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Are You Thinking of Refinancing Your Home? Consider a HELOC.

Let's Talk Home Financing

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Recently, several readers have asked about the wisdom of refinancing their mortgages to retrieve equity, with the goal of eliminating very costly consumer debt. Since long-term mortgage rates have stubbornly refused to fall, a HELOC or similar second mortgage may be a better option. I talked to **Jaxzann Riggs** at **The Mortgage Network** for her advice and to gather more information.

HELOCs are a line of credit secured by the equity in your home. Most offer a variable rate, which means that the cost of borrowing will fall if rates improve in the next 24-36 months. Some HELOCs offer an "interest only" option, while others are second mortgages with fixed interest rates and monthly payments applied to both principal and interest. These terms are often used interchangeably, so be sure that you are clear on which kind of loan you are applying.

Many consumers have 10 to 20 revolving accounts. Along with traditional credit cards, they have in-store accounts that came with a great introductory rate but now have higher interest rates. The minimum monthly payments may be only $30-$100 a month per account, but in total they add up quickly.

While some people can easily afford minimum payments, they may be shocked to learn how much is going towards interest each month. Consolidating these debts into a HELOC may save hundreds or even thousands of dollars monthly.

According to LendingTree, the average interest rate for new credit cards is 24.66% and in-store retail credit cards can top 30%. Currently HELOC rates are averaging 13 to 15 percent. While this rate is likely considerably higher than your current mortgage interest rate, it's much lower than most credit card APRs. A HELOC allows borrowers to utilize equity in their home without sacrificing the low rate that they may have on the bulk of their housing debt.

Let's do the math with a hypothetical scenario. Richard and Amanda have a home in Denver with significant equity. They have eleven revolving accounts that include both traditional and "in-store" cards. In total, their revolving debt is just under $56,000, and their minimum monthly payments come to $1,735. If we use the average APR of 24.66%, $1,150 of that payment is being applied towards interest, and only $584 pays down their balances.

If they obtain a HELOC for $56,000 and pay off their credit cards, even with a high interest rate estimate of 14%, their new monthly payment is only $664, **saving them $1,071 each month!**

It's crucial to consider the costs and risks of a HELOC as well. If they get a 30-year second mortgage, only about $10 goes towards reducing the principal each month initially. If their loan is an interest only loan, 100% of the payment is paying interest with the balance staying the same. To truly take advantage of the loan to eliminate their debt, they would need to pay more than their statement balance each month. If they paid an additional $500, totaling $1,164 each month, their entire debt will be paid off in under 6 years, saving over $156,000 in interest.

The best time to apply for a HELOC is when it's an option, not a necessity. Changes in income or a Debt-to-Income ratio that is too high can limit your options, increase your offered interest rate, or even disqualify you altogether. Many HELOCs allow you to pay your line of credit to zero and redraw as needed for up to 10 years. If you have equity in your home and are considering a refinance or a HELOC, I suggest you call Jaxzann Riggs at **303-990-2992** for an analysis of your circumstance.