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## Some advisers say homeowners should get equity out of their homes while they can

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By Tim Grant, Pittsburgh Post-Gazette



Daniel Marsula/Post-Gazette

As housing prices drop in some areas of the country and economists predict that we have not seen the worst of it, some financial planners are urging clients to pull the equity out of their homes while they still can.

"When done correctly, it is not only a way to preserve net worth you already have, but also build wealth," said Dave Muti, author of "Mortgages: What You Need To Know," and a senior planner at Millennium Home Mortgage in Parsippany, N.J.

"When you lose your job if you need money where will it come from? You can no longer get a mortgage because mortgages are based on proof of your ability to pay it back," he said. "If you have the equity pulled out and growing in a side account, you could use part of that to pay the mortgage."

Conventional wisdom would suggest that a debt-free home is the true path to financial freedom, but another school of thought promoted by some financial experts is this: It's risky and bad planning for people to have too much of their net worth invested in their primary residence.

They say the same homeowner that would be inclined to hold 75 percent or more of their net worth in one piece of real estate -- their home -- would probably cringe at the idea of having 75 percent of their total stock portfolio in one single stock.

"Falling home prices are one of the reasons people should look at this option more urgently. Loss of jobs is also a factor," said William Jordan, president of the Sentinel Group in Laguna Hills, Calif.

"In the house, the equity has no rate of return," he said. "Once you take it out, you can have a positive rate of return. For most clients, the only downside is when they die, they'll leave a smaller estate for their children."

The Federal Reserve recently reported that the amount of equity Americans have in their homes fell below 50 percent for the first time since the Fed started tracking the data in 1945.

Home equity has steadily decreased even as home prices increased earlier this decade due to creative mortgage financing, home equity loans and lines of credit. Houses also have become a substitute credit card as homeowners borrow their equity to finance a higher standard of living.

Paul Brahim, executive vice president of BPU Investment Management, Downtown, is among the financial advisers who do not recommend people use the risky strategy of leveraging their homes to invest in financial markets.

"People given a choice would like to know when it rains they'll stay dry," Mr. Brahim said. "That's what a house does. It's where you live. Should I take equity out of my house because values are down? That's like selling a stock when the market is in decline. It's a bad idea."

"Ask yourself about the transaction. Is it something a prudent person would do with his or her own money? The tendency is to look only at returns, and not enough respect is given to risk. The job of an adviser is to balance risk and reward. That's what prudent people do."

Craig Venezia, author of "Buying a Second Home: Income, Getaway or Retirement," said the only time homeowners truly get equity out of their homes is when they sell. And the only thing home equity loans will do is put them deeper in debt, he said.

"That is a financial version of Russian Roulette," Mr. Venezia said. "To borrow money hoping to make more in interest is playing a very dangerous game, and I'd be skeptical of that advice."

"If the stock market is going down, where do you invest the money you take out? The first rule of investing is never do so with borrowed funds. You use savings."

The downfall of using a home equity loan to invest in the financial markets is that homeowners will pay interest on money used for speculation. If the investments decline when homeowners need to liquidate, they will end up losing even more.

Mr. Brahim said the only way the strategy would make sense would be if the home equity loan were used to buy rental property. The problem is, "financial planners have tried to [transfer] that model to homeowners who are paying their own mortgages without the benefit of tenants doing it for them."

Many homeowners are relying on rising real estate values to help fund their retirement, but the stark reality is that many of them have saved so little that they may need to tap into their home equity for big-ticket buying, emergencies and investment capital.

Advisers who advocate using home equity for investments say that one of the benefits is that the interest homeowners pay on the loans is simple interest, while the interest they earn is compound interest.

"Even if the interest rate is the same on both [the loan and the investment], you also get tax breaks, which is the cherry on top of the whole pie," Mr. Muti said.

Peter Miralles, president of Atlanta Wealth Consultants in Atlanta, said Americans have been erroneously sold on the idea that their home is their investment when it really should be viewed as their place to live.

It doesn't produce income, he said, and it actually costs homeowners about 2.5 percent of its value each year in taxes and upkeep.

"When someone retires at age 65, do they really want to have a mortgage or a paid-for house?" Mr. Miralles asked. "Most Americans need to think about being unemployed one year and living off unemployment insurance. Now picture doing that for 30 years. We call that Social Security."

But decisions about money matters rarely are black and white.

Whether using home equity for investment gain is a good idea depends on someone's "money type," said Brent Kessel, author of "It's Not About the Money: Unlock Your Money Type to Achieve Spiritual and Financial Abundance."

His book defines the eight major personalities that people have in relation to their money. He says that before people know if this strategy is good for them, they need to know their money type.

"If someone has been a chronic overspender, it's a bad idea," Mr. Kessel said. "They will increase their mortgage payment and won't necessarily be disciplined about saving or investing those proceeds from the home-equity loan."

"If alternatively, they have been strong savers and investors, then taking advantage of today's historically low interest rates is a great strategy. It's all based on their relationship to money and their historical use of it."

There's nothing wrong with a home-equity loan or line of credit as long as the homeowner can manage the payments if things go against them, says Sanford Kahn author of "The Thirteen Great Economic/Business Myths That Dominate Our Lives."

But he thinks it's a rash idea and cautions people against thinking they can pull equity out of their homes and walk away from the loan by filing for bankruptcy.

"It's not a non-recourse loan," Mr. Kahn said. "If you go to bankruptcy, you'll still be liable for it. It's gambling and I don't see the wisdom in this. No matter what, this will be on their credit record and will hurt their score."

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