

Using a Home Equity Loan - Benefits and Dangers

A home equity loan can be a beneficial instrument used by homeowners to help pay for certain expenses such as home improvements, college tuition loans, etc. There are several items you should weigh before deciding that this type of loan is your best financial option. Let's take a look at some of the benefits and dangers involved in making this decision.

Benefits

1. A primary benefit of using your home equity is the lower interest rates you'll be able to get. Since you are borrowing off of the equity you've secured, banks will generally charge a lower rate than they will for other unsecured loans. This is advantageous because it greatly reduces your overall cost in the long-term.
2. A home equity loan is generally much easier to get than many other types of loans. There is little chance you will be denied this type of loan if you've built up the necessary collateral over time. Your accumulated collateral makes it much easier for banks to approve you for the loan.
3. A benefit which reduces overall cost even further is the tax deductibility of this type of loan. Most other loans, such as personal loans and car loans are not tax deductible. When you file your federal tax return, you'll be able to claim a deduction based around the amount you paid in interest. This is another great tool to minimize the cost of borrowing.
4. Another great feature of home equity loans is that you may usually borrow up to 80% of the equity you have accumulated in your home. In other words, if you owe \$50,000 on a home valued at \$100,000, your equity would be \$50,000 and you could borrow a maximum of 80% of that, or \$40,000.

Dangers

1. One disadvantage to consider is placing your home at risk. Your home is the collateral for this type of loan. If hard financial times come and you end up defaulting on your payments, the bank has a right to demand your property as payment. At least with other types of unsecured loans your house is not at stake.
2. If your property devalues, your loan amount does not change. Real estate markets can vary depending upon economic conditions and whether the housing market is in boom or bust. If conditions worsen and your property value diminishes, you will still owe the initial amount you borrowed.
3. You can be lulled into a false sense of security by taking out too large of a loan. Keep in mind that you still have to pay back every penny of this loan, no matter how easy it is to obtain and how many low interest rate and tax advantages it holds. You'll want to treat this like any

other form of debt you may possess and pay it back as soon as possible to avoid unnecessary penalties, or future balloon payments.

Weigh carefully your decision to use a home equity loan based on your particular financial situation. The above pros and cons should help inform you in making a wise financial borrowing decision.

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