Read the Fine Print on Your Home Equity Loan BEFORE You Sign

Do you know enough about the details of a home equity loan to protect yourself from unpleasant surprises?

Let's start with interest rates! Before you sign up for that home equity loan, you should understand the interest rate.

The Annual Percentage Rate (APR) is the key to a loan. In the case of a home equity loan, the bank will often give you a discounted introductory rate to get you to sign up for the loan.

But that rate is temporary. It usually only lasts about six months. Then most home equity loans will convert to a variable rate, dependent on the prime rate set by the Federal Reserve Bank.

You need to know what the CEILING for your rate increase will be. What is the maximum the loan interest rate can increase over the life of the loan? Can you handle payments at the rate if necessary?

Don't compare the interest rate for a home equity line of credit to the interest rate of a standard home equity loan. The structure, term and type of loan are very different from the structure of a home equity line of credit, so you would be comparing apples to oranges.

If the terms and length of a home equity loan are the same as a home equity loan offered by another lender, you can compare THOSE interest rates and draw conclusions. But be sure that all terms and conditions are the same or you are not comparing two equal loans.

The interest rate is NOT the total cost of the loan. When you sign up for a home equity loan you will have closing fees and 'points' on that loan. You'll have to pay an appraisal fee for the bank to estimate the value of your home and decide how much money they are willing to lend you.

You'll also have to pay an application fee, and points on the loan (as a percentage of the credit the bank is giving you), title search fees, and maybe attorneys fees (depending on the loan total, and the state where you are applying for the loan).

Some banks charge a transaction fee when take money from your line of credit, but that is only if you have a home equity line of credit, NOT if you have a home equity LOAN.

It is important to find out if your loan structure includes balloon payments. If you have to pay a large lump sum at the end of the loan term you may not be able to make the payment, and the ownership of your home may be in jeopardy.

Balloon payments are part of a home equity loan structure that allows you to pay the interest on the loan amount over the life of the loan. At the end of the term you have to pay the full principal (which can be $30,000, $60,000 or even more). Can you afford that?

The lender will offer you a better interest rate, which will make your life easier as you are making payments, but you will have to swallow the entire principal of the loan when the loan expires.

You should also look at the loan-to-value ratio of your loan. Loan-to-value (LTVR) means the percentage of the value of your home your bank will lend.

LTVR used to be restricted of 80% of your home value, so if your home valued at $200,000, the bank would loan you $180,000.

Some home equity loans today let you borrow 100% of your home value - OR EVEN MORE.

These loan interest rates are very high and you can't write off more than 100% of the value of your home on your taxes, so you are left to swallow the rest of your interest payments on your own.

Furthermore, if you sell your house for its appraised value, you owe more money on the loan than your home sale provide, and you have to come up with the extra money to pay off the loan.

For a loan that is 100% of the value of your home or higher, you will need loan insurance and that is also expensive. Try to pick a loan that does not exceed 70% to 80% of the value of your house (including outstanding mortgages) and you will protect your investment and your financial security.

If you research your loan and read the fine print, if you compare banks and loan terms and understand ALL the charges included in the loan, you are on the right track. Just remember to avoid balloon payments and overextended loan-to-value ratios, and you can protect yourself and the value of your home.

Source: http://www.articlecircle.com

About the Author

Are you considering a home equity loan or line of credit? Find out everything you need to know about home equity loans at our web site: http://www.homeequityloansdnld.com