

# Understanding Mortgages

**SUBMITTED BY:** WGYP Summer 2011 Instructor

**SUBJECT(S):** Personal Finance

## ≡ OVERVIEW:

In this lesson, students will begin to understand the process of how to go about owning a house. They will study the application process for a mortgage; who to talk to in order to buy a house; what criteria are used to get mortgage approval; and the popular types of mortgages available in the market. They will be given different types of mortgages and asked to make a choice based on their preferred mode of payment, using the consumer decision-making process.

## ≡ NBEA STANDARD(S):

- Personal Finance, V. Buying Goods and Services
- Personal Finance, VII. Using Credit

## ≡ WHARTON GLOBAL YOUTH PROGRAM ARTICLE:

- “Payday Loans and the Perils of Borrowing Fast Cash”

## Common Core Standard(s):

- Reading Informational Text — RI.9 -10.1.; RI.9 -10.2.
- Speaking and Listening — SL.9 -10.1.

## Purpose:

- By the end of this session, students would have a better understanding of the types of mortgages available in the market.
- They will learn about the key steps they need to take in order to own a house, such as talking to a loan officer and selecting a neighborhood based on certain criteria.

**Knowledge@Wharton Article:**

Worksheet 1: Excerpt from, “[Victimizing the Borrowers: Predatory Lending’s Role in the Subprime Mortgage Crisis](#)”

**Other Resources/Materials:**

Internet/Computer/Projector

**Key Terms:**

Wharton Global Youth Program glossary: [Housing Bubble](#), [Mortgage Loan](#)

**Activity:**

*Introduction (5 -7 mins)*

Begin the lesson by asking students to think about the main factors that people consider when choosing a house or neighborhood. When it comes to real estate, price has a lot to do with location. Ask them to think about what would make them want to live in a particular neighborhood. Some reasons could include: good schools, hospitals, public transport system, shopping, safety, parks, beaches, living close to downtown, suburb, access to main highways, etc.

*Wharton Global Youth Program Video (5 mins)*

Show the video about mortgage loans. Explain to students what a mortgage is, and that unless they have the cash to buy a house, a mortgage loan is the only way to do it.

*Teacher-led Discussion (15 mins)*

As a class the following key areas should be discussed to give a basic understanding of mortgage loans. After students think about where they would want to live and negotiate the price,

the next step is how to pay for the house? In other words, how does one apply for a mortgage loan and what are the different types of mortgage loans available?

The teacher can introduce the following facts to the students:

- They can choose a mortgage option that best suits their financial situation:
  - Types of mortgages:
    - 30 Year Fixed (lower monthly payment).
    - 15 Year Fixed (higher monthly payment).
    - ARM (adjusted rate mortgage) for 5 years and 3 years.
- Usually the buyer has to pay 20% of the home's price as a down payment. If you can't, then you may have to buy private mortgage insurance.
- The buyer also has to pay all closing costs, which are essentially different fees relating to the mortgage.
- You can also use your IRA account to get some more liquid assets for the payment.

What are the steps in to apply for a mortgage?

- Income/Salary
  - One rule says that a home should cost about two-and-a-half times your gross annual salary. If you have significant credit card debt or other financial obligations like alimony or even an expensive hobby, then you may need to set your sights lower.
  - Another rule of thumb: All your monthly home payments should not exceed 36 percent of your gross monthly income.
- Down payment Savings
  - Making sure you have enough cash on hand for this. If not, you may need to save or end up paying a higher interest.
- Past credit performance
  - Credit card debts.
  - Lenders consider your debt to income ratio in order to get approved for a mortgage (it should be relatively low).

*Reading (5 mins)*

Have the students read Worksheet 1 on predatory lending.

*Group Discussion (5 mins)*

Who are subprime mortgages designed for? What is predatory lending? What are foreclosures? Why would someone have poor credit?

**Tying It All Together:**

The teacher can close the discussion by going over some of the highlights of the lesson: the effect of location and other factors on real estate prices; the importance of understanding how mortgage loans work; and the importance of avoiding subprime loans and predatory lending.

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