



APR - Comparing Apples to Apples

What is APR?

APR stands for "Annual Percentage Rate" and is the cost of credit expressed as an annual rate. APR is one of the most misunderstood numbers people come across when applying for a loan.

As consumer loans, and mortgage loans in particular have become more complicated, it became necessary to help standardize the ways lenders advertise and quote interest rates. APR was created to help people compare similar loans from different lenders and to explain the ultimate cost of credit. Quoting APR is required by Regulation Z of the Federal Truth-in-Lending Act.

Why is the APR higher than the interest rate?

Because you may be paying loan discount "points" and other "prepaid" finance charges at closing, the APR disclosed is often higher than the interest rate on your loan. This APR figure can be compared to the APR on other loan programs to help you compare the cost of credit for each type of loan.

How do I find the APR on my loan?

Once you have applied for a mortgage loan, the Federal Truth-in-Lending Disclosure Form (TIL) will be sent to you. If you have applied for more than one type of loan, you will receive a TIL for each loan type. At the top of the form, you'll find your "APR."

How do I use this figure to compare loans?

Great question! Here's an example: <<locompany>> offers a 30-year fixed rate mortgage for 8.000% and Teeny Tiny Bank offers a 30-year fixed rate mortgage for 7.000%.

Easy choice, right? Not so fast...! Before lenders and mortgage brokers were required to quote the APR it was hard to tell which loan would be the better deal. In this example, Teeny Tiny Bank quotes the lowest rate (note rate) but neglected to list a few other things. They also charge 7 discount points, a 1.000% origination fee, and they require mortgage insurance. <<locompany>> quotes no points and no origination.

On a \$100,000 loan, Teeny Tiny Bank charges an additional \$10,000 compared to <<locompany>>'s fixed rate loan. You could save \$68 per month with Teeny Tiny Bank's loan, but you had to spend \$10,000 to receive this benefit. The \$10,000 must be included as a cost of financing and is reflected in the APR figure. In this case, if you plan to be in the home less than 12 years, the 7.000% rate doesn't make financial sense.