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8 Key Facts About Your Mortgage APR

credit.com By Scott Sheldon | Credit.com – Wed, May 22, 2013 7:30 AM EDT

Securing a mortgage today requires careful consideration of all the figures associated with the transaction. The biggest figures most homebuyers pay attention to include loan amount, interest rate, closing costs and the one most benign to consumers, the annual percentage rate (APR for short), which is a disclosure item required in loan advertisements and loan disclosures.

Set forth by TILA (Truth In Lending Act) and overseen by the Fed, APR is touted as most accurate barometer to compare mortgage offers from one offer to another. In comparing mortgages, there is oftentimes inaccurate distinctions made with regard to disclosures between APR and interest rate, and what consumers are actually borrowing that creates confusion around the numbers. Here are some terms you need to understand to cut through the confusion.

Annual Percentage Rate (APR): A function of blending the closing costs associated with the loan transaction and re-amortizing that figure over the term of the loan.

Interest Rate: The actual interest rate tied to the amount of money being borrowed. Also called a “note rate,” it is what determines the amount of interest you’ll pay over the life of the loan on an amortization schedule.

The Facts About Mortgage Annual Percentage Rate

Fact: The annual percentage rate does not determine the monthly mortgage payment. The note rate is what determines the monthly mortgage payment.

Fact: Lenders must disclose the annual percentage rate on their loan disclosures after you submit a mortgage application.

Fact: The APR is usually within a .125% range above the note rate. This is positive because it indicates your closing costs are very small in relationship to the amount being borrowed and the interest rate (note rate) you are receiving.

Fact: If the APR is substantially over the .125% range above the note rate, this is an indicator of higher fees (closing costs) associated with the amount borrowed.

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Fact: The APR is higher than the note rate because the APR takes into consideration a “blending” of the interest rate and closing costs over the life of the loan.

Fact: APR is not paid over the term of the loan — for example, 360 months representing a 30-year fixed rate mortgage. The note rate is the interest rate paid over the term of the loan.

Fact: The APR is a measuring tool used upfront to compare mortgage offers only, usually during the initial application process in comparing different loans.

Fact: APR represents the total cost picture in securing a mortgage, not the total interest paid over the life of the loan.

While APR is the standard used to compare mortgages, it is not the only way to compare mortgages. Rather than trying to figure out the intricacies of APR, consumers could also be served by comparing the following items to determine what mortgage choice is ideal.

These include:

- Loan term
- Interest rate
- Closing costs

- One loan term versus another
- Closing costs recapture (determined by taking amount of closing costs divided by payment savings)

One last takeaway: The mortgage with the financing terms most consistent with your long-term goals and objectives is the ideal direction to take.

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