

## Escrow Accounts Provide You with Peace of Mind

### What is an escrow account?

An escrow account is often established on your behalf by your mortgage lender or servicer when you take out your mortgage loan. However, if an escrow account was not set up when you took out your mortgage loan, you may now be able to do so.

The purpose of the account is to collect and hold funds to pay your property taxes, property insurance premiums, or other charges when they become due.

Real estate taxes and property insurance premiums must be paid regularly—typically, payments are due once or twice a year—and failure to pay these charges on time may result in tax penalties or lapses in insurance coverage.

### What are the benefits of an escrow account?

Most lenders require an escrow account for mortgage loans with less than a 20 percent down payment. An escrow account helps you:

- **Manage your budget:** You don't have to make lump sum payments when your taxes and insurance are due because funds from your monthly payments throughout the year are set aside to cover those obligations.
- **Gain peace of mind:** You don't need to keep track of when your tax and insurance bills are due, knowing the payments will be made, on time, on your behalf.
- **Ensure that your home is protected:** With paid-up insurance coverage and taxes, you protect your investment in your home and meet your lender's requirements.

### How an escrow account works

- Your monthly mortgage payment includes an amount for property taxes and insurance, in addition to the amount you owe for principal and interest.
- The amount of your monthly mortgage payment that is for taxes and insurance is placed by your lender or mortgage servicer into an escrow account—meaning that the funds must be used only for the intended purpose of paying your taxes and insurance on your behalf.
- Your lender or mortgage servicer pays the taxes and insurance bills for you when they are due.
- Your lender or mortgage servicer examines any changes in your tax and insurance costs (for example, your local government may change the amount of your real estate taxes). Your lender or servicer then sends you a statement each year showing the prior year's activity—amounts collected from you and placed in escrow as well as the payments made on your behalf—and showing any adjustments that may be needed based on changes in your tax and insurance costs.

**Here is a simplified example\* of how escrow payments are calculated:**

Annual real estate taxes:  $\$1,800 \div 12 \text{ months} = \mathbf{\$150 \text{ per month}}$   
Annual property insurance:  $\$720 \div 12 \text{ months} = \mathbf{\$60 \text{ per month}}$   
**Total monthly taxes and insurance: \$210**

So in this example, \$210 would be added to your total monthly mortgage payment and applied to your escrow account. You might hear your total monthly mortgage payment referred to as your "PITI"—for principal, interest, taxes, and insurance.

\*The amounts you owe for real estate taxes and insurance will vary—this is a simplified example, and your lender likely will use a more detailed calculation method that considers various factors. Ask your lender for a full explanation and an estimate of the escrow payment on your mortgage.

**Do you have an escrow account?**

If you are not sure if you have an escrow account, check your monthly mortgage account statement or contact your mortgage loan servicer directly. Your account statement will typically indicate your "Escrow Balance" and the amount of your total monthly mortgage payment that is applied to "Escrow."

**Should you establish an escrow account?**

If you do not have an escrow account, you may want to establish one. Again, ask your mortgage loan servicer for more information.

With an escrow account, you can be assured that your taxes and insurance will be paid on time. Because funds are automatically collected each month, you can also be assured that you will have enough funds ready for this purpose. And most importantly, you can protect yourself against serious consequences, such as tax penalties for late payment of taxes, or lack of insurance coverage on your home should disaster strike when your insurance policy has lapsed.

**Want more information?**

For more information, talk with your lender or mortgage servicer to determine if you are setting aside adequate funds in your escrow account or if you should set up an escrow account. Also, the U.S. Department of Housing and Urban Development offers "Frequently Asked Questions about Escrow Accounts for Consumers" at: [www.hud.gov/offices/hsg/sfh/res/respfaq.cfm](http://www.hud.gov/offices/hsg/sfh/res/respfaq.cfm).