



Being a Responsible Homeowner

Home Equity Loans

Being a Responsible Homeowner: Home Equity Loans

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Many homeowners purchase property to build equity. Equity is the difference between the market value and the amount owed on the property. The following examples illustrate this concept.

Example 1

Market Value	Amount Owed		Equity
\$110,000	– \$65,000	=	\$45,000

Example 2

Market Value	Amount Owed		Equity
\$102,000	– \$90,000	=	\$12,000

As a homeowner you can build equity by paying down your mortgage. The more you pay down your mortgage the more equity you build. You also can build equity in your neighborhood by keeping up the maintenance of your house and encouraging your neighbors to maintain their property. The more homeowners do to help make their neighborhoods attractive the more potential homebuyers will want to buy in that neighborhood.

Another way to build equity is to buy in an area where houses are selling quickly. This is not a guarantee that the houses will appreciate any faster than another area. However, as long as demand continues for that specific area, the prices of the houses there should continue to go up.

It is possible that equity can decrease. If homeowners do not maintain their home, crime

goes up in a neighborhood or the economy slows, the overall market value can either remain steady or decrease. For example, if people start moving out of a neighborhood (for whatever reason) at a faster rate than people buy in the neighborhood, some sellers could lower the asking price of their house. This could cause a domino effect for other sellers. When one seller lowers the price the others will probably follow. This could decrease the market value of your house.

Home equity loans

Home equity loans are loans against the equity you have in your home. Home equity loans can be taken out as a second or junior mortgage. Some are fixed loans with a definite amount, while others are lines of credit. This process can become expensive and complicated if not done properly.

The difference between a home equity loan and a home refinance is that the primary mortgage loan will remain in place. Like the original mortgage, the loan will be secured by your house. If you default on the loan the mortgage company will have the option to foreclose on your property.

Reasons for taking out a home equity loan vary from person to person. Some borrow to consolidate bills, while others may do it to pay for a child's education, make house repairs or pay medical expenses. Regardless of the reason, it is not recommended that you turn unsecured debt, such as credit card debt, into debt secured by your house.

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The first financial responsibility of a homeowner is to pay the mortgage payment on time each month. Because some homeowners are uncomfortable having a large mortgage debt, they pay ahead on their loans to get out of debt sooner. Other people refinance their loan to get better interest rates.

Getting Ahead on Your Loan

Even though homeowners can expect to pay more interest throughout the life of the 30-year term than on a shorter-term loan, there are ways to minimize the total interest paid. A simple step is to make more than the minimum monthly payment, if prepayment is allowed. Some people take out a 30-year mortgage but make payments as if it were a 15-year term. By doing this they are on track to pay off their mortgage in 15 years. However, if something happens and they cannot make the higher payment, they can make the 30-year term payment until they get back on track.

Another option is to make an additional payment each year. If making this extra payment all at once is a challenge, consider dividing up the principal and interest portion of the payment into 12 equal amounts. This can shorten a 30-year mortgage by several years.

Example

If your payment is \$700 (excluding taxes and insurance) divide the payment by 12:

$$\$700 / 12 = \$58.33$$

Making an additional \$58.33 payment toward the principal each month could save about seven years on the mortgage. This adds up to about \$58,800. To calculate the exact savings on the loan use an amortization schedule which you can get from your loan officer.

Refinance Your Home

A decision that many homeowners will encounter at some time is deciding whether to refinance. Refinancing consists of paying off a current loan through a new loan on the home.

Refinancing can be a great tool for homeowners if done appropriately. Some homeowners decide to refinance their mortgage when interest rates drop. Others may choose to pay off their current loan and get extra money to make home improvements, pay for child's education or for other personal reasons. Refinancing your loan with a lower interest rate may lower your mortgage payment. Homeowners that are currently in adjustable rate mortgages or balloon mortgages also may consider refinancing.

Refinancing can be worthwhile, but it may not be for everyone. Consider refinancing when interest rates drop below the rate on your current loan. The interest rate on the loan is not the only thing to consider. You also should consider how long you plan to live in the house. It takes about three years to see the benefit of refinancing because of the fees and costs associated with the process. Refinancing also may be a good option if the lender is willing to work with you to negotiate fees based on your past relationship with the financial institution.

Reasons to consider refinancing include:

- Interest rates have dropped and you have calculated the cost and benefits, determining that refinancing would be financially wise.
- You feel your interest rates may increase with your adjustable rate mortgage and want to stabilize your payment by refinancing to a fixed-rate mortgage. Mortgage options are discussed in the Home-buying Process module.
- You find a better mortgage product that will meet your current and future needs. For

example: Better rates, lower payment, more flexible payment options, etc.

- Refinancing to a loan product that will allow you to build equity faster.
- Refinancing to allow you to tap into your home equity to pay for major expenses or purchases such as tuition expenses for your child.

When a lender gives you a quote for a new loan make sure the benefits outweigh the costs of refinancing your current loan. If you determine the loan product is not the best option, do not give up. Go somewhere else and shop around. A different financial institution may offer a better loan option that meets your needs. Do not rush refinancing. In a few months interest rates could actually go down, putting you in a better position for refinancing. Refer to the Mortgage Shopping Work Sheet to help you with this process. If you would like to read more on the mortgage process refer to the Home-buying Process module.

Some of the costs associated with refinancing include:

- Loan Application Origination or Processing Fee – This charge covers the expenses of preparing mortgage documents, legal services, borrower credit investigation, notary charges, appraisal fee and any other fees. These expenses are sometimes itemized. When FHA or VA financing is obtained, the origination fee is limited to 1 percent of the mortgage. Other expenses will be added to this fee.
- Title Search and Title Insurance – This is a fee charged to the applicant to verify ownership of the property through the county assessor's office. Also included in this fee will be the title insurance which protects all stake holders of the transactions in case of discrepancies with the title of the property. If you are using the same title insurance company that you used for your initial purchase you may qualify for a discount.

You choose the title insurance company. If you change financial institutions and the new loan officer does not use the title insurance company you worked with previously, you have the right to request this company.

When you refinance you can expect to pay many of the same fees as when you purchased your home including:

- Application fee
- Appraisal fee
- Survey costs
- Homeowners hazard insurance
- Lender's attorney's review fees
- Title search and title insurance
- Home inspection fees
- Loan origination fees
- Mortgage insurance
- Points

Property Taxes

One of the responsibilities all homeowners have is to pay their local property taxes. Some people see this as a disadvantage, but in reality they have probably already paid into the local property tax system. When renting, property taxes are included in the rent and the landlord pays taxes for the property. An advantage to owning a home is that you may deduct property taxes on your income tax return. Consult with your income tax professional to see if you qualify for the deduction.

As a homeowner you are responsible for making sure your property taxes get paid. Homeowners pay taxes to their local tax office for owning property in the county. Property taxes help fund the operations of local school systems and local government (state, county, city). The amount paid is calculated on the value of the property (the

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higher your property is valued, the more property taxes owed). The assessed value is determined by the local assessor's office. Sometimes homeowners do not agree with the value given to their properties. When this happens, the homeowner has the right to dispute the assessed value. It is very important to know the correct process in your county for doing this. For more information, contact the county assessor or visit the county Web site.

The value given by the assessor is not the same as the property value determined by a certified appraiser for selling purposes. Certified appraisers base the value on the local housing market and the general condition of the home. Frequently the value given by the appraiser may be higher than the value given by the assessor. If the appraised value is lower than the assessed value contact the assessor's office and consider disputing the amount of the assessed value.

Some homeowners may qualify for certain exemptions. In New Mexico these include head of family and veterans exemptions. Each has its own eligibility requirements. Other states may have similar or different exemptions such as homestead exemptions. To find out if you qualify contact your county assessor's office.

Some homeowners have their property taxes and insurance included in the mortgage payment. If your lender requires you to pay taxes and insurance in the mortgage payment, an escrow account will be opened to hold this money until the payments are due. Many people consider this convenient because they do not have to make separate payments. In some cases, however, the lender may give you the option to pay taxes and insurance separately from your mortgage payment. Even if your mortgage company collects the tax payment, you are still ultimately responsible for making sure the property taxes are paid. You can check to see if your mortgage company is making the payment by contacting

the local taxing system. Some taxing entities have the information online. Contact your county or state office for more information. If you live in the state of New Mexico you can call the State of New Mexico Taxation and Revenue Department, Property Tax Division at (505) 827-0870 or visit http://www.state.nm.us/tax/ptd/ptd_hom1a.htm.

Homeowners Insurance

Purchasing homeowners insurance is important to protect your home.. As the homeowner, you are responsible for keeping your insurance coverage low and up-to-date. Proper home maintenance will help you avoid claims and keep your insurance rates down.

Keeping cost down

Insurance does not pay for routine maintenance or damage resulting from neglect. The cost for proper care should be included in your overall budget. It is your responsibility to be the risk manager for your home. There are things you can do to reduce the chance your home will experience water damage, fire or other insured losses. If you do experience an insurable loss you should consider all your options. It may benefit you to make the repairs yourself versus making a claim on your homeowners insurance policy. When you make a claim it is documented on your Comprehensive Loss Underwriting Exchange (CLUE) report. Your CLUE report is like your credit report. The difference is your CLUE report tracks your home insurance claim history. If your CLUE report lists frequent claims, you may be charged higher premiums on future homeowners insurance policies, and it could cause your current rates to increase. Even worse, a poor CLUE report may disqualify you from obtaining future coverage.

The CLUE report also stays with the history of the property. If you plan to sell your house, a claim history on your CLUE report may cause the

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new homeowner to be charged higher insurance premiums. This could make your property less attractive to homebuyers. If you take care of your home and make appropriate repairs and improvements, your CLUE report should not be a problem.

Be sure to keep your homeowners insurance up-to-date. Let your insurer know about alterations, additions and improvements to your home to maximize your insurance dollars by not being either under- or over-insured.

Consider shopping around for rates when your insurance policy comes up for renewal. Just because an insurance company offered you a competitive rate when you purchased your property that may change when you renew the policy. Consider the option of combining your car, life and home insurance with one company which may qualify you for discounts. Use the Homeowners Insurance Comparison Work Sheet provided and shop around to try to save money.

How to file a homeowners claim

If someone has become injured on your property or if a violent storm destroys your home, you will need to file a claim with your insurance company. Remember, a homeowners policy is a contract between you and your insurance company. There are rules and procedures that you and your insurer must follow. Read your insurance policy to determine your responsibilities.

1) Report any crime to the police.

If you are the victim of a theft or your home has been vandalized, report it to the police. Get a police report and the names of law enforcement personnel with whom you speak.

2) Phone your agent or company immediately.

Insurance policies place a time limit on filing claims. Find out the time limit. Ask questions: Am I covered? Does my claim exceed my deductible? (Your deductible is the amount of

loss you agree to pay when you buy a policy.) How long will it take to process my claim? Will I need to obtain estimates for repairs to structural damage?

3) Make temporary repairs.

Take reasonable steps to protect your property from further damage. Save receipts for what you spend and submit them to your insurance company for reimbursement.

4) Prepare a list of lost or damaged articles.

You will need to substantiate your loss. Avoid throwing out damaged items until the adjuster has visited your home. Consider photographing or videotaping the damage. Prepare a home inventory. Make a copy for your adjuster and supply copies of receipts from damaged items.

5) If you need to relocate, keep your receipts.

If your home is severely damaged and you need to find other accommodations while repairs are being made, keep records of all additional expenses incurred. Most homeowners insurance policies provide coverage for loss of use of your home.

6) Get claim forms.

Once your insurance company has been notified of your claim, the company is required to send the necessary claim forms to you by the end of a specified time period. (The time period varies from state to state.) Return the properly filled out forms as soon as possible to avoid delays.

7) Have an adjuster inspect the damage to your home.

Your insurance company will probably arrange for the adjuster to come and inspect your home.

Once you and your insurance company agree on the terms of your settlement, state laws require that you be paid promptly. If you have any questions about the claim filing laws or need to file a complaint in New Mexico contact:

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NEW MEXICO - DEPARTMENT OF
INSURANCE
P.E.R.A. Building, 1120 Paseo de Peralta, PO Box
1269
Santa Fe, NM 87504-1269
phone: 505-827-4601
fax: 505-827-4734
[www.nmprc.state.nm.us/consumers/crdinsurance.
htm](http://www.nmprc.state.nm.us/consumers/crdinsurance.htm)

If you live in another state you can contact your
state department of insurance.

Mortgage Insurance (MI)

Mortgage insurance (MI) protects the mortgage
holder if the borrower defaults on the loan. This
insurance is usually required for government
secured loans (FHA, VA loans) or loans in which
the amount financed is more than 80 percent of
the property value. On conventional loans once
the balance on your mortgage loan is less than
80 percent of the property value, contact your
mortgage company to remove this extra fee.

*This resource is one in a series on **Being a Responsible Homeowner** which include:*

Getting to Know Your New Home

Maintenance Repairs, Home Improvements
Universal Design for Easy Living
When and How to Hire a Professional

Financial Issues for Responsible Homeowner

Financial Responsibilities
Predatory Lending

Managing Financial Difficulties

Foreclosure

Legal Responsibilities

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