FREMONT BANK

MORTGAGE APPLICATION BOOKLET

Thank you for applying for a real estate loan with Fremont Bank. We understand how important it is to make the right choice when it comes to financing. You want a competitive rate with flexible terms. You want to work with people who know the market and can process your loan quickly and easily — without a lot of hassle.

At Fremont Bank we've got the perfect solution.

Whether you're a first-time home buyer, an experienced borrower, or looking to refinance your present home, we are committed to making the financing experience a positive one. And, what's more… we make it as easy as possible.

EQUAL HOUSING LENDER

MEMBER FDIC

BORROWER'S DOCUMENT CHECKLIST

If this is a purchase transaction, please provide a copy of the sales agreement. If you are paying alimony or child support, please provide your Divorce Decree or Child Support papers.

It's fast and easy to apply by phone!

Call toll-free to apply by phone or to set up an appointment

800-659-7334

9:00 am to 6:00 pm

Monday – Friday

Apply online at

www.fremontbank.com

Fremont Bank

P.O. Box 5101

Fremont, CA

94537-5101

Salaried (without other income)

- Pay stubs for the most recent month
- Last two years' W-2 forms
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

Salaried (with other income)

- Pay stubs for the most recent month
- Last two years' W-2 forms
- Last two years' completed personal Federal tax returns
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

Self-employed

- Last two years' completed personal Federal tax returns
- Year-to-date Profit and Loss Statement
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

A partner in a Limited Partnership

- Last two years' completed personal Federal tax returns (1040)
- Prior two years' K-1 forms
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

A partner in a General Partnership

- Last two years' completed personal Federal tax returns
- Year-to-date Profit and Loss Statement
- Prior two years' Federal Partnership tax returns (1065)
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

A Major Shareholder of a Corporation

- Pay stubs for the most recent month
- Last two years' W-2 forms
- Last two years' complete personal Federal Tax Returns (1040)
- Year-to-date Profit and Loss Statement
- Prior two years' Corporate Federal Tax Returns (1120)
- Current mortgage statements and payment coupons for all mortgages
- Copies of three most recent statements of deposits including retirement accounts, stocks and bonds
- Copy of current Homeowners' Insurance declaration page showing premium, coverage for fire and hazard insurance, and any other coverage

Other Income

Retirement/Social Security

Social Security Award Letter or two months' deposit statements (if direct deposit)

Child Support/Alimony

Divorce Decree or Child Support Papers*

Rental Income

Rental/Lease Agreement (if not on tax returns)

Trust

Signed Trust Agreement or Trust Certification

Important Information about Opening a New Account

To help the government fight the funding of terrorism and money laundering activities, U.S. Federal law requires financial institutions to obtain, verify, and record information that identifies each person (individuals and businesses) who opens an account. What this means for you: when you open an account, we will ask for your name, address, date of birth and other information that will allow us to identify you. We may also ask for your driver's license or other identifying documents.

During this application process Fremont Bank may verify your identity using commercially available databases containing information from public records, other financial institutions and consumer reporting agencies.

* Alimony, child support or separate maintenance income need not be revealed if you do not choose to have it considered as a basis for determining credit worthiness.

No Closing Cost Loans

If you close your Fremont Bank loan under a “No Closing Cost” Loan Program, there will be no charge for the following customary closing costs for a mortgage loan.

- Appraisal
- Credit Report
- Reconveyance Tracking
- Title Insurance
- Courier Expense
- Wire Fee*
- Points
- Tax Service
- Loan Origination
- Loan Documentation
- Escrow
- Notary
- Recording*
- Flood Certification & Monitoring

* Fremont Bank Documents

Only those costs listed above will be paid by Fremont Bank. If your application is for a loan to purchase a home, all other customary costs associated with the purchase transaction (including title company document preparation fees) will be paid by you. If your application is for a refinance loan, you will be responsible for paying all fees and charges imposed directly or indirectly by an existing third party lender (for example, a payoff demand statement fee and/or a reconveyance fee). Loans with lower nominal rates may be available for borrowers willing to pay points and/or closing costs.

Closing costs **DO NOT** include the following: interest; mortgage, hazard, flood, or earthquake insurance premiums; property or transfer taxes; impounds; structural pest control, roof, or other inspections. The “No Closing Cost" Loan Programs do not include extraordinary items, including, but not limited to, the following: the additional cost of a “complex" residential real estate appraisal (as defined under federal appraisal guidelines); additional credit reports for the same loan transaction; redrawing of loan documents due to changes requested by you; and grant deeds and any associated notary and recording fees. Additionally, if your application is for a refinance loan, you will be responsible for paying any prepayment penalty on an existing loan, whether imposed by a third party lender or by Fremont Bank.

2-to-4 Family Reduced Closing Cost Loan Programs

“No Closing Cost" loans are only available for loans secured by a single-family dwelling. For 2-4 family homes, the borrowers will pay a part of the closing costs shown above. If your loan is approved, and you close your loan under the reduced cost loan program, $300 of the application fee will be refunded through escrow. However, the application fee is not refundable if: 1) your loan is declined; 2) your application is withdrawn by you; or 3) your application is approved, but your loan does not close for any reason.

Point and Fee

Fremont Bank offers loans with points and/or fees (Closing Costs) which may have a lower nominal interest rate than “No Closing Costs" loans. Generally, loans with fees and no points (“Zero Point" or “0 Point") are available, as are loans with one (1) or two (2) points. Additionally, we may offer loans with points and no fees. Closing Costs (fees) range from approximately $1,800 to $2,500 (plus interest) for conforming loans and up to $3,500 (plus interest) for jumbo loans (up to $650,000). Please ask about available programs.

Application Fee

You may be required to pay an application fee as indicated to Fremont Bank for a loan or line of credit. This fee is non-refundable if your loan does not close for any reason or if you choose other than a “No Closing Cost” Loan Program. If your loan is approved and you close your loan under a “No Closing Cost" Loan Program, the application fee, or $300 of the application fee in the case of 2-to-4 family reduced closing cost Loan Program, will be refunded through escrow (on refinances see your HUD-1A).

However, the application fee is not refundable if:

1. your loan is declined;
2. your application is withdrawn by you;
3. your application is approved, but your loan does not close for any reason; or
4. you change to or apply for a Loan Program other than a “No Closing Cost” Loan Program; any application fee you have paid will be credited toward fees and/or points charged under that Loan Program.

Once your loan is closed (funded), withdrawn or declined, Fremont Bank will not accept a new First Mortgage application to refinance the same property for a period of ninety (90) days.

Single Family Loans
First Mortgage Loans, Conforming Owner Occupied - $395
First Mortgage Loans, Conforming Non-Owner Occupied - $495
First Mortgage Loans, Jumbo Conforming and Jumbo - $495

Ask whether your loan is Conforming, Jumbo or Jumbo Conforming.

2-4 Family Loans - $750

Rate Lock Fee

You may be required to pay a rate lock fee as indicated to Fremont Bank at the time you lock in the rate on your loan. If your loan is approved, and you close your loan under a “No Closing Cost" Loan Program, the rate lock fee will be refunded at closing. The rate lock fee will be refunded only if Fremont Bank declines your loan application due to income or credit qualifying reasons.

However, the rate lock fee is not refundable if:

1. you decide to withdraw your application, or
2. your application is approved and you fail to close, or fails to fund for any reason, or
3. you provided any significantly inaccurate information or omit any significant information, whether in your application or otherwise.

If you change to or apply for a Loan Program other than a “No Closing Cost” Loan Program, any rate lock fee you have paid will be credited toward fees and/or points charged under that Loan Program.

Interest Rates on Mortgage Loans

Floating Rate at Application
The rate on a Fremont Bank mortgage loan application is not "locked in" at the time of application. Unless specified otherwise in a written rate lock confirmation, the interest rate, points, and/or origination fee for your loan will be set at the time your loan documents are prepared for signature, and therefore, may be higher or lower than the rate, points, and/or origination fee at the time of application.

The interest rate for your pending loan will continue to fluctuate until the date that the Bank is ready to prepare your loan documents for signing. When Fremont Bank is ready to prepare your loan documents for signing, you will be contacted by a representative and only then will the interest rate for your loan be established. Once the rate is established, failure by the borrower to close the loan will result in cancellation of the rate lock and forfeiture of the application fee.

Rate Lock Agreement
For certain loan programs, you may request that the rate on your loan application be "locked in". If rates subsequently go up, you will not pay the higher rate; however, if rates drop, you will not benefit. Ask for a copy of the agreement, or speak with your loan officer for more information.

Interim Interest
Interim Interest (sometimes referred to as Odd Days Interest) is calculated on the loan balance from the date the loan proceeds are disbursed to the first day of the following month. Regularly scheduled payments pay interest for full months. At Fremont Bank's option, this interest payment may be made at the time of loan closing or billed at or after loan closing. Any billed interim interest will be due on the tenth day of the following month with no grace period.

How We Calculate Interest
The interest accrual method is calculated based on a 30-day month and a 360 day year.

Insurance

Property Insurance
We require fire and hazard insurance coverage with an insurance carrier acceptable to the Bank in an amount at least equal to the lesser of:

- the loan amount (as long as it equals the minimum amount required under the terms of coverage to fully compensate for damage or loss to the dwelling on a replacement cost basis), or
- 100% replacement value of the improvements with deduction for depreciation.
- The lender cannot require hazard insurance coverage on your property in excess of the replacement value of the improvements.

A guaranteed Replacement Cost Endorsement is required whenever available. A Lender's Loss Payable Endorsement (Form 438-BFU) in favor of the Bank must be attached to the policy. In order to utilize your current policy, we require an endorsement to the policy changing the mortgagee clause to read as follows:

Fremont Bank, its successors or assignees
PO Box 7295
Fremont CA 94537-7295

Refinance - For refinance loans, existing policies must have a minimum of three months remaining on the term from the date of closing or the next year's premium must be paid at or before closing.

Purchase - For purchase money loans, at least one full year's premium must be paid in advance.

Flood Insurance
The Flood Disaster Protection Act of 1973 requires lenders under the jurisdiction of Federal entities (FDIC for Fremont Bank) to require that loans secured by improved real property have flood insurance coverage when the properties are in a Special Flood Hazard Area as defined by the Federal Emergency Management Agency (FEMA).

Fremont Bank will be making a determination during the underwriting process as to whether or not your property is located in a Special Flood Hazard Area, and if flood insurance will be required.

Flood insurance may be required at a later time if there are changes to the area designated as Special Flood Hazard Areas. If flood insurance becomes necessary, you will be notified in writing.

Private Mortgage Insurance
Private Mortgage Insurance (sometimes referred to as PMI or MI) is required on first mortgage loans where the loan to value ratio exceeds 80%. For owner-occupied loans, the PMI will be dropped by federal law when your loan reaches a loan-to-value ratio of 78% based on the value at the time your loan was approved. If certain requirements are met, you may be able to drop the PMI sooner. Please call Customer Service for more information.

Impounds (Escrow Account)

Establishment of an impound (escrow) account for payment of such obligations as property taxes and/or insurance premiums, will not be required as a condition to loan approval and funding unless the loan-to-value ratio of your first mortgage is 90% or more. Different requirements may apply to second mortgage loans or loans secured by non-owner occupied property or two-to-four unit dwellings.

Additionally, Fremont Bank will require Private Mortgage Insurance for loans with loan-to-value ratios exceeding specified percentages (for example, 80% for loans secured by first liens on single family, owner occupied property). Depending on the type of loan and the Bank's requirements, Private Mortgage Insurance (PMI) premiums may be included in the monthly payments or paid when due.

Even if your mortgage loan does not fall into one of the categories of loans for which an impound account will be required, you may, at your option, choose to have an impound account established. An impound account is a convenient way to pay property taxes and insurance premiums in monthly installments. If you elect not to have an impound account established for your loan, Fremont Bank will consider your loan in default if you fail to pay two consecutive tax installments on the property prior to the delinquency date for such payments, or fail to pay insurance premiums when due.

When taxes and insurance become due if your loan has an impound account, the Bank will automatically pay these obligations from the impound account funds. Interest will be paid on any impound account you establish. Ask about the current interest rate on impound account balances. Other terms governing impound accounts are set forth in the deed of trust and in federal and state law.

Analysis of Impound (Escrow) Accounts

Under the Federal Real Estate Settlement Procedures Act (RESPA), lenders are limited as to the amount of funds we can collect to establish a required impound (escrow) account. These rules also establish the timing and method of the analysis of impound accounts. Lenders are allowed a “cushion" equal to one-sixth of the total amount or approximately two-months of escrow payments in the account. Fremont Bank has elected to collect the full amount allowed. At the time your impound account is established, and at least once each year, you will receive a statement on your impound account showing the charges made for the past year, and the expected charges for the coming year. At the time of any review, the impound amount that you pay monthly in your payment will be adjusted based on the projections for the coming year.

NOTICE OF RIGHT TO COPY OF APPRAISAL

Unless a real estate related loan application is declined or withdrawn before the property value is determined, Fremont Bank will determine the value of your property in one of three (3) ways.

Appraisal: A professional determination of value of real property done by a state licensed or certified appraiser following prescribed uniform standards. The appraiser may be an employee of Fremont Bank or may be an independent or outside appraiser providing this service.

Evaluation: A professional determination of value of real property done by an outside service or an employee of Fremont Bank who may or may not be a state licensed or certified appraiser. Evaluations can only be used when the relationship of the total loans to apparent value of the property does not require the services of a professional appraiser.

Condition and Marketability Report: Our Secondary Market Investors review the value of your property as collateral for your loan using a property valuation computer model and/or an exterior-only inspection, or by some other means that is not an appraisal of the property.

You have a right under the law to receive a copy of any appraisal, evaluation or other report prepared in connection with your application for a loan or line of credit to be secured by real property. Please note that any appraisal, evaluation or other report obtained is to assist Fremont Bank in determining whether or not to extend credit to you under the terms you have requested. The valuation should not be relied upon by you or anyone else to determine the value of the property. If you wish professional assistance in determining these matters, you should retain your own appraiser or other advisor.

If you want a copy of the property valuation, we must hear from you no later than 90 days after we notify you about the action taken on your credit application or you withdraw your application. Please write us at the address shown below and include in your letter 1) your name, 2) the property address, and 3) your loan number, if known. Under certain circumstances, you may be required to reimburse us for the cost of the valuation as a condition to receiving the copy.

Fremont Bank Appraisal Department
PO Box 5101
Fremont, CA 94537-5101

THE HOUSING FINANCIAL DISCRIMINATION ACT OF 1977 FAIR LENDING NOTICE

It is illegal to discriminate in the provision of, or in the availability of, financial assistance because of the consideration of:

- Trends, characteristics or conditions in the neighborhood or geographic area surrounding a housing accommodation, unless the financial institution can demonstrate in the particular case that such consideration is required to avoid an unsafe and unsound business practice; or
- Race, color, religion, sex, marital status, national origin or ancestry.

It is illegal to consider the racial, ethnic, religious or national origin composition of a neighborhood or geographic area surrounding a housing accommodation or whether or not such composition is undergoing change, or is expected to undergo change, in appraising a housing accommodation or in determining whether or not, or under what terms and conditions, to provide financial assistance.

These provisions govern financial assistance for the purpose of the purchase, construction, rehabilitation or refinancing of one-to-four-unit family residences occupied by the owner and for the purpose of the home improvement of any one-to-four-unit family residence.

If you have questions about your rights, or if you wish to file a complaint, contact the management of this financial institution or:

Department of Financial Institutions
300 South Spring Street Suite 15513
Los Angeles, California 90013-1204

Department of Financial Institutions
111 Pine Street
Suite 1100
San Francisco, California 94111-5613

Fremont Bank Servicing Disclosure Statement

NOTICE TO FIRST LIEN MORTGAGE LOAN APPLICANTS: THE RIGHT TO COLLECT YOUR MORTGAGE LOAN PAYMENTS MAY BE TRANSFERRED.

Because you are applying for a mortgage loan covered by the Real Estate Settlement Procedures Act (RESPA) (12 U.S.C. Section 2601, *et seq*.). RESPA gives you certain rights under Federal law.

This statement describes whether the servicing for this loan may be transferred to a different loan servicer. "Servicing" refers to collecting your principal, interest and escrow payments, if any as well as sending any monthly or annual statements, tracking account balances, and handling other aspects of your loan. You will be given advance notice before a transfer occurs.

Servicing Transfer Information

The following is the best estimate of what will happen to the servicing of your mortgage loan. Business conditions, or other circumstances, may affect our future transferring decisions.

We may assign, sell, or transfer the servicing of your loan while the loan is outstanding.

This information does not include assignments, sales, or transfers to affiliates or subsidiaries.

CONSUMER HANDBOOK ON ADJUSTABLE-RATE MORTGAGES

This handbook gives you an over-view of ARMs, explains how ARMs work, and discusses some of the issues that you might face as a borrower. It includes:

- ways to reduce the risks associated with ARMs;
- pointers about advertising and other sources of information, such as lenders and other trusted advisers;
- a glossary of important ARM terms; and
- a worksheet that can help you ask the right questions and figure out whether an ARM is right for you. (Ask lenders to help you fill out the worksheet so you can get the information you need to compare mortgages.)

An adjustable-rate mortgage (ARM) is a loan with an interest rate that changes. ARMs may start with lower monthly payments than fixed-rate mortgages, but keep the following in mind:

- Your monthly payments could change. They could go up--sometimes by a lot--even if interest rates don't go up. See page 9
- Your payments may not go down much, or at all--even if interest rates go down. See page 7
- You could end up owing more money than you borrowed--even if you make all your payments on time. See page 10
- If you want to pay off your ARM early to avoid higher payments, you might pay a penalty. See page 10.

You need to compare the features of ARMs to find the one that best fits your needs. See the Mortgage Shopping Worksheet on page 5 can help you get started.

This handbook explains how ARMs work and discusses some of the issues that borrowers may face. It includes ways to reduce the risks and gives some pointers about advertising and other ways you can get information from lenders and other trusted advisers. Important ARM terms are defined in a glossary. And the Mortgage Shopping Worksheet can help you ask the right questions and figure out whether an ARM is right for you. Ask lenders to help you fill out the worksheet so you can get the information you need to compare mortgages.

MORTGAGE SHOPPING WORKSHEET

Ask your lender or broker to help you fill out this worksheet.

	Fixed-rate Mortgage	ARM 1	ARM 2	ARM 3
Name of lender or broker and contact information				
Mortgage amount				
Loan term (e.g. 15 years, 30 years)				
Loan description (e.g., fixed rate, 3/1 ARM, payment-option ARM, interest-only ARM)				
Basic Features for Comparison				
Fixed-rate mortgage interest rate and annual percentage rate (APR) (For graduated –payment or stepped-rate mortgages, use the ARM columns.)				
ARM initial interest rate and APR How long does the initial rate apply?				
What will the interest rate be after the initial period?				
ARM features How often can the interest rate adjust?				
What is the index and what is the current rate?				
What is the margin for this loan?				
Interest-rate caps What is the periodic interest-rate cap?				
What is the lifetime interest-rate cap? How high could the rate go?				
How low could the interest rate go on this loan?				
What is the payment cap?				
Can this loan have negative amortization (that is, increase in size)?				
What is the limit to how much the balance can grow before the loan will be recalculated?				
Is there a prepayment penalty if I pay off this mortgage early?				
How long does that penalty last? How much is it?				
Is there a balloon payment on this mortgage? If so, what is the estimated amount and when would it be due?				
What are the estimated origination fees and charges for this loan?				
Monthly Payment Amounts				
What will the monthly payment be for the first year of the loan?				
Does this include taxes and insurance? Condo or homeowner’s association fees? If not, what are the estimates for these amounts?				
What will my monthly payment be after 12 months if the index rate… …stays the same?				
…goes up 2%?				
…goes down 2%?				
What is the **most** my minimum monthly payment could be after 1 year?				
What is the **most** my minimum monthly payment could be after 3 years?				
What is the **most** my minimum monthly payment could be after 5 years?				

What Is an ARM?

An adjustable-rate mortgage differs from a fixed-rate mortgage in many ways. Most importantly, with a fixed-rate mortgage, the interest rate stays the same during the life of the loan. With an ARM, the interest rate changes periodically, usually in relation to an index, and payments may go up or down accordingly.

To compare two ARMs, or to compare an ARM with a fixed-rate mortgage, you need to know about indexes, margins, discounts, caps on rates and payments, negative amortization, payment options, and recasting (recalculating) your loan. You need to consider the maximum amount your monthly payment could increase. Most important, you need to know what might happen to your monthly mortgage payment in relation to your future ability to afford higher payments.

Lenders generally charge lower initial interest rates for ARMs than for fixed-rate mortgages. At first, this makes the ARM easier on your pocketbook than a fixed-rate mortgage for the same loan amount. Moreover, your ARM could be less expensive over a long period than a fixed-rate mortgage--for example, if interest rates remain steady or move lower.

Against these advantages, you have to weigh the risk that an increase in interest rates would lead to higher monthly payments in the future. It's a trade-off--you get a lower initial rate with an ARM in exchange for assuming more risk over the long run. Here are some questions you need to consider:

- Is my income enough--or likely to rise enough--to cover higher mortgage payments if interest rates go up?
- Will I be taking on other sizable debts, such as a loan for a car or school tuition, in the near future?
- How long do I plan to own this home? (If you plan to sell soon, rising interest rates may not pose the problem they do if you plan to own the house for a long time.)
- Do I plan to make any additional payments or pay the loan off early?

Lenders and Brokers
Mortgage loans are offered by many kinds of lenders--such as banks, mortgage companies, and credit unions. You can also get a loan through a mortgage broker. Brokers "arrange" loans; in other words, they find a lender for you. Brokers generally take your application and contact several lenders, but keep in mind that brokers are not required to find the best deal for you unless they have contracted with you to act as your agent.

How ARMs Work: The Basic Features

Initial rate and payment
The initial rate and payment amount on an ARM will remain in effect for a limited period of time--ranging from just 1 month to 5 years or more. For some ARMs, the initial rate and payment can vary greatly from the rates and payments later in the loan term. Even if interest rates are stable, your rates and payments could change a lot. If lenders or brokers quote the initial rate and payment on a loan, ask them for the annual percentage rate (APR). If the APR is significantly higher than the initial rate, then it is likely that your rate and payments will be a lot higher when the loan adjusts, even if general interest rates remain the same.

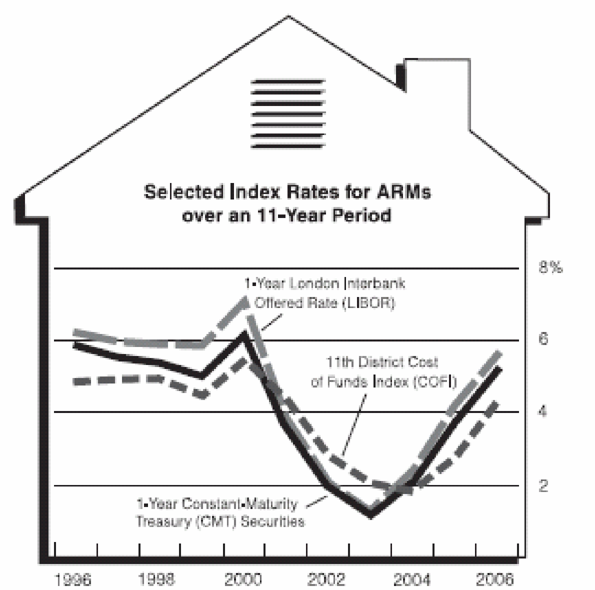
The adjustment period
With most ARMs, the interest rate and monthly payment change every month, quarter, year, 3 years, or 5 years. The period between rate changes is called the adjustment period. For example, a loan with an adjustment period of 1 year is called a 1-year ARM, and the interest rate and payment can change once every year; a loan with a 3-year adjustment period is called a 3-year ARM.

Loan Descriptions
Lenders must give you written information on each type of ARM loan in which you are interested. The information must include the terms and conditions for each loan, including information about the index and margin, how your rate will be calculated, how often your rate can change, limits on changes (or *caps*), an example of how high your monthly payment might go, and other ARM features such as negative amortization.

The index
The interest rate on an ARM is made up of two parts: the index and the margin. The index is a measure of interest rates generally, and the margin is an extra amount that the lender adds. Your payments will be affected by any caps, or limits, on how high or low your rate can go. If the index rate moves up, so does your interest rate in most circumstances and you will probably have to make higher monthly payments. On the other hand, if the index rate goes down, your monthly payment could go down. Not all ARMs adjust downward, however--be sure to read the information for the loan you are considering.

Lenders base ARM rates on a variety of indexes. Among the most common indexes are the rates on 1-year constant-maturity Treasury (CMT) securities, the Cost of Funds Index (COFI), and the London InterBank Offered Rate (LIBOR). A few lenders use their own cost of funds as an index, rather than using other indexes. You should ask what index will be used, how it has fluctuated in the past, and where it is published--you can find a lot of this information in major newspapers and on the Internet.

To help you get an idea of how to compare different indexes, the following chart shows a few common indexes over an 11-year period (1996-2008). As you can see, some index rates tend to be higher than others, and some change more often. But if a lender bases interest-rate adjustments on the average value of an index over time, your interest rate would not change as dramatically.



The margin

To set the interest rate on an ARM, lenders add a few percentage points to the index rate, called the *margin*. The amount of the margin may differ from one lender to another, but it is usually constant over the life of the loan. The *fully indexed rate* is equal to the margin plus the index. If the initial rate on the loan is less than the fully indexed rate, it is called a *discounted index rate*. For example, if the lender uses an index that currently is 4% and adds a 3% margin, the fully indexed rate would be

	Index	**4%**
+	**Margin**	**3%**
	Fully indexed rate	**7%**

If the index on this loan rose to 5%, the fully indexed rate would be 8% (5% + 3%). If the index fell to 2%, the fully indexed rate would be 5% (2% + 3%).

Some lenders base the amount of the margin on your credit record--the better your credit, the lower the margin they add--and the lower the interest you will have to pay on your mortgage. In comparing ARMs, look at both the index and margin for each program.

No-Doc/Low-Doc Loans
When you apply for a loan, lenders usually require documents to prove that your income is high enough to repay the loan. For example, a lender might ask to see copies of your most recent pay stubs, income tax filings, and bank account statements. In a "no-doc" or "low-doc" loan, the lender doesn't require you to bring proof of your income, but you will usually have to pay a higher interest rate or extra fees to get the loan. Lenders generally charge more for no-doc/low-doc loans.

Interest-rate caps

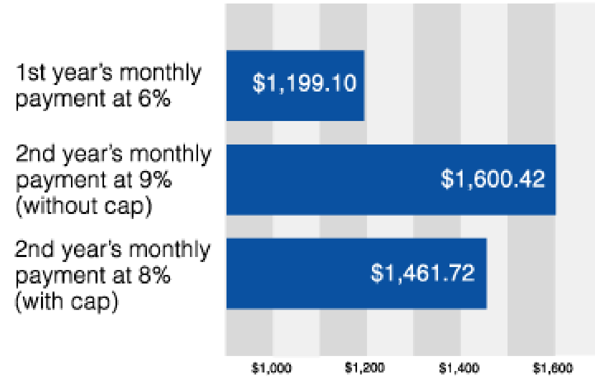
An interest-rate cap places a limit on the amount your interest rate can increase. Interest caps come in two versions:

- A *periodic adjustment cap*, which limit the amount the interest rate can adjust up or down from one adjustment period to the next after the first adjustment, and
- A *lifetime cap*, which limit the interest-rate increase over the life of the loan. By law, virtually all ARMs must have a lifetime cap.

Periodic adjustment caps

Let's suppose you have an ARM with a periodic adjustment interest-rate cap of 2%. However, at the first adjustment, the index rate has risen 3%. The following example shows what happens.

Examples in This Handbook
All examples in this handbook are based on a $200,000 loan amount and a 30-year term. Payment amounts in the examples do not include taxes, insurance, condominium or home-owner association fees, or similar items. These amounts can be a significant part of your monthly payment.



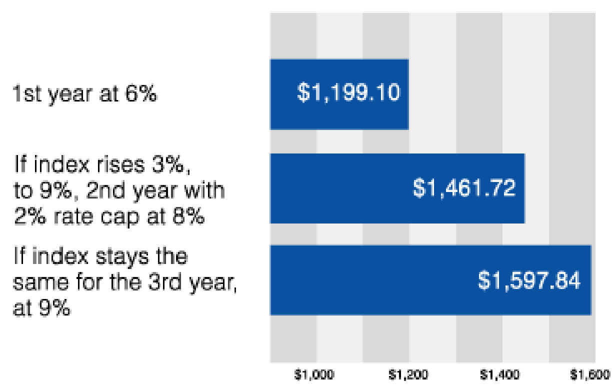
Difference in 2nd year between payment with cap and payment without = $138.70 per month

In this example, because of the cap on your loan, your monthly payment in year 2 is $138.70 per month lower than it would be without the cap, saving you $1,664.40 over the year.

Some ARMs allow a larger rate change at the first adjustment and then apply a periodic adjustment cap to all future adjustments.

A drop in interest rates does not always lead to a drop in your monthly payments. With some ARMs that have interest-rate caps, the cap may hold your rate and payment below what it would have been if the change in the index rate had been fully applied. The increase in the interest that was not imposed because of the rate cap might carry over to future rate adjustments. This is called *carryover*. So at the next adjustment date, your payment might increase even though the index rate has stayed the same or declined.

The following example shows how carryovers work. Suppose the index on your ARM increased 3% during the first year. Because this ARM limits rate increases to 2% at any one time, the rate is adjusted by only 2%, to 8% for the second year. However, the remaining 1% increase in the index carries over to the next time the lender can adjust rates. So when the lender adjusts the interest rate for the third year, even if there is no change in the index during the second year, the rate still increases by 1%, to 9%.

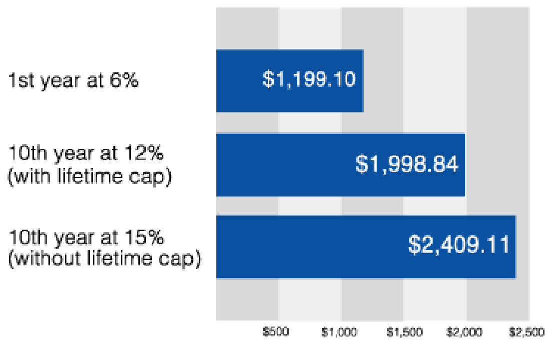


In general, the rate on your loan can go up at any scheduled adjustment date when the lender's standard ARM rate (the index plus the margin) is higher than the rate you are paying before that adjustment.

Lifetime caps

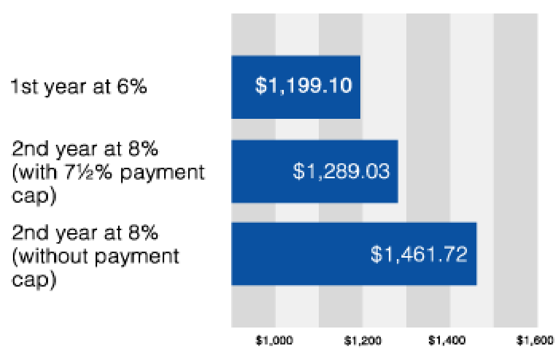
The next example shows how a lifetime rate cap would affect your loan. Let's say that your ARM starts out with a 6% rate and the loan has a 6% lifetime cap--that is, the rate can never exceed 12%.

Suppose the index rate increases 1% in each of the next 9 years. With a 6% overall cap, your payment would never exceed $1,998.84--compared with the $2,409.11 that it would have reached in the tenth year without a cap.



Payment caps
In addition to interest-rate caps, many ARMs--including payment-option ARMs--limit, or cap, the amount your monthly payment may increase at the time of each adjustment. For example, if your loan has a payment cap of 7½%, your monthly payment won't increase more than 7½% over your previous payment, even if interest rates rise more. For example, if your monthly payment in year 1 of your mortgage was $1,000, it could only go up to $1,075 in year 2 (7½% of $1,000 is an additional $75). Any interest you don't pay because of the payment cap will be added to the balance of your loan. A payment cap can limit the increase to your monthly payments but also can add to the amount you owe on the loan. (This is called *negative amortization,* a term that is explained on page 10.)

Let's assume that your rate changes in the first year by 2 percentage points but your payments can increase no more than 7½% in any one year. The following graph shows what your monthly payments would look like.



Difference in monthly payment = $172.69

While your monthly payment will be only $1,289.03 for the second year, the difference of $172.69 each month will be added to the balance of your loan and will lead to negative amortization.

Some ARMs with payment caps do not have periodic interest-rate caps. In addition, as explained below, most payment-option ARMs have a built-in recalculation period, usually every 5 years. At that point, your payment will be recalculated (lenders use the term *recast*) based on the remaining term of the loan. If you have a 30-year loan and you are at the end of year 5, your payment will be recalculated for the remaining 25 years. The payment cap does not apply to this adjustment. If your loan balance has increased, or if interest rates have risen faster than your payments, your payments could go up a lot.

Types of ARMs

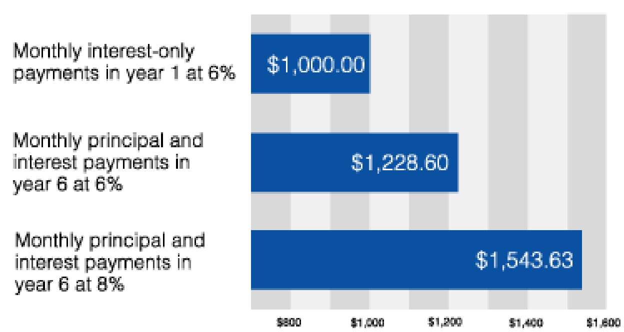
Hybrid ARMs
Hybrid ARMs often are advertised as 3/1 or 5/1 ARMs--you might also see ads for 7/1 or 10/1 ARMs. These loans are a mix--or a hybrid--of a fixed-rate period and an adjustable-rate period. The interest rate is fixed for the first few years of these loans--for example, for 5 years in a 5/1 ARM. After that, the rate may adjust annually (the 1 in the 5/1 example), until the loan is paid off. In the case of 3/1 or 5/1 ARMs

- the first number tells you how long the fixed interest-rate period will be and
- the second number tells you how often the rate will adjust after the initial period.

You may also see ads for 2/28 or 3/27 ARMs--the first number tells you how long the fixed interest-rate period will be, and the second number tells you the number of years the rates on the loan will be adjustable. Some 2/28 and 3/27 mortgages adjust every 6 months, not annually.

Interest-only (I-O) ARMs
An interest-only (I-O) ARM payment plan allows you to *pay only the interest* for a specified number of years, typically between 3 and 10 years. This allows you to have smaller monthly payments for a period of time. After that, your monthly payment will increase--even if interest rates stay the same--because you must start paying back the principal as well as the interest each month. For some I-O loans, the interest rate adjusts during the I-O period as well.

For example, if you take out a 30-year mortgage loan with a 5-year I-O payment period, you can pay only interest for 5 years and then you must pay both the principal and interest over the next 25 years. Because you begin to pay back the principal, your payments increase after year 5, even if the rate stays the same. Keep in mind that the longer the I-O period, the higher your monthly payments will be after the I-O period ends.



Payment-option ARMs
A payment-option ARM is an adjustable-rate mortgage that allows you to choose among several payment options each month. The options typically include the following:

- *a traditional payment of principal and interest*, which reduces the amount you owe on your mortgage. These payments are based on a set loan term, such as a 15-, 30-, or 40-year payment schedule.
- *an interest-only payment*, which pays the interest but does not reduce the amount you owe on your mortgage as you make your payments.
- *a minimum (or limited) payment* that may be less than the amount of interest due that month and may not reduce the amount you owe on your mortgage. If you choose this option, the amount of any interest you do not

pay will be added to the principal of the loan, **increasing the amount you owe and your future monthly payments**, and increasing the amount of interest you will pay over the life of the loan. In addition, if you pay only the minimum payment in the last few years of the loan, you may owe a larger payment at the end of the loan term, called a *balloon payment*.

The interest rate on a payment-option ARM is typically very low for the first few months (for example, 2% for the first 1 to 3 months). After that, the interest rate usually rises to a rate closer to that of other mortgage loans. Your payments during the first year are based on the initial low rate, meaning that if you only make the minimum payment each month, it will not reduce the amount you owe and it may not cover the interest due. The unpaid interest is added to the amount you owe on the mortgage, and your loan balance increases. This is called *negative amortization*. This means that even after making many payments, you could owe more than you did at the beginning of the loan. Also, as interest rates go up, your payments are likely to go up.

Payment-option ARMs have a built-in recalculation period, usually every 5 years. At this point, your payment will be recalculated (lenders use the term *recast*) based on the remaining term of the loan. If you have a 30-year loan and you are at the end of year 5, your payment will be recalculated for the remaining 25 years. If your loan balance has increased because you have made only minimum payments, or if interest rates have risen faster than your payments, your payments will increase each time your loan is recast. At each recast, your new minimum payment will be a fully amortizing payment and any payment cap will not apply. This means that your monthly payment can increase a lot at each recast.

Lenders may recalculate your loan payments before the recast period if the amount of principal you owe grows beyond a set limit, say 110% or 125% of your original mortgage amount. For example, suppose you made only minimum payments on your $200,000 mortgage and had any unpaid interest added to your balance. If the balance grew to $250,000 (125% of $200,000), your lender would recalculate your payments so that you would pay off the loan over the remaining term. It is likely that your payments would go up substantially.

More information on interest-only and payment-option ARMs is available in the Federal Reserve Board's brochure titled *Interest-Only Mortgage Payments and Payment-Option ARMs--Are They for You?*

Consumer Cautions

Discounted interest rates

Many lenders offer more than one type of ARM. Some lenders offer an ARM with an initial rate that is lower than their fully indexed ARM rate (that is, lower than the sum of the index plus the margin). Such rates--called discounted rates, start rates, or teaser rates--are often combined with large initial loan fees, sometimes called *points*, and with higher rates after the initial discounted rate expires.

Your lender or broker may offer you a choice of loans that may include "discount points" or a "discount fee." You may choose to pay these points or fees in return for a lower interest rate. But keep in mind that the lower interest rate may only last until the first adjustment.

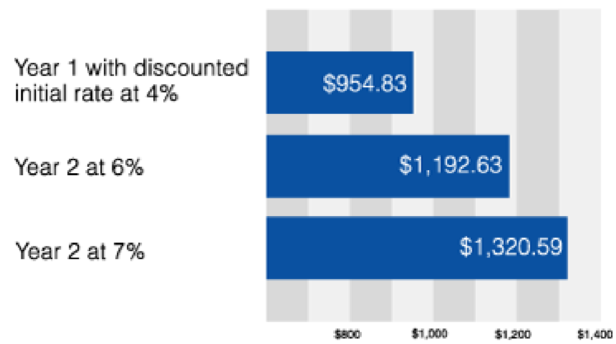
If a lender offers you a loan with a discount rate, don't assume that means that the loan is a good one for you. You should carefully consider whether you will be able to afford higher payments in later years when the discount expires and the rate is adjusted.

Here is an example of how a discounted initial rate might work. Let's assume that the lender's fully indexed one-year ARM rate (index rate plus margin) is currently 6%; the monthly payment for the first year would be $1,199.10. But your lender is offering an ARM with a discounted initial rate of 4% for the first year. With the 4% rate, your first-year's monthly payment would be $954.83.

With a discounted ARM, your initial payment will probably remain at $954.83 for only a limited time--and any savings during the discount period may be offset by higher payments over the remaining life of the mortgage. If you are considering a discount ARM, be sure to compare future payments with those for a fully indexed ARM. In fact, if you buy a home or refinance using a deeply discounted initial rate, you run the risk of payment shock, negative amortization, or prepayment penalties or conversion fees.

Payment shock

Payment shock may occur if your mortgage payment rises sharply at a rate adjustment. Let's see what would happen in the second year if the rate on your discounted 4% ARM were to rise to the 6% fully indexed rate.



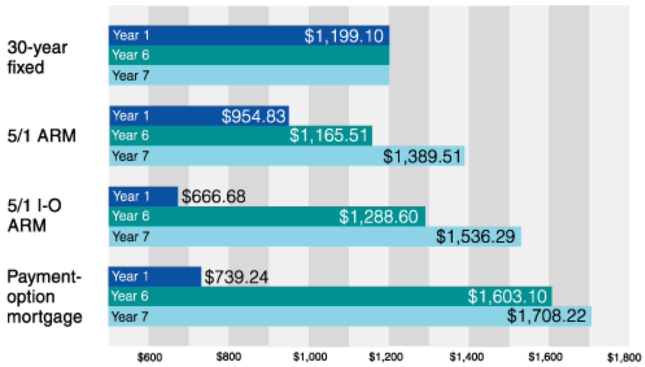
As the example shows, even if the index rate were to stay the same, your monthly payment would go up from $954.83 to $1,192.63 in the second year.

Suppose that the index rate increases 1% in one year and the ARM rate rises to 7%. Your payment in the second year would be $1,320.59.

That's an increase of $365.76 in your monthly payment. You can see what might happen if you choose an ARM because of a low initial rate without considering whether you will be able to afford future payments.

If you have an interest-only ARM, payment shock can also occur when the interest-only period ends. Or, if you have a payment-option ARM, payment shock can happen when the loan is recast.

The following example compares several different loans over the first 7 years of their terms; the payments shown are for years 1, 6, and 7 of the mortgage, assuming you make interest-only payments or minimum payments. The main point is that depending on the terms and conditions of your mortgage and changes in interest rates, ARM payments can change quite a bit over the life of the loan--so while you could save money in the first few years of an ARM, you could also face much higher payments in the future.



Negative amortization--When you owe more money than you borrowed
Negative amortization means that the amount you owe increases even when you make all your required payments on time. It occurs whenever your monthly mortgage payments are not large enough to pay all of the interest due on your mortgage--meaning the unpaid interest is added to the principal on your mortgage, and you will owe more than you originally borrowed. This can happen because you are making only minimum payments on a payment-option mortgage or because your loan has a payment cap.

For example, suppose you have a $200,000, 30-year payment-option ARM with a 2% rate for the first 3 months and a 6% rate for the remaining 9 months of the year. Your minimum payment for the year is $739.24, as shown in the previous graph. However, once the 6% rate is applied to your loan balance, you are no longer covering the interest costs. If you continue to make minimum payments on this loan, your loan balance at the end of the first year of your mortgage would be $201,118--or $1,118 more than you originally borrowed.

Because payment caps limit only the amount of payment increases, and not interest-rate increases, payments sometimes do not cover all the interest due on your loan. This means that the unpaid interest is automatically added to your debt, and interest may be charged on that amount. You might owe the lender more later in the loan term than you did at the beginning.

A payment cap limits the increase in your monthly payment by deferring some of the interest. Eventually, you would have to repay the higher remaining loan balance at the interest rate then in effect. When this happens, there may be a substantial increase in your monthly payment.

Some mortgages include a cap on negative amortization. The cap typically limits the total amount you can owe to 110% to 125% of the original loan amount. When you reach that point, the lender will set the monthly payment amounts to fully repay the loan over the remaining term. Your payment cap will not apply, and your payments could be substantially higher. You may limit negative amortization by voluntarily increasing your monthly payment.

Be sure you know whether the ARM you are considering can have negative amortization.

Home Prices, Home Equity, and ARMs
Sometimes home prices rise rapidly, allowing people to quickly build equity in their homes. This can make some people think that even if the rate and payments on their ARM get too high, they can avoid those higher payments by refinancing their loan or, in the worst case, selling their home. It's important to remember that home prices do not always go up quickly--they may increase a little or remain the same, and sometimes they fall. If housing prices fall, your home may not be worth as much as you owe on the mortgage. Also, you may find it difficult to refinance your loan to get a lower monthly payment or rate. Even if home prices stay the same, if your loan lets you make minimum payments (see *payment-option ARMs* on page 12), you may owe your lender more on your mortgage than you could get from selling your home.

Prepayment penalties and conversion

If you get an ARM, you may decide later that you don't want to risk any increases in the interest rate and payment amount. When you are considering an ARM, ask for information about any extra fees you would have to pay if you pay off the loan early by refinancing or selling your home, and whether you would be able to convert your ARM to a fixed-rate mortgage.

Prepayment penalties
Some ARMs, including interest-only and payment-option ARMs, may require you to pay special fees or penalties if you refinance or pay off the ARM early (usually within the first 3 to 5 years of the loan). Some loans have *hard prepayment penalties*, meaning that you will pay an extra fee or penalty if you pay off the loan during the penalty period for any reason (because you refinance or sell your home, for example). Other loans have *soft prepayment penalties*, meaning that you will pay an extra fee or penalty only if you refinance the loan, but you will not pay a penalty if you sell your home. Also, some loans may have prepayment penalties even if you make only a partial prepayment.

Prepayment penalties can be several thousand dollars. For example, suppose you have a 3/1 ARM with an initial rate of 6%. At the end of year 2 you decide to refinance and pay off your original loan. At the time of refinancing, your balance is $194,936. If your loan has a prepayment penalty of 6 months' interest on the remaining balance, you would owe about $5,850.

Sometimes there is a trade-off between having a prepayment penalty and having lower origination fees or lower interest rates. The lender may be willing to reduce or eliminate a prepayment penalty based on the amount you pay in loan fees or on the interest rate in the loan contract.

If you have a hybrid ARM--such as a 2/28 or 3/27 ARM--be sure to compare the prepayment penalty period with the ARMs first adjustment period. For example, if you have a 2/28 ARM that has a rate and payment adjustment after the second year, but the prepayment penalty is in effect for the first 5 years of the loan, it may be costly to refinance when the first adjustment is made.

Most mortgages let you make additional principal payments with your monthly payment. In most cases, this is *not* considered prepayment, and there usually is no penalty for these extra amounts. Check with your lender to make sure there is no penalty if you think you might want to make this type of additional principal prepayment.

Conversion fees
Your agreement with the lender may include a clause that lets you convert the ARM to a fixed-rate mortgage at designated times. When you convert, the new rate is generally set using a formula given in your loan documents.

The interest rate or up-front fees may be somewhat higher for a convertible ARM. Also, a convertible ARM may require a fee at the time of conversion.

Graduated-payment or stepped-rate loans
Some fixed-rate loans start with one rate for 1 or 2 years and then change to another rate for the remaining term of the loan. While these are not ARMs, your payment will go up according to the terms of your contract. Talk with your lender or broker and read the information provided to you to make sure you understand when and by how much the payment will change.

Where to Get Information

Disclosures from lenders
You should receive information in writing about each ARM program you are interested in before you have paid a nonrefundable fee. It is important that you read this information and ask the lender or broker about anything you don't understand--index rates, margins, caps, and other ARM features such as negative amortization. After you have applied for a loan, you will get more information from the lender about your loan, including the APR, a payment schedule, and whether the loan has a prepayment penalty.

The APR is the cost of your credit as a yearly rate. It takes into account interest, points paid on the loan, any fees paid to the lender for making the loan, and any mortgage insurance premiums you may have to pay. You can compare APRs on similar ARMs (for example, compare APRs on a 5/1 and a 3/1 ARM) to determine which loan will cost you less in the long term, but you should keep in mind that because the interest rate for an ARM can change, APRs on ARMs cannot be compared directly to APRs for fixed-rate mortgages.

You may want to talk with financial advisers, housing counselors, and other trusted advisers. Contact a local housing counseling agency, call the U.S. Department of Housing and Urban Development toll-free at 800-569-4287, or visit www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm to find a center near you.

Newspapers and the Internet
When buying a home or refinancing your existing mortgage, remember to shop around. Compare costs and terms, and negotiate for the best deal. Your local newspaper and the Internet are good places to start shopping for a loan. You can usually find information on interest rates and points for several lenders. Since rates and points can change daily, you'll want to check information sources often when shopping for a home loan.

The Mortgage Shopping Worksheet on page 5 may also help you. Take it with you when you speak to each lender or broker and write down the information you obtain. Don't be afraid to make lenders and brokers compete with each other for your business by letting them know that you are shopping for the best deal.

Advertisements
Any initial information you receive about mortgages probably will come from advertisements or mail solicitations from builders, real estate brokers, mortgage brokers, and lenders. Although this information can be helpful, keep in mind that these are marketing materials--the ads and mailings are designed to make the mortgage look as attractive as possible. These ads may play up low initial interest rates and monthly payments, without emphasizing that those rates and payments could increase substantially later. So, get all the facts.
Any ad for an ARM that shows an initial interest rate should also show how long the rate is in effect and the APR on the loan. If the APR is much higher than the initial rate, your payments may increase a lot after the introductory period, even if interest rates stay the same.

Choosing a mortgage may be the most important financial decision you will make. You are entitled to have all the information you need to make the right decision. Don't hesitate to ask questions about ARM features when you talk to lenders, mortgage brokers, real estate agents, sellers, and your attorney, and keep asking until you get clear and complete answers.

GLOSSARY

Adjustable-rate mortgage (ARM)
A mortgage that does not have a fixed interest rate. The rate changes during the life of the loan based on movements in an index rate, such as the rate for Treasury securities or the Cost of Funds Index. ARMs usually offer a lower initial interest rate than fixed-rate loans. The interest rate fluctuates over the life of the loan based on market conditions, but the loan agreement generally sets maximum and minimum rate. When interest rates increase, generally your loan payments increase; and when interest rates decrease, your monthly payments may decrease.

Annual percentage rate (APR)
The cost of credit expressed as a yearly rate. For closed-end credit, such as car loans or mortgages, the APR includes the interest rate, points, broker fees, and other credit charges that the borrower is required to pay. An APR, or an equivalent rate, is not used in leasing agreements.

Balloon payment
A large extra payment that may be charged at the end of a mortgage loan or lease.

Buydown
When the seller pays an amount to the lender so that the lender can give you a lower rate and lower payments, usually for an initial period in an ARM. The seller may increase the sales price to cover the cost of the buydown. Buydowns can occur in all types of mortgages, not just ARMs.

Cap, interest rate
A limit on the amount your interest rate can increase. The two types of interest rate caps are *periodic adjustment caps* and *lifetime caps* . *Periodic adjustment caps* limit the interest-rate increase from one adjustment period to the next. *Lifetime caps* limit the interest-rate increase over the life of the loan. All adjustable-rate mortgages have an overall cap.

Cap, payment
A limit on the amount that your monthly mortgage payment on a loan may change, usually a percentage of the loan. The limit can be applied each time the payment changes or during the life of the mortgage. Payment caps may lead to negative amortization because they do not limit the amount of interest the lender is earning.

Conversion clause
A provision in some ARMs that allows you to change the ARM to a fixed-rate loan at some point during the term. Conversion is usually allowed at the end of the first adjustment period. At the time of the conversion, the new fixed rate is generally set at one of the rates then prevailing for fixed-rate mortgages. The conversion feature may be available at extra cost.

Discounted initial rate (also known as a start rate or teaser rate)
In an ARM with a discounted initial rate, the lender offers you a lower rate and lower payments for part of the mortgage term (usually for 1, 3, or 5 years). After the discount period, the ARM rate will probably go up depending on the index rate. Discounts can occur in all types of mortgages, not just ARMs.

Equity
In housing markets, equity is the difference between the fair market value of the home and the outstanding balance on your mortgage plus any outstanding home equity loans. In vehicle leasing markets, equity is the positive difference between the trade-in or market value of your vehicle and the loan payoff amount.

Hybrid ARM
These ARMs are a mix—or a hybrid—of a fixed-rate period and an adjustable-rate period. The interest rate is fixed for the first several years of the loan; after that period, the rate can adjust annually. For example, hybrid ARMs can be advertised as 3/1 or 5/1—the first number tells you how long the fixed interest-rate period will be and the second number tells you how often the rate will adjust after the initial period. For example, a 3/1 loan has a fixed rate for the first 3 years and then the rate adjusts once each year beginning in year 4.

Index
The economic indicator used to calculate interest-rate adjustments for adjustable-rate mortgages or other adjustable-rate loans. The index rate can increase or decrease at any time. *See also* the chart on page 6, *Selected index rates for ARMs over an 11-year period,* for examples of common indexes that have changed in the past.

Interest
The rate used to determine the cost for borrowing money, usually stated as a percentage and as an annual rate.

Interest-only (I-O)t ARM
Interest-only ARMs allow you to pay only the interest for a specified number of years, typically between 3 and 10 years. This arrangement allows you to have smaller monthly payments for a prescribed period. After that period, your monthly payment will increase – even if interest rates stay the same—because you must start paying back the principal and the interest each month. For some I-O loans, the interest rate adjusts during the I-O period as well.

Margin
The number of percentage points the lender adds to the index rate to calculate the interest rate of an adjustable-rate mortgage (ARM) at each adjustment.

Negative amortization
Occurs when the monthly payments in an adjustable-rate mortgage loan do not cover all the interest owed. The interest that is not paid in the monthly payment is added to the loan balance. This means that even after making many payments, you could owe more than you did at the beginning of the loan. Negative amortization can occur when an ARM has a payment cap that results in monthly payments that are not high enough to cover the interest due or when the minimum payments are set at an amount lower than the amount you owe in interest.

Payment-option ARM
An ARM that allows the borrower to choose among several payment options each month. The options typically include (1) a traditional amortizing payment of principal and interest, (2) an interest-only payment, or (3) a minimum (or limited) payment that may be less than the amount of interest due that month. If the borrower chooses the minimum-payment option, the amount of any interest that is not paid will be added to the principal of your loan. *See also* Negative amortization on page 10.

Points (also called discount points)
One point is equal to 1 percent of the principal amount of a mortgage loan. For example, if the mortgage is for $200,000, one point equals $2,000. Lenders frequently charge points in both fixed-rate and adjustable-rate mortgages in order to cover loan origination costs or to provide additional compensation to the lender or broker. These points usually are paid at closing and may be paid by the borrower or the home seller, or may be split between them. In some cases, the money needed to pay points can be borrowed (incorporated in the loan amount), but doing so will increase the loan amount and the total costs. Discount points (also called discount fees) are points that the borrower voluntarily chooses to pay in return for a lower interest rate.

Prepayment penalty
Extra fees that may be due if you pay off the loan early by refinancing your loan or selling your home. The penalty is usually limited to the first 3 to 5 years of the loan's term. If your loan includes a prepayment penalty, make sure you understand the cost. Compare the length of the prepayment penalty period with the first adjustment period of the ARM to see if refinancing is cost-effective before the loan first adjusts. Some loans may have a prepayment penalty even if you make a partial prepayment. Ask the lender for a loan without a prepayment penalty and the cost of that loan.

Principal
The amount of money borrowed or the amount still owed on a loan.

Where to go for help

For additional information or to file a complaint about a bank, savings and loan, credit union, or other financial institution, contact one of the following federal agencies, depending on the type of institution.

State-chartered bank that are members of the Federal Reserve System
Federal Reserve Consumer Help
PO Box 1200
Minneapolis, MN 55480
(888) 851-1920 (toll free)
(877) 766-8533 (TTY) (toll free)
(877) 888-2520 (fax) (toll free)
e-mail: ConsumerHelp@FederalReserve.gov
www.FederalReserveConsumerHelp.gov

Federally insured state-chartered banks that are not members of the Federal Reserve System
Federal Deposit Insurance Corporation (FDIC)
Consumer Response Center
2345 Grand Blvd., Suite 100
Kansas City, MO 64108
(877) ASK-FDIC (877-275-3342) (toll free)
e-mail: consumeralerts@fdic.gov
www.fdic.gov/consumers/consumer/ccc/index.html

National banks (banks with "National" in the name or "N.A." after the name) and national-bank-owned mortgage companies
Office of the Comptroller of the Currency (OCC)
Customer Assistance Group
1301 McKinney Street, Suite 3450
Houston, TX 77010
(800) 613-6743 (toll free)
(713) 336-4301 (fax)
e-mail: customer.assistance@occ.treas.gov
www.occ.treas.gov
www.helpwithmybank.gov

Savings and loan associations (federally chartered and some state chartered)
Office of Thrift Supervision (OTS)
Consumer Affairs
1700 G Street NW, 6th Floor
Washington, DC 20552
(800) 842-6929 (toll free)
(800) 877-8339 (TTY) (toll free)
www.ots.treas.gov

Federally chartered credit unions (those with "Federal" in the name)
National Credit Union Administration (NCUA)
Office of Public and Congressional Affairs
1775 Duke Street
Alexandria, VA 22314
(800) 755-1030 (toll free)
(703) 518-6409 (fax)
e-mail: consumerassistance@ncua.gov
www.ncua.gov / ConsumerInformation/ index.htm

State-chartered credit unions
Contact the regulatory agency in the state in which the credit union is chartered.

Finance companies, stores, auto dealers, mortgage companies,and other lenders, and credit bureaus
Federal Trade Commission (FTC)
Consumer Response Center – 240
600 Pennsylvania Avenue NW
Washington, DC 20580
(877) FTC-HELP (877-382-4357) (toll free)
(866) 653-4261 (TTY) (toll free)
www.ftc.gov
www.ftc.gov/bcp/edu/microsites/idtheft

More resources and ordering information

Looking for the Best Mortgage—Shop, Compare, Negotiate
(at www.federalreserve.gov / pubs / mortgage/mortb_1.htm)

Interest-Only Mortgage Payments and Payment-Option ARMs—Are They for You?
(at www.federalreserve.gov / pubs /mortgage_interestonly /)

A Consumer's Guide to Mortgage Lock-Ins
(at www.federalreserve.gov / pubs / lockins / default.htm)

A Consumer's Guide to Mortgage Settlement Costs
(at www.federalreserve.gov / pubs / settlement / default.htm)

Know Before You Go . . .To Get a Mortgage: A Guide to Mortgage Products and a Glossary of Lending Terms
(at www.bos.frb.org / consumer / knowbeforeyougo / mortgage / mortgage.pdf)

Partners Online Mortgage Calculator
(at www.frbatlanta.org / partnerssoftwareonline / dsp_main.cfm)

For more information on mortgage and other financial topics, including interactive calculators, visit www.federalreserve.gov / consumerinfo. To order print copies of brochures, visit www.federalreserve.gov/pubs/order.htm.

Interest-Only Mortgage Payments and Payment-Option ARMs- Are They for You?

Owning a home is part of the American dream. But high home prices may make the dream seem out of reach. To make monthly mortgage payments more affordable, many lenders offer home loans that allow you to (1) pay only the interest on the loan during the first few years of the loan term or (2) make only a specified minimum payment that could be less than the monthly interest on the loan.

Whether you are buying a house or refinancing your mortgage, this information can help you decide if an interest-only mortgage payment (an I-O mortgage)—or an adjustable-rate mortgage (ARM) with the option to make a minimum payment (a payment-option ARM)—is right for you. Lenders have a variety of names for these loans, but keep in mind that with I-O mortgages and payment-option ARMs, you could face

- *payment shock.* Your payments may go up a lot— as much as double or triple—after the interest-only period or when the payments adjust.

In addition, with payment-option ARMs you could face

- *negative amortization.* Your payments may not cover all of the interest owed. The unpaid interest is added to your mortgage balance so that you owe more on your mortgage than you originally borrowed.

Be sure you understand the loan terms and the risks you face. And be realistic about whether you can handle future payment increases. If you're not comfortable with these risks, ask about another loan product.

What is an I-O mortgage payment?

Traditional mortgages require that each month you pay back some of the money you borrowed (the principal) plus the interest on that money. The principal you owe on your mortgage decreases over the term of the loan. In contrast, an I-O payment plan allows you to pay only the interest for a specified number of years. After that, you must repay both the principal and the interest.

Most mortgages that offer an I-O payment plan have adjustable interest rates, which means that the interest rate and monthly payment will change over the term of the loan. The changes may be as often as once a month or as seldom as every 3 to 5 years, depending on the terms of your loan. For example, a 5/1 ARM has a fixed interest rate for the first 5 years; after that, the rate can change once a year (the "1" in 5/1) during the rest of the loan. More information on ARMs is available in the Federal Reserve Board's *Consumer Handbook on Adjustable Rate Mortgages*.

The I-O payment period is typically between 3 and 10 years. After that, your monthly payment will increase—even if interest rates stay the same—because you must pay back the principal as well as the interest. For example, if you take out a 30-year mortgage loan with a 5-year I-O payment period, you can pay only interest for 5 years and then both principal and interest over the next 25 years. Because you begin to pay back the principal, your payments increase after year 5.

What is a payment-option ARM?
A payment-option ARM is an adjustable-rate mortgage that allows you to choose among several payment options each month. The options typically include

- *a traditional payment of principal and interest* (which reduces the amount you owe on your mortgage). These payments may be based on a set loan term, such as a 15-, 30-, or 40-year payment schedule.

- *an interest-only payment* (which does not change the amount you owe on your mortgage).

- *a minimum (or limited) payment* (which may be less than the amount of interest due that month and may not pay down any principal). If you choose this option, the amount of any interest you do not pay will be added to the principal of the loan, increasing the amount you owe and increasing the interest you will pay.

Interest rates. The interest rate on a payment-option ARM is typically very low for the first 1 to 3 months (2%, for example). After that, the rate usually rises to a rate closer to that of other mortgage loans. Your monthly payments during the first year are based on the initial low rate, meaning that if you only make the minimum payment, it may not cover the interest due. The unpaid interest is added to the amount you owe on the mortgage, resulting in a higher balance. This is known as *negative amortization.* Also, as interest rates go up, your payments are likely to go up.

Payment changes. Many payment-option ARMs limit, or cap, the amount the monthly minimum payment may increase from year to year. For example, if your loan has a payment cap of 7.5%, your monthly payment won't increase more than 7.5% from one year to the next (for example, from $1,000 to $1,075), even if interest rates rise more than 7.5%. Any interest you don't pay because of the payment cap will be added to the balance of your loan.

Payment-option ARMs have a built-in recalculation period, usually every 5 years. At this point, your payment will be recalculated (lenders use the term *recast*) based on the remaining term of the loan. If you have a 30-year loan and you are at the end of year 5, your payment will be recalculated for the remaining 25 years. **The payment cap does not apply to this adjustment.** If your loan balance has increased, or if interest rates have risen faster than your payments, your payments could go up a lot.

Ending the option payments. Lenders end the option payments if the amount of principal you owe grows beyond a set limit, say 110% or 125% of your original mortgage amount. For example, suppose you made minimum payments on your $180,000 mortgage and had negative amortization. If the balance grew to $225,000 (125% of $180,000), the option payments would end. Your loan would be recalculated and you would pay back principal and interest based on the remaining term of your loan. It is likely that your payments would go up significantly.

What do you need to ask when shopping for an I-O mortgage or a payment-option ARM?

Use the Mortgage Shopping Worksheet to compare different loan products. Ask lenders or brokers about the details of their loans and about the different loan options they offer. And don't be afraid to make lenders and brokers compete with each other by letting them know you are shopping for the best deal. Look for a mortgage that allows you to buy the house and continue to afford the payments, even if payments go up over time.

Mortgage Shopping Worksheet

(See the *Consumer Handbook on Adjustable Rate Mortgages* to help you compare other ARM features and *Looking for the Best Mortgage* to help you compare other loan features.

	Example
Name of lender or broker & contact information	ABC Mortgage Co. 800-123-4567
Mortgage amount	$180,000
Loan description	Payment-option ARM; 1-month introductory rate: 30-year term
Is this an I-O payment or a payment option ARM?	Payment-option ARM
If different payment options are available, what are the options?	1. First year's minimum payment based on initial interest rate 2. Interest-only payment based on rate after adjustment 3. Fully amortizing payment based on 30-year term
What is the full term of the mortgage?	30 years
How long is the options period?	The loan will be recalculated (recast) every 5 years. Payment options are available every month except (1) when loan is recast every 5 years, (2) when balance is 125% of original loan, or (3) if you fall more than 60 days behind in your payments.
What is the initial interest rate?	1.6%
For a payment-option ARM, how long does the initial interest rate apply?	1 month
What will the interest rate be after the initial rate?	6.4%
How often can the interest rate adjust?	Monthly
What is the periodic interest rate cap?	2% per year
What is the overall interest rate cap?	6% lifetime max cap (maximum interest rate is 12.4%)
How often will the monthly payments adjust?	Annually
What is the payment cap?	7.5% per year: does not apply to recalculation every 5th year
Can this loan have negative amortization?	Yes
Is there a limit to how much the balance can grow before the loan will be recalculated?	Up to 125% of original amount borrowed (loan will be recalculated if balance grows to $225,000)
Is there a prepayment penalty if I end this mortgage early by refinancing or selling my home?	Yes
How much is the penalty?	3% of amount borrowed in 1st year ($5,400), down to 1% of amount borrowed in 3rd year ($1,800); no prepayment penalty after year 3
What will my monthly payments be for the first year of the loan?	$630
Does this include taxes and insurance? Homeowner's association fees?	No
What is the most my minimum monthly payment could be after 12 months?	$677 (based on 7.5% cap)
What is the most my minimum monthly payment could be after 24 months?	$728 (based on 7.5% cap)
What is the most my minimum monthly payment could be after 36 months?	$783 (based on 7.5% cap)
What is the most my minimum monthly payment could be after 48 months?	$2,491 (based on recalculation of the loan when balance is $225,000)
What is the most my minimum monthly payment could be after 60 months (5 years)?	$2491 (based on recalculation of the loan after 4 years)
What would my minimum monthly payment be after 60 months (5 years) **if the interest rate stays the same?**	$1,308 (based on recalculation of the loan after 5 years)
What are the fees and charges due at closing on this loan?	See good faith estimate

When might an I-O mortgage payment or a payment-option ARM be right for you?

Despite the risks of these loans, an I-O mortgage payment or a payment-option ARM might be right for you if the following apply:

- you have modest current income but are reasonably certain that your income will go up in the future (for example, if you're finishing your degree or training program),
- you have sizable equity in your home and will use the money that would go toward principal payments for other investments, or
- you have irregular income (such as commissions or seasonal earnings) and want the flexibility of making I-O or option-ARM minimum payments during low-income periods and larger payments during higher-income periods.

When might an I-O mortgage payment or a payment-option ARM *not* make sense?

Interest-only or option-ARM minimum payments may be risky if you won't be able to afford the higher monthly payments in the future. For example, suppose you are in the market for a home and can afford a monthly payment of about $1,100. Depending on the interest rate, with a traditional 30-year, fixed-rate mortgage, you might expect to get a $180,000 mortgage. A lender or broker could offer you an I-O mortgage payment of $1,100 monthly that might enable you to get a $215,000 mortgage—and, therefore, a more expensive house. But keep in mind that your payments could go up because of interest rate increases when the I-O period ends, or when the loan is recalculated. Your $1,100 monthly payment could jump to $1,340 or more. If you cannot reasonably expect to make this larger payment when the time comes, you might want to think about a different type of loan.

Mortgage Shopping Worksheet

Use this worksheet to compare mortgages.

	Mortgage 1	Mortgage 2
Name of lender or broker & contact information		
Mortgage amount		
Loan description		
Is this an I-O payment or a payment option ARM?		
If different payment options are available, what are the options?		
What is the full term of the mortgage?		
How long is the option period?		
What is the initial interest rate?		
For a payment-option ARM, how long does the initial interest rate apply?		
What will the interest rate be after the initial rate?		
How often can the interest rate adjust?		
What is the periodic interest rate cap?		
What is the overall interest rate cap?		
How often will the monthly payments adjust?		
What is the payment cap?		
Can this loan have negative amortization?		
Is there a limit to how much the balance can grow before the loan will be recalculated?		
Is there a prepayment penalty if I end this mortgage early by refinancing or selling my home?		
How much is the penalty?		
What will my monthly payments be for the first year of the loan?		
Does this include taxes and insurance? Homeowner's association fees?		
What is the **most** my minimum monthly payment could be after 12 months?		
What is the **most** my minimum monthly payment could be after 24 months?		
What is the **most** my minimum monthly payment could be after 36 months?		
What is the **most** my minimum monthly payment could be after 48 months?		
What is the **most** my minimum monthly payment could be after 60 months (5 years)?		
What would my minimum monthly payment be after 60 months (5 years) **if the interest rate stays the same?**		
What are the fees and charges due at closing on this loan?		

What are the alternatives to I-O mortgage payments and payment-option ARMs?

If you are not sure that an I-O mortgage payment or a payment-option ARM makes sense for you, there are several other alternatives you could consider.

- Find out if you qualify for a community housing program that offers lower interest rates or reduced fees for first-time homebuyers, making homeownership more affordable.
- Consider a fixed-rate mortgage or a fully amortizing ARM. Shop around for terms and features that fit your needs and your budget.
- Take more time to save for a larger down payment, reducing the amount you need to borrow and making your mortgage payments more affordable.
- Look for a less expensive home. Once you build up equity, you could buy a more expensive home.

What should I keep in mind when it comes to an I-O mortgage payment or a payment-option ARM?

- Both types of loans can be flexible and allow you to make lower monthly payments during the first few years of the loan. You can repay some of the principal at any time to help keep future payments lower.
- Neither loan may be the right choice if the attraction of an initial smaller monthly payment leads you to take out a larger mortgage than you will be able to afford when the interest-only period ends or when the option payments are recalculated.
- Eventually you will have to pay back the principal you borrowed, plus any amounts added to the principal as negative amortization.
- You will have lower monthly payments only during the first few years. You will have larger payments later—and you will need to have the income to cover those larger payments.

Also, note that

- with an adjustable-rate mortgage, interest-only and option-ARM monthly payments can increase, even during the I-O-payment or option period.
- by making I-O or minimum payments, you will not be building equity in your home by paying down the principal on the loan, even though you are making monthly payments. The equity in your home may increase if the market value of your home increases, but the equity could also go down if the market value of your home goes down.
- with payment-option ARMs, you may be adding to the amount you owe on your mortgage if you pay less than the full interest owed each month.

Glossary

Adjustable-rate mortgage (ARM)
A mortgage that does not have a fixed interest rate. The rate changes during the life of the loan in line with movements in an index rate, such as the rate for Treasury securities or the Cost of Funds.

Amortizing loan
Monthly payments are large enough to pay the interest and reduce the principal on your mortgage.

Cap, interest rate
A limit on the amount your interest rate can increase. Interest caps come in two versions:

- periodic caps, which limit the interest-rate increase from one adjustment period to the next, and
- overall caps, which limit the interest-rate increase over the life of the loan. By law, virtually all ARMs must have an overall cap.

Cap, payment
A limit on how much the monthly payment may change, either each time the payment changes or during the life of the mortgage. Payment caps do not limit the amount of interest the lender is earning, so they may lead to negative amortization.

Equity
The difference between the fair market value of the home and the outstanding mortgage balance.

Good faith estimate
The Real Estate Settlement Procedures Act (RESPA) requires your mortgage lender to give you a good faith estimate of all your closing costs within 3 business days of submitting your application for a loan, whether you are purchasing or refinancing a home. The actual expenses at closing may be somewhat different from the good faith estimate.

Index
The index is the measure of interest-rate changes that the lender uses to decide how much the interest rate on an ARM will change over time. No one can be sure when an index rate will go up or down. Some index rates tend to be higher than others, and some change more often. You should ask your lender how the index for any ARM you are considering has changed in recent years, and where the index is reported.

Interest
The price paid for borrowing money, usually given in percentages and as an annual rate.

Margin
The number of percentage points the lender adds to the index rate to calculate the ARM interest rate at each adjustment.

Negative amortization
Occurs when the monthly payments do not cover all the interest owed. The interest that is not paid in the monthly payment is added to the loan balance. This means that even after making many payments, you could owe more than you did at the beginning of the loan.

Prepayment penalty
Extra fees that may be due if you pay off the loan early by refinancing your home. These fees may make it too expensive to get out of the loan. If your loan includes a prepayment penalty, be aware of the penalty you would have to pay. Ask the lender if you can get a loan without a prepayment penalty, and what that loan would cost.

Principal
The amount of money borrowed or the amount still owed on a loan.

For More Information
Additional information about interest-only mortgages and payment-option ARMs is available on the Federal Reserve Board's web site at
www.federalreserve.gov/pubs/mortgage_interestonly/default.htm.

See also these sites:
Looking for the Best Mortgage – Shop, Compare, Negotiate
(at www.federalreserve.gov/pubs/mortgage/mortb_1.htm)

Consumer Handbook on Adjustable Rate Mortgages
(at www.federalreserve.gov/pubs/arms/arms_english.htm)

A Consumer's Guide to Mortgage Settlement Costs
(at ww.federalreserve.gov/pubs/settlement/default.htm)

Partners Online Mortgage Calculator
(at www.frbatlanta.org/partnerssoftwareonline/dsp_main.cfm)

This information was prepared in consultation with the following agencies and organizations:

Center for Responsible Lending

Consumer Federation of America

Consumer Mortgage Coalition

Consumers Union

Credit Union National Association

Federal Deposit Insurance Corporation

Federal Reserve Bank of New York

Federal Trade Commission

Financial Services Roundtable

Freddie Mac

National Consumers League

Office of the Comptroller of the Currency

Office of Thrift Supervision

Rutgers Cooperative Extension

University of Illinois Cooperative Extension

To request additional copies of *Interest-Only Mortgage Payments and Payment-Option ARMs*, please send your name, address, and the number of copies requested to Publications Fulfillment, Board of Governors of the Federal Reserve System, Washington, DC 20551.

November 2006

COMPARISON OF SAMPLE MORTGAGE FEATURES

(for illustration and educational purposes only- does not represent actual terms of loan available from any particular lender)

	Mortgages with a Fixed Interest Rate		Mortgages with an Adjustable Interest Rate (ARM)		
A Typical Mortgage Transaction **Loan Amount $200,000** **30-Year Term**	**Principal and Interest** Fixed Rate (7.0%)	**Interest Only** Fixed Rate (7.0%) Interest Only for the First 5 Years	**5/1 ARM** Fixed Rate for First 5 Years; Adjustable Each Year After First 5 Years Initial Rate for Years 1-5 is 7.0%; Maximum Rate is 12.0%	**Interest Only** Interest Only and Fixed Rate for First 5 Years; Adjustable Rate Each Year After First 5 Years Initial Rate is 7.0%; Maximum Rate is 12.0%	**Option Payment** Adjustable Rate for Entire Term of the Mortgage Rate in Month 1 is 1.25%; Rate in Month 2 through year 5 is 7.0%; Minimum Rate is 12.0%

How Your Monthly Payment May Change	**Minimum Monthly Payment Years 1-5, except as noted**	**$1,331***	**$1,167**	**$1,331**	**$1,167**	**$739-987 (Increasing Annually)**
	Minimum Monthly Payment Year 6 No change in rates	**$1,331**	**$1,414****	**$1,331**	**$1,414**	**$1,565**
	Minimum Monthly Payment Year 6 2% rise in rates	**$1,331**	**$1,414**	**$1,580**	**$1,678**	**$1,859**
	Minimum Monthly Payment Year 8 5% rise in rates	**$1,331**	**$1,414**	**$1,971**	**$2,094**	**$2,319**

How Your Outstanding Balance May Change	**How Much Will You Owe after 5 years?**	**$188,263**	**$200,000**	**$188,263**	**$200,000**	**$221,486**
	Have You Reduced Your Loan Balance after 5 Years of Payments?	**YES** **Your loan balance was reduced by $11,737**	**NO** **You did not reduce you loan balance**	**YES** **Your loan balance was reduced by $11,737**	**NO** **You did not reduce you loan balance**	**NO** **Your loan balanced INCREASED by $21,486**

* This illustrates an interest rate and payments that are fixed for the life of the loan.

** This illustrates payments that are fixed after the first 5 years of the loan at a higher amount because they cover both principal and interest.

*** This illustrates minimum monthly payments that are based on an interest rate that is in effect during the first month only. The payments required during the first year will not be sufficient to cover all of the interest that's due when the rate increases in the second month of the loan. Any unpaid interest amount will be added to the loan balance. Minimum payments for years 2-5 are based on the higher interest rate in effect at the time, subject to a contract limits on payment increases. Minimum payments will be recast (recalculated) after 5 years, or when the loan balance reaches a certain limit, to cover both principal and interest at the applicable rate.

<u>IMPORTANT NOTE</u>: Please use this chart to discuss possible loans with you lender.

ADJUSTABLE RATE MORTGAGE LOAN INFORMATION

IMPORTANT MORTGAGE LOAN INFORMATION PLEASE READ CAREFULLY!

This disclosure describes the features of Adjustable Rate Mortgage (ARM) programs you are considering. Information on other ARM programs available from FREMONT BANK (the "Lender") will be provided to you upon request.

What is an Adjustable Rate Mortgage?
An Adjustable Rate Mortgage is a loan in which the interest rate and the monthly principal and interest payment may change from time to time. If the interest rate increases, your monthly payment will increase. If the interest rate decreases, your monthly payment will decrease. Interest rate and monthly payment changes will be made according to certain rules, which are explained in this disclosure.

How the Interest Rate and Monthly Payment are Determined
Depending on market conditions, your initial interest rate either may be a "premium" rate which is higher than, or a "discounted" rate which is lower than, the sum of the index used to make subsequent adjustments to the interest rate and margin, or your initial interest rate may be based on the rounded sum of the index and the margin. Ask us about the current initial interest rates and the current amount of any interest rate premiums or discounts for the ARM program.

Your initial monthly payment will be calculated in an amount necessary to fully repay the loan balance with interest at the initial interest rate over the loan term.

How Your Interest Rate Can Change
The first interest rate change date can be as soon as the first day of the second month of your loan term, or may not occur for several years. Review the information for the specific ARM program for details.

The rate on some loans changes monthly, some change twice per year, most change annually, and some only change once or twice during the life of the loan. The more often your rate can change, the more you benefit during declining rates. Conversely, during rising rates, your rate and payment will increase sooner.

Starting with the first interest rate change date, your interest rate will be based on the index as of a specific date plus a margin (then rounded to the nearest one-eighth of one percent [0.125%]). Ask us about our current margin for the ARM program(s) in which you are interested.

The “Index" is a rate established in the financial marketplace, not a rate established or controlled by Fremont Bank. Index rates may be published in newspapers such as The Wall Street Journal, or be available from sources such as the Federal Reserve Board. The index for each ARM program is indicated below, as is the source of index values. Should the index cease to be available, the lender will choose a new index based upon comparable information.

If there is a limitation on how much the rate can change on each rate change date that limitation is called the rate change "cap". Some programs have no cap on any change; some have a cap only beginning with the second change, and some have a cap on all changes. See the specific ARM program for the amount of any cap for that program.

Increases in your interest rate are also subject to a lifetime interest rate cap, usually 4% to 7% over the initial rate for your loan. The lifetime cap is shown for each ARM program.

Because of any discounted or premium initial rate and the effect of interest rate caps, changes in your interest rate may not correspond directly to changes in the Index.

How Your Monthly Payment Can Change
The first payment change date can be as soon as the first day of the second month, or may not occur for several years. Payment changes are usually effective the month following rate changes. Review the information for the specific ARM program for details.

At each change date, the lender will recalculate your monthly payment based on the amount necessary to fully repay the remaining loan balance, with interest at the new interest rate, over the remaining term of the loan.

Some loans are amortized over a longer period than the actual term of the loan. These loans are called Balloon Payment Loans. For example, our 30/15 Treasury ARM Loans described below are amortized over 30 years, but the balance owing is due and payable at the end of 15 years. It must be paid in full or refinanced at that time.

You will be notified in writing at least 25 days before the due date of a payment at a new level. This notice will include information about your interest rate, index value, payment amount and loan balance.

Indexes:
An index is an average, usually weighted, which measures changes in the financial "Market" taking place over a time period. It is intended to follow the movement of the cost of funds to the lender.

1 Year Treasury

> This is the weekly average yield on US Treasury Securities adjusted to a constant maturity of one year as made available by the Federal Reserve Board* weekly in Statistical Release H.15. http://www.federalreserve.gov/releases/h15/
> * Subscriptions (for a fee) are available from:
>
> Publication Services
> Board of Governors PO Box 27531
> Richmond VA 23261-7531

Loans tied to the 1-year Treasury index generally have a rate adjustment each year with a lifetime cap of up to 6% over the initial rate. Some programs adjust on the first anniversary of the loan, others do not adjust until the second, third, fifth, seventh or tenth anniversary of the loan (these loans are called 2/1, 3/1, 5/1, 7/1 and 10/1 Treasury ARM Loans respectively). The average interest rate (Index) for 1-year Treasury Securities for December 31, 2008, was 0.40%.

A 30-year1/1 "No Closing Cost" refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.750% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually based on changes in the interest rate. Assuming a maximum rate increase of 2.000% each year, the cap (of 9.125%) would be reached February 1, 2012, and the payment would be $79.30 beginning March 1, 2012. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $42.84 = $1,028.10.

A 30-year 2/1 “No Closing Cost” refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.75% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually after the two-year initial fixed rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 2.000% each year, the cap (of 9.125%) would be reached February 1, 2013, and the payment would be $78.12 beginning March 1, 2013. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $42.84 = $1.028.10.

A 30-year 3/1 "No Closing Cost" refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.750% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually after the three year initial fixed rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 2.000% each year, the cap (of 9.125%) would be reached February 1, 2014, and the payment would be $76.94 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $42.84 = $1,028.10.

A 30-year 5/1 Non-Conforming "No Closing Cost" refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.750% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually after the five-year initial fixed-rate period ends based on changes in the interest rate.

Assuming the maximum rate increase of 5.000% the first adjustment, the cap (of 8.125%) would be reached February 1, 2014, and the payment would be $69.51 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $450,000 would be: $450,000 ÷ $10,000 = 45; 45 x $42.84 = $1,927.69.

A 30-year 7/1 conforming "No Closing Cost" refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.750% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually after the seven-year initial fixed-rate period ends based on changes in the interest rate. Assuming a maximum rate increase of 5.000% the first adjustment, the cap (of 8.125%) would be reached February 1, 2016, and the payment would be $67.53 beginning March 1, 2016. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $42.84 = $1028.10.

A 30-year 10/1 conforming "No Closing Cost" refinance Treasury ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 3.125% (Index of 0.40% + a margin of 2.750% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $42.84. Your payment may change annually after the tenth-year initial fixed-rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 5.000% the first adjustment, the cap (of 8.125%) would be reached February 1, 2019, and the payment would be $64.48 beginning March 1, 2019. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x 42.84 = $1,028.10.

A 30/15 Treasury 30-year 1/1 "No Closing Costs" Treasury ARM loan of $10,000 originated on January 2, 2009, at an initial rate of 3.25% (Index of 0.40% + a margin of 2.875% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $43.52. Your interest rate and payment may change annually beginning on the first anniversary of your loan.

Assuming maximum rate increases of 2.000% each year, the cap (of 9.25%) would be reached February 1, 2012 and the payment would be $80.22 beginning March 1, 2012. Other than the balloon payment (estimated to be $7,794.17) due February 1, 2024, this would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be $240,000 ÷ $10,000 = 24; 24 x $43.52 = $1,044.50.

A 30/15 Treasury 30-year 3/1 "No Closing Costs" Treasury ARM loan of $10,000 originated on January 2, 2009, at an initial rate of 3.25% (Index of 0.40% + a margin of 2.875% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $43.52. Your interest rate and payment may change annually beginning on the third anniversary of your loan. Assuming maximum rate increases of 2.000% each year, the cap (of 9.25%) would be reached February 1, 2014, and the payment would be $77.87 beginning March 1, 2014. Other than the balloon payment (estimated to be $7,566.07) due February 1, 2024, this would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be $240,000 ÷ $10,000 = 24; 24 x $43.52= $1,044.50.

A 30/15 Treasury 30-year 5/1 "No Closing Costs" Treasury ARM loan of $10,000 originated on January 2, 2009, at an initial rate of 3.25% (Index of 0.40% + a margin of 2.875% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $43.52. Your interest rate and payment may change annually beginning on the fifth anniversary of your loan. Assuming a maximum rate increase of 5.000% the first adjustment, the cap (of 8.25%) would be reached February 1, 2014, and the payment would be $70.41 beginning March 1, 2014. Other than the balloon payment (estimated to be $7,258.12) due February 1, 2024, this would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be $240,000 ÷ $10,000 = 24; 24 x $43.52 = $1,044.50.

LIBOR

One-Year LIBOR

The LIBOR Index is the average of InterBank offered rates for one-year U.S. dollar-denominated deposits in the London market (London InterBank Offered Rate – “LIBOR"), as published in The Wall Street Journal. Your interest rate and monthly payment can change every 12 months under this program. Your initial interest rate is not based on the index used to make later adjustments. The initial interest rate could be below the sum of the then-current index plus margin (the “fully indexed rate”). This is called a “discounted” interest rate. Or, the initial interest rate could be above the sum of the fully indexed rate, called a “premium” interest rate. After the initial period, your interest rate will be based on an index rate plus a margin and rounded to the nearest 1/8% (.125%). Your payments will be based on the interest rate, loan balance, and remaining loan term. Ask us for the amount of our current interest rate discounts or premiums.

Loans tied to the 1-Year LIBOR Index generally have a rate adjustment each year with a lifetime cap of up to 6% over the term of the loan. Some programs adjust on the first anniversary of the loan; others do not adjust until the second, third, fifth, seventh or tenth anniversary of the loan. The 1-Year LIBOR index for December 31, 2008 was 2.02500%.

A 30-year 1/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the one-year initial fixed rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 2.000% each year, the cap (of 10.25%) would be reached February 1, 2012, and the payment would be $87.70 beginning March 1, 2012. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

A 30-year 2/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the two-year initial fixed-rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 2.000% each year, the cap (of 10.25%) would be reached February 1, 2013, and the payment would be $86.60 beginning March 1, 2013. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

A 30-year 3/1 “No Closing Cost” Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.25% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the three-year initial fixed-rate period ends based on changes in the interest rate.

For the first 3 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the fourth year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming a maximum rate increase of 2.000% each year, the cap (of 10.25%) would be reached February 1, 2014, and the payment, including both principal and interest would be $90.23 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 3/1 “No Closing Cost” 10yr Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.25% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the three-year initial fixed rate period ends based on changes in the interest rate.

For the first 3 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the eleventh year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming a maximum rate increase of 2.000% each year, the cap (of 10.25%) would be reached February 1, 2014, and the interest only payment would be $85.42 beginning March 1, 2014. This would remain your payment until February 1, 2019 when your interest only period would end and you would begin paying principal and interest. Beginning March 1, 2019 your new principal and interest payment would be $98.16. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 3/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the three-year initial fixed-rate period ends based on changes in the interest rate.

Assuming a maximum rate increase of 2.000% each year, the cap (of 10.25%) would be reached February 1, 2014, and the payment would be $85.47 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

A 30-year 5/1 “No Closing Cost” Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the five-year initial fixed-rate period ends based on changes in the interest rate.

For the first 5 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the sixth year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming the maximum rate increase of 5%, the maximum lifetime cap (of 9.25%) would be reached February 1, 2014, and the payment, including both principal and interest would be $85.64 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 5/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the five-year initial fixed-rate period ends based on changes in the interest rate.

Assuming the maximum rate increase of 5% the first adjustment, the cap of (9.25%) would be reached February 1, 2014, and the payment would be $77.77 beginning March 1, 2014. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

A 30-year 5/1 “No Closing Cost” 10yr Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.25% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the five-year initial fixed rate period ends based on changes in the interest rate.

For the first 10 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the eleventh year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming a maximum rate increase of 5.000%, the maximum lifetime cap (of 9.25%) would be reached February 1, 2014, and the interest only payment would be $77.08 beginning March 1, 2014. This would remain your payment until February 1, 2019 when your interest only period would end and you would begin paying principal and interest. Beginning March 1, 2019 your new principal and interest payment would be $91.59. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 7/1 “No Closing Cost” Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the seven-year initial fixed-rate period ends based on changes in the interest rate.

For the first 7 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the eighth year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming the maximum rate increase of 5%, the maximum lifetime cap (of 9.25%) would be reached February 1, 2016, and the payment, including both principal and interest would be $87.61 beginning March 1, 2016. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 7/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the seven-year initial fixed-rate period ends based on changes in the interest rate.

Assuming the maximum rate increase of 5% the first adjustment, the cap of (9.25%) would be reached February 1, 2016 and the payment would be $75.82 beginning March 1, 2016. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

A 30-year 10/1 “No Closing Cost” Interest Only LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial interest only payment of $35.42. Your payment may change annually after the tenth-year initial fixed-rate period ends based on changes in the interest rate.

For the first 10 years of your loan, your regular monthly payments will not reduce your loan balance. Payments would remain interest only until the eleventh year when payments would be adjusted to fully amortize (pay off) the loan. Your monthly payment will increase - even if interest rates stay the same – because you must pay back the principal as well as the interest.

Assuming the maximum rate increase of 5%, the maximum lifetime cap (of 9.25%) would be reached February 1, 2019, and the payment, including both principal and interest would be $91.59 beginning March 1, 2019. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $35.42 = $850.00.

A 30-year 10/1 “No Closing Cost” refinance LIBOR ARM loan of $10,000 originated January 2, 2009, at an initial interest rate of 4.25% (Index of 2.02500% + a margin of 2.250% and rounded to the nearest 1/8%) would have an initial monthly principal and interest payment of $49.19. Your payment may change annually after the tenth-year initial fixed-rate period ends based on changes in the interest rate.

Assuming the maximum rate increase of 5% the first adjustment, the cap of (9.25%) would be reached February 1, 2019 and the payment would be $72.76 beginning March 1, 2019. This would be the maximum possible payment on the loan. The initial rate and payment can increase or decrease substantially on the loan depending on changes in the index.

To determine what your payment would be, divide your proposed loan amount by $10,000. Then multiply the monthly payment by that amount. For example, the monthly payment for a loan amount of $240,000 would be: $240,000 ÷ $10,000 = 24; 24 x $49.19 = $1,180.66.

Thank you again for choosing Fremont Bank to help you with your real estate financing needs. It is our pleasure to serve you.