

Debt Consolidation: Using your home equity to get out of debt.

by Dave Muti

Would you pay 16% or more for your mortgage? Of course not! If you carry credit card debt you are probably paying at least this much and your payments are not tax deductible.

The holiday season is over and we as a society spent record amounts again on gifts for friends and relatives who really did not need them with money that we really didn't have. Worse, you just received your first of several credit card statements. You quickly realize that you spent more than you had planned and you can't pay off your bills in one payment. So you plan to systematically pay off all of the holiday gifts by summer. Well that is the good intention of many consumers and that is why bankruptcies and foreclosures are reaching new highs.

The average person is living paycheck to paycheck and suddenly life gets in the way. You need new tires, the refrigerator is on the fritz, the hot water heater blows or one of your children needs braces. This causes you to miss a mortgage payment. As a result your credit score goes down and the interest rate on your credit cards go up. This in turn increases your minimum payment and you can see how many people can get into trouble. Even if you are able to make the minimum payments you will never be able to get ahead and you will end up paying often 2 to 5 times the cost of the item over time than if you simply paid in cash or paid off the credit card in full when you received your first statement.



Each month you have three major spending categories; your mortgage, your credit card bills and your retirement accounts. One will get squeezed out and can you guess which one it is? Many books and articles have been written that detail if you carry debts other than your mortgage you will never be able to get ahead. Carrying debt prevents you from saving. You will struggle all year to get your credit cards paid off and then the holidays hit again and the cycle starts all over. If you own a home you may have another choice. Maybe it makes sense for you to tap the equity that has built up over the years to consolidate your debts into one payment? This approach will

often reduce your monthly obligations while possibly increasing your tax deductions. A strategic refinance to consolidate your debts can also free up cash to actually invest towards your retirement. Now you might be thinking you are simply borrowing from Peter to pay Paul and that you are actually extending the overall cost of the credit card debt. But are you really? Here is an example of a recent client in her 50's (we will call her Mary) we helped out of this exact situation.

Mary and her husband had run up some significant debt on several credit cards and they were recommended to us by their accountant. Like many of us life had gotten in the way and over the

years they amassed \$35,000 in credit card debt in addition to 3 mortgages. They had no retirement savings. As you can imagine the minimum payments were killing them as the average interest rate was 23% on their cards. We were able to structure a program that reduced their overall monthly payments by \$1,260, that's over \$15,000 per year. The client now has positive cash every month. We then set up a methodical contribution plan with a financial planner using half of the monthly savings for their retirement planning. The other half of the savings is going into an emergency fund to pay for sudden expenses that come up in life. They are able to enjoy life again knowing they are not drowning in debt and that their retirement planning is now on track to attain their goals.

In the above situation we did increase the size of their mortgage and yes we also increased the time frame for them to pay it off. But the positives are that they now have a mortgage plan that enables them to save for both short and long term goals. If they had not taken this approach they would have continued to struggle and most likely would have never gotten out of debt. They would not have been able to create the retirement funds nor would they have been able to meet their monthly obligations. As pointed out above, not being able to meet monthly obligations causes good people to lose their homes. If you are in a situation similar to Mary or even if you do not have a good mortgage plan perhaps a new year's resolution would be to sit down with a mortgage planner to design a solution that is right for your circumstances.

If you are in the market to purchase a new home or refinance your existing loan make sure the person you are dealing with is able to provide you with a reason why you should or should not be in the program they are recommending to you. They should be able to offer you several options and a mortgage plan to accomplish your financial goals. Don't let them just push a mortgage on you. Take the time to research, read and then sit down to discuss different options available with a qualified Mortgage Planner to make sure you are in the right program for YOUR circumstances.



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