loan agreement at the time of the quote. The quoted terms may not be the terms available to you at settlement weeks or even months later. Therefore, you should not rely on the terms quoted to you when shopping for a loan unless a lender is willing to offer a lock-in.

What Is a Lock-In?

A lock-in, also called a rate-lock or rate commitment, is a lender's promise to hold a certain interest rate and a certain number of points for you, usually for a specified period of time, while your loan appli-cation is processed. (Points are additional charges imposed by the lender that are usually prepaid by the consumer at settlement but can sometimes be financed by adding them to the mortgage amount. One point equals one percent of the loan amount.) Depending upon the lender, you may be able to lock in the interest rate and number of points that you will be charged when you file your application, during processing of the loan, when the loan is approved, or later.

A lock-in that is given when you apply for a loan may be useful because it's likely to take your lender several weeks or longer to prepare, document, and evaluate your loan application. During that time, the cost of mortgages may change. But if your interest rate and points are locked in, you should be protected against increases while your application is processed. This protection could affect whether you can afford the mortgage. However, a locked-in rate could also prevent you from taking advantage of price *decreases*, unless your lender is willing to lock in a lower rate that becomes available during this period.

It is important to recognize that a lock-in is not the same as a *loan commitment,* although some loan commitments may contain a lock-in. A loan commitment is the lender's promise to *make you a loan* in a specific amount at some future time. Generally, you will receive the lender's commitment only after your loan application has been approved. This commitment usually will state the loan terms that have been approved (including loan amount), how long the commitment is valid, and the lender's conditions for making the loan such as receipt of a satisfactory title insurance policy protecting the lender.

Will Your Lock-In Be In Writing?

Some lenders have preprinted forms that set out the exact terms of the lock-in agreement. Others may only make an oral lock-in promise on the telephone or at the time of application. Oral agreements can be very difficult to prove in the event of a dispute.

Some lenders' lock-in forms may contain crucial information that is difficult to under-stand or that is in fine print. For example, some lock-in agreements may become void through some unrelated action such as a change in the maximum rate for Veterans Administration guaranteed loans. Thus, it is wise to obtain a blank copy of a lender's lock-in form to read carefully before you apply for a loan. If possible, show the lock-in form to a lawyer or real estate professional.

It is wise to obtain written, rather than verbal, lock-in agreements to make sure that you fully understand how your lender's lock--ins and loan commitments work and to have a tangible record of your arrangements with the lender. This record may be useful in the event of a dispute.

Will You Be Charged for a Lock-In?

Lenders may charge you a fee for locking in the rate of interest and number of points for your mortgage. Some lenders may charge you a fee up-front, and may not refund it if you withdraw your application, if your credit is denied, or if you do not close the loan. Others might charge the fee at settlement. The fee might be a flat fee, a percentage of the mortgage amount, or a fraction of a per-centage point added to the rate you lock in. The amount of the fee and how it is charged will vary among lenders and may depend on the length of the lock-in period.

What Options Are Available for Set-ting the Mortgage Terms?

Lenders may offer different options in establishing the interest rate and points that you will be charged, such as:

- **Locked-In Interest Rate--Locked-In Points.** Under this option, the lender lets you lock in both the interest rate and points quoted to you. This option may be considered to be a true lock-in because your mortgage terms should not increase above the interest rate and points that you've agreed upon even if market conditions change.
- **Locked-In Interest Rate--Floating Points.** Under this option, the lender lets you lock in the interest rate, while permit-ting or requiring the points to rise and fall (float) with changes in market conditions. If market interest rates drop during the lock-in period, the points may also fall. If they rise, the points may increase. Even if you float your points, your lender may allow you to lock-in the points at some time before settlement at whatever level is then current. (For instance, say you've locked in a 10½ percent interest rate, but not the 3 points that went with that rate. A month later, the market interest rate remains the same, but the points the lender charges for that rate have dropped to 2½. With your lender's agreement, you could then lock in the lower 2½ points.) If you float your points and market interest rates increase by the time of settlement, the lender may charge a greater number of points for a loan at the rate you've locked in. In this case, the benefit you might have had by locking in your rate may be lost because you'll have to pay more in up-front costs.
- **Floating Interest Rate--Floating Points.** Under this option, the lender lets you lock in the interest rate and the points at some time after application but before settlement. If you think that rates will remain level or even go down, you may want to wait on locking in a particular rate and points. If rates go up, you should expect to be charged the higher rate.

Because practices vary, you may want to ask your lender whether there are other options available to you.

How Long Are Lock-Ins Valid?

Usually the lender will promise to hold a certain interest rate and number of points for a *given number of days*, and to get these terms you must settle on the loan within that time period. Lock-ins of 30 to 60 days are com-mon. But some lenders may offer a lock-in for only a short period of time (for example, 7 days after your loan is approved) while some others might offer longer lock-ins (up to 120 days). Lenders that charge a lock-in fee may charge a higher fee for the longer lock-in period. Usually, the longer the period, the greater the fee.

The lock-in period should be long enough to allow for settlement, and any other contin-gencies imposed by the lender, before the lock-in expires. Before deciding on the length of the lock-in to ask for, you should find out the average time for processing loans in your area and ask your lender to estimate (in writ-ing, if possible) the time needed to process your loan. You’ll also want to take into account any factors that might delay your set-tlement. These may include delays that you can anticipate in providing materials about your financial condition and, in case you are purchasing a new house, unanticipated con-struction delays. Finally, ask for a lock-in with as few contingencies as possible.

What Happens If the Lock-in Period Expires?

If you don’t settle within the lock--in period, *you might lose* the interest rate and the number of points you had locked in. This could happen if there are delays in processing whether they are caused by you, others involved in the settlement process, or the lender. For example, your loan approval could be delayed if the lender has to wait for any documents from you or from others such as employers, appraisers, termite inspectors, builders, and individuals selling the home. On occasion, lenders are themselves the cause of processing delays, particularly when loan demand is heavy. This sometimes happens when interest rates fall suddenly.

If your lock-in expires, most lenders will offer the loan based on the prevailing interest rate and points. If market conditions have caused interest rates to rise, most lenders will charge you more for your loan. One reason why some lenders may be unable to offer the lock-in rate after the period expires is that they can no longer sell the loan to investors at the lock-in rate. (When lenders lock in loan terms for borrowers, they often have an agreement with investors to buy these loans based on the lock-in terms. That agreement may expire around the same time that the lock-in expires and the lender may be unable to afford to offer the same terms if market rates have increased.) Lenders who intend to keep the loans they make may have more flexibility in those cases where settlement is not reached before the lock-in expires.

How Can You Speed Up the Approval of the Loan?

While the lender has the greatest role in how fast your loan application is processed, there are certain things you can do to speed up its approval. Try to find out what documentation the lender will require from you.

Much of the information required by your lender can be brought with you when you apply for a loan. This may help to get your application moving more quickly through the process. When you first meet with your lender, be sure to bring the following documents:

- The *purchase contract* for the house (if you don't have the contract, check with your real estate agent or the seller).
- Your *bank account numbers,* the *address of your bank branch* and *your latest bank statement,* plus *pay stubs, W-2 forms,* or other proof of employment and salary, to help the lender check your finances.
- If you are self-employed, *balance sheets, tax returns for 2-3 previous years,* and other information about your business.
- Information about debts, including *loan and credit card account numbers* and the n*ames and addresses of your creditors.*
- Evidence of *your mortgage or rental payments*, such as cancelled checks.
- Certificate of Eligibility from the Veterans Administration if you want a VA-guaranteed loan. Your lender may be able to help you obtain this.

Be sure to respond promptly to your lender's requests for information while your loan is being processed. It is also a good idea to call the lender and real estate agent from time to time. By calling occasionally, you can check on the status of your application, and offer to help contact others such as employers who may need to provide documents and other information for your loan. It is also helpful to keep notes on your contacts with the lender so that you will have a record of your conversations.

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Ask About Lock-Ins

When you’re ready to settle on your loan, you’ll want to get the loan terms that you’ve locked in. To increase that likelihood, it is important to learn as much as you can about what the lender is promising you before you apply for a loan. *Ask for the following infor-mation when you shop for a loan:*

Lock-Ins and Fees

- Does the lender offer a lock-in of the interest rate and points?
- When will the lender let you lock in the interest rate and points? When you apply? When the loan is approved?
- Will the lock-in be in writing? If the lock-in is not in writing, you will have no record of the lender’s agreement with you in case of a dispute.
- Does the lender charge a fee to lock in your interest rate? Does the fee increase for longer lock-in periods? If so, how much?
- If you have locked in a rate, and the lender’s rate drops, can you lock in at the lower rate? Does the lender charge you an additional fee to lock in the lower rate?
- Can you float your interest rate and points for now, and lock them in later?

Loan Processing Time

- How long does the lender expect to take to process your loan?
- What has been the lender’s average time for processing loans recently?
- Has the lender’s loan volume increased? Heavy volume might increase the lender’s average processing time.

Expiration of Lock-ins

- What rate will be charged if the lock-in expires before settlement-the rate in effect when the lock-in expires?

- If you don’t settle within the lock-in period, will the lender refund some or all of your application or lock-in fees if you decide to cancel the loan application?
- If your lock-in expires and you want to get another lock-in at the rate in effect at the time of the expiration, will the lender charge an additional fee for the second lock-in?

Complaints About Lock-Ins

Knowing what to look for puts you in a better position to decide whether, when, and how long to lock in mortgage terms. Also, by helping to keep the loan process moving, you can lessen the chance that your lock-in will run out before settlement.

But what if your lock-in does lapse? If you believe that the lapse was due to delays caused by the lender or someone else involved in the loan process, you should try first to reach a mutually satisfactory agree-ment with the lender. If that effort fails, con-sider writing to the appropriate state or fed-eral regulatory agency.

Some lender actions, such as offering lock--in terms which are impossible to fulfill, fail-ing to process your loan diligently, or caus-ing your lock-in to expire are improper-and may even be illegal. In addition, because you may have contractual rights under your lock--in or loan commitment, you may want to consult with an attorney. Be aware, though, that complaints may not be resolved as quickly as may be necessary for a home purchase.

Depending upon their authority under applicable state or federal law, regulatory agencies may either attempt to help you resolve your complaint directly or record your complaint and recommend other action.

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