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Mortgage Interest Buydowns Can Benefit Both Buyers and Sellers

Let's Talk Home Financing

By JIM SMITH Realtor®

Interest rates have doubled in the last year. Buyers have reduced buying power at higher rates, and sellers are seeing their listings take longer to go under contract. Lowering the list price is one strategy to entice buyers, but that makes a nominal difference in terms of the monthly payment for a prospective purchaser.

I talked with **Jaxzann Riggs** at **The Mortgage Network** to learn how buying down the interest rate can take the sting out of rising rates and more importantly, how sellers might employ the offer of a buydown to increase the number of offers received.

There are two types of buydowns — temporary and permanent, and each has its own benefits, but the ***MOST*** important thing to know about buydowns is that ***they can be paid for by either the buyer or the seller.***

Let's look at both options for a fictitious buyer. Rebecca is interested in a house that is listed for $695,000. She is planning on putting 20% down, and her mortgage broker quoted her a rate of 5.454%, with a monthly P&I payment of $3,141. This payment is a little above what Rebecca was hoping for, so she is thinking about asking the seller to assist with the cost of an interest rate buydown.

Temporary buydowns allow the seller or the buyer to contribute money to an escrow account for the benefit of the buyer at the time of closing. A portion of the escrow is used each month to reduce the borrower's payments for a set amount of time. A "**2-1 Buydown**" is a common option that decreases the interest rate for the first two years of the mortgage. The rate is 2% lower the first year, and 1% lower the second. While the buyer's mortgage contract is always going to reflect the note rate, the buydown escrow is used to pay the remaining interest balance each month. To ensure that she can afford the full monthly payment, she must qualify for the loan based on the note rate.

In Rebecca's scenario, a 2-1 buydown will cost $11,968, and would lower her first year's monthly payments to $2,482, equivalent to an interest rate of 3.454%. This is a monthly savings of $659, which will be paid out of the buydown account. The second year she will pay $2,802 monthly, comparable to a 4.454% rate, with a savings of $339 a month. The third year she will have exhausted the subsidized funds and she will pay the full payment of $3,141 for the remainder of the loan. While the effects of this option only last a couple of years, the monthly savings are significant and for borrowers who anticipate increases in income, this can make home ownership more of possibility.

Permanent Buydowns allow the rate to be "bought down" for the life of the loan. "Points" are paid to the lender at the time of closing in exchange for a lower rate for the life of the loan. While the monthly savings aren't quite as dramatic as with the temporary buydowns, the benefit will continue throughout the life of the mortgage.

For Rebecca, the dollars that she would spend for a temporary buydown, $11,968 would buy her rate down to 4.796% for 30 years, lowering her monthly payments to $2,968, saving her $157 a month versus a payment based upon a current rate of 5.45%. Again, this buydown could be paid for by the seller instead of lowering their sale price, to make their listing more attractive to more buyers.

The bottom line is that buydowns make sense for some. And sellers who are willing to participate in the cost of buydowns will dramatically increase their buying pool.

If you would like more information about buydowns, call **Jaxzann** at **(303) 990-2992.**