

What are “points” and who pays them?



What is a point?

A point is equal to one percent (1%) of a mortgage amount. For example, on a \$120,000 mortgage, one point is \$1,200.

Are there different types of points?

Customarily points are quoted as something plus one. For instance, a 10% interest rate with points of three plus one: The one point is a loan origination fee which pays the cost of processing the mortgage; the three points are discount points.

What is the purpose of discount points?

Discount points are used to purchase a lower rate of interest over the life of a mortgage. For example, let's say that a house is selling for \$100,000 and the mortgage is \$80,000. There are two rates of interest quoted: 10% with points of two and one; 10.5% with points of zero plus one. Principal and interest at 10% for thirty years on \$80,000 is \$702.06; at 10.5% it is \$731.79. Thus for an up-front fee of \$1,600 (2% of \$80,000), the borrower will pay \$29.73 less each month for thirty years.

Who decides what points are?

Points are determined by the return demanded by the final investor on a loan. In other words, investors place open market bids for mortgages at different interest rates.

Who pays these points?

Except in the case of VA loans, the issue of who pays discount points is negotiable between buyer and seller.

Why would a buyer pay points?

The obvious advantage to a buyer is the lower payment on a mortgage.

What are the advantages of the seller paying points?

There are a number of potential advantages to sellers in these cases:

- Some buyers do not have the funds to pay points themselves and cannot or will not qualify for a lower rate of interest.
- Lower payments qualify more buyers for property. This results in more potential buyers for a home, meaning possibly a higher selling price.
- Lower payments which qualify more buyers can result in a quicker sale.
- Points are customary in most real estate transactions. Some buyers will refuse to consider a property where the seller refuses to negotiate.

To sum it up...

Points offer buyers and sellers more options. If a lender has mortgages available at 8%, ask yourself how that lender could or would lend money for the same terms at 7%. The lender can't. Points expand the ways that a real estate transaction can be completed.

