# *What is an assumable mortgage and how does it work? Pros and cons*

### What is an assumable mortgage loan?

An assumable mortgage is one that allows a new borrower to take over an existing loan from the current borrower. Typically, this entails a home buyer taking over the home seller's mortgage.

The new borrower — the person 'assuming' the loan — is in the same position as the person passing it on. They'll have the same terms and conditions, the same mortgage rate, the same remaining repayment period, and the same mortgage balance.

In other words, it's effectively swapping one borrower's name on the mortgage agreement for another.

### How does an assumable mortgage work?

An assumable mortgage seems simple at face value: You take over an existing mortgage from someone else and its terms, interest rate, and loan amount stay the same.

That means your monthly payments are in the same amount as the original borrower, and if you pay the loan in full, you'll finish paying off the home on the same date they would have.

In practice, though, assumable mortgages are a little more complex. They're not exactly a free pass for someone who's having trouble qualifying for a new loan.

There are three things that buyers should know about how assumable mortgages work:

1. Not all types of mortgage loans are assumable. Conventional loans cannot be assumed, for example, but FHA and VA loans can

2. Not just anyone can assume an existing mortgage. You still must apply with the lender and qualify for the loan
3. You generally need to make a down payment when assuming a mortgage, and it may be larger than expected

Remember, when you assume a mortgage, you're taking over the homeowner's *remaining* loan balance. In most cases that won't cover the full purchase price of the home, so you'll still need a down payment to make up the difference.

In the right situation, there can be big benefits to taking on an assumable mortgage. But this strategy won't work for everyone, so it's important to understand the pros and cons before signing on.

**Why use an assumable mortgage?**

An assumable mortgage could be a great find in a rising interest rate environment.

One of the biggest benefits to this type of mortgage is that you could lock in a rate far below the current market, provided rates have risen since the original loan was made.

Look at one example.

According to Freddie Mac, the all-time low weekly mortgage rate occurred on Jan. 7, 2021, when it dipped to 2.65% for a 30-year fixed-rate mortgage.

But, just two months later, rates had risen above 3%. And some expect these rates to top 4% or higher over time.

Now imagine it's a few years later, and Freddie Mac's weekly average is 4.6% for a 30-year mortgage. If you're offered an assumable mortgage at 2.6%, you'd likely be over the moon.

According to our **mortgage calculator** (which you can use to model your own scenario), monthly principal and interest payments at 4.65% would be $1,025 on a $200,000 loan. But they'd be $800 at 2.6%.

That's a saving of $225 per month or $2,700 per year — every year.

That’s the fantastic advantage assumable mortgages can offer. But few scenarios will play out exactly like this. So, we also need to look at the restrictions and downsides of assumable home loans.

## Assumable mortgage pros and cons

Clearly, an assumable mortgage makes little sense when mortgage rates are falling. There’s no advantage in taking over an existing loan when its rate is higher than one you can get by making a new application.

That’s why there’s very little awareness of this option: nobody has wanted an assumable loan during the many years that rates have been falling. But rates are starting to swing back upward. So, there’s a chance assumable mortgages could look more attractive in the coming months and years.

### Assumable mortgage pros

For a home buyer, the upsides of assuming a mortgage loan include:

- **Low interest rates** — Assuming rates are rising, you could lock in an older, lower interest rate
- **Capped closing costs** — The FHA, VA, and USDA impose limits on closing costs when a mortgage is assumed. And you probably won’t need a new home appraisal
- **Long-term savings** — You’ll likely save on interest because you’re borrowing less over a shorter time than with a new mortgage

Those pros may not be numerous. But they’re powerful.

### Assumable mortgage cons

Again, for buyers, the downsides tend to be:

- **A higher down payment** — You may need a bigger down payment than the typical minimums allowed
- **Mortgage insurance** — For FHA and USDA loans, you inherit mortgage insurance premiums, which are always required on

these types of mortgages. VA loans do not have continuing mortgage insurance

- **Limited loan options** — Not all types of mortgage loans are assumable. For borrowers with great credit and big down payments, it might make more sense to take out a new conventional loan rather than assuming an existing government-backed loan

That higher down payment could be a big drawback of assuming a mortgage. But when does it apply?

The down payment requirement will depend on the unique circumstances of the loan you're assuming.

**Do I need a down payment when assuming a mortgage?**

When you assume a mortgage, you take over the homeowner's remaining principal balance.

The current borrower has likely paid off a chunk of their mortgage. The home may have also increased in value since it was purchased. So, there will be a 'difference' between the loan amount you assume and the purchase price.

That difference is your down payment. And it may be higher than the down payment you'd have to make on a new loan.

Let's go back to the example we used above: Say the seller got a $200,000 mortgage at 2.6% in January 2021.

Imagine it's now January 2023, and you want to assume that mortgage.

Well, the original borrower made a 3.5% FHA down payment of $7,500 on a $207,500 home. And home price inflation means the market value is now, perhaps, $220,000.

**Working out your down payment amount**

Because the homeowner made all their monthly payments over the past two years, they reduced the mortgage balance to around $190,900.

Imagine you're buying the house at its exact market value: $220,000.

- You're paying $220,000
- But your assumed mortgage is only $190,900
- You need a down payment of $29,100
- **That's a 13% down payment**

If you're assuming a VA or FHA loan, the minimum down payment is 0% or 3.5%, respectively. So, you're putting *a lot* more money down than you'd need to on a new mortgage.

But you're also securing a far lower interest rate than you'd likely get otherwise.

If you don't have that much for your down payment, should you pass on this sweet deal? Or should you try to bridge the difference?

**Using a home equity loan to fund your down payment**

One option for home buyers is to use a **home equity loan** to supplement the down payment on an assumable mortgage.

This involves taking out a second mortgage at the same time you assume the primary mortgage. Moving forward, you'll have two separate mortgage payments until the home equity loan is paid off.

FHA, VA, and USDA loans allow second mortgages to purchase property — a.k.a subordinate financing. But there's no guarantee. These agencies can reject a second mortgage if they don't like the terms. Fully disclose to the relevant agency that you will be obtaining subordinate financing and submit any related documentation.

Is the second mortgage strategy worth it? It's a question of running the numbers.

You know how much you're going to save through lower interest (around $2,700 per year in our example). And you can find out how much you'll pay for a home equity loan.

If your home equity loan costs are lower than your overall savings, this strategy might make sense for you.

Note, however, that your second mortgage will likely come from a different lender than the one that owns the mortgage you're assuming. So, you must work with the current mortgage lender and make sure it's willing to play ball.

You'll also likely need a credit score of 680 or higher to qualify for a home equity loan.

## Two kinds of assumable mortgages

There are two types of assumable mortgages.

### Simple assumption

The first is a 'simple assumption.' This means the buyer takes over making payments on the mortgage without involving the lender.

Anyone can do a simple assumption through a purely private arrangement. But these agreements are risky.

The trouble with a simple assumption is that the original borrower retains complete liability for the mortgage.

If the buyer falls behind with payments or otherwise breaches the mortgage agreement, it's the seller whose credit and bank balance will suffer. And if the lender finds out, it might demand that the mortgage balance is paid in full right away.

**Simple assumptions are exceedingly rare except sometimes for family transactions.** You may be willing to accept the risk if the person taking on the mortgage is, say, your spouse, son, or daughter. But in most situations, a simple assumption is too risky to make sense.

### Novation

Most assumable mortgages are 'novations.' These require the consent of the mortgage lender, so the buyer will go through the same underwriting process as any other new borrower — complete with a credit evaluation and financial documentation.

The good news is, with a novation, the original borrower walks away free and clear. Whatever happens to the loan after the transaction is complete is purely between the lender and the new borrower.

**Which mortgage loan types are assumable?**

Government-backed mortgages are generally assumable. That means an assumable loan will typically be one of three types:

- FHA assumable mortgage — Backed by the Federal Housing Administration
- VA assumable mortgage — Backed by the Department of Veterans Affairs
- USDA assumable mortgage — Backed by the U.S. Department of Agriculture

If you want to assume any of these loans, you must be eligible.

**FHA loans** are the most flexible. Credit score requirements start at just 580 FICO, and you don't need a perfect credit history to qualify.

USDA loans are geographically restricted, but you won't have to worry about that since the existing loan was already found to be USDA-eligible. However, the new borrower must meet regional income limits.

**VA loans** are a little more restrictive. You must be a veteran, active-duty service member, or surviving spouse to qualify. The lender will check your status by requesting a Certificate of Eligibility (COE) from the VA.

**Conventional loans are not assumable**

Unfortunately, nearly all mortgage agreements for conventional loans (those **not** backed by the government) contain a "due on sale" provision. As the name implies, the full mortgage balance falls due when the home is sold. So conventional and conforming loans are generally not assumable.

Fannie Mae does offer an exception. But only for adjustable-rate mortgages (ARMs). And, except in some weird circumstances, that defeats the object of assuming a mortgage.

What might those ‘weird circumstances’ be? Well, it might just be possible for mortgage rates to rocket so high that the **caps limiting rate rises** on ARMs make assumption attractive.

And there’s another exception in the form of ‘non-qualifying assumable mortgages.’ These are loans that existed prior to December 14, 1989, which is over 30 years ago. Given that most mortgages last only 30 years at most, you’re unlikely to find one of these.

**Assumable mortgage process**

If rates are rising — and you happen to find a home seller with an assumable mortgage — this option might look attractive. In this case, the process is straightforward.

You don’t get to shop around for the best mortgage rate because that rate is already set. You wouldn’t want the existing rate if you weren’t happy with it.

But, besides that, the process is very similar to applying for any other mortgage. You’ll fill out a loan application and provide supporting documents like:

- Income and employment information
- Previous 2 years tax returns
- Recent paystubs
- Recent bank statements
- Proof of other assets, like retirement and investment accounts

The mortgage underwriter will also pull your credit report and credit score to make sure you meet minimum credit requirements for the loan type being assumed.

Finally, you’ll have to show you can afford the down payment and closing costs — whether using money in your bank account, a second mortgage, or another source of funds like **down payment assistance**.

## Assumable mortgage FAQ

### How do you qualify for a mortgage assumption?

The same way you qualify for any other mortgage. You'll need to apply and get approved for the mortgage by meeting the lender's requirements for credit, debt-to-income ratio, down payment, income, and assets.

### How much does a loan assumption cost?

You'll have to pay closing costs on a loan assumption, which are typically 2-5% of the loan amount. But some of those may be capped. And you're unlikely to need a new appraisal. So, you may pay less on closing than a 'typical' home purchase — but only a bit less.

### Do you need a down payment to assume a mortgage?

Usually. And it's often more than with a new mortgage, because you'll probably be covering some or all the present owner's past payments. But you might not need one if you're assuming a recent VA or USDA loan because the lender doesn't require a down payment. So, it comes down to your negotiations with the owner.

### Do assumable mortgages have closing costs?

Yes. Assumable mortgage closing costs are close to those for a traditional mortgage, though you may save a few hundred dollars or more by skipping a home appraisal.

### Can my spouse assume my mortgage?

Certainly. Anyone can assume your mortgage with the lender's consent. But you may be inquiring about a "simple assumption," where the lender knows nothing about it. Some borrowers do come to these private arrangements, but they're loaded with risk — so read the relevant section above. Lenders often have special assumption arrangements for surviving family members if a borrower dies.

### Can my children assume my mortgage?

Yes. But the same cautions apply if you're hoping to do a 'simple assumption' (see the previous FAQ).

### What is a non-qualifying assumable mortgage?

A 'non-qualifying assumable mortgage' is one that originated prior to December 14, 1989. Since most mortgages have a loan term of 30 years or less, non-qualifying assumable mortgages are extinct.

### Is an assumable mortgage a good idea?

It certainly can be. But, like all similar questions, the answer will depend on your circumstances and needs. If you get the chance to assume a mortgage at an appreciably lower rate than you can get elsewhere, you should run the numbers.