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FINANCIAL PLANNING PERSPECTIVES

If Rates Are Heading Up, Should You Refinance Now?

As the economy recovers, homeowners are faced with the good news/bad news prospect of a better real estate market with the likelihood of higher mortgage interest rates. For many, that leaves three choices – sell, refinance or sit tight with the mortgage they have now.

Despite the average 30-year mortgage rate that stood at 4.8 percent in late December, the decision to refinance isn't always a great idea. In fact, it should be considered as part of an overall financial plan that is as individual as you are.

It makes sense to confer with financial and tax experts before you make such a move because there are more questions to consider beyond "How do I get that low rate!" Among them:

What are your current financial goals? If you're planning to stay in your home for the next 20 years, your outlook is far different than someone who wants to retire and move in the next five. Many people focus on paying off their mortgage instead of planning for retirement or education savings for their children. It's important to get advice on this question that fits your overall lifestyle and financial needs. The important question is when you'll get to breakeven on the cost of the refinance – generally 3 to 6 percent of the total loan amount. If your breakeven is at 12 months and you plan to stay in the home five years or longer, it will probably be worth doing.

What's your current debt load? If you're swimming in debt, don't expect to get the lowest, most attractive rate available on the market. While the credit crunch is loosening, many mortgage lenders are being quite picky about whom they'll offer their most affordable loans to and many are still turning away borrowers in significant trouble. It's best to try and cut your level of credit card and other consumer debt before applying for any loan.

When was the last time you checked your credit reports and credit score? You have the right to get all three of your credit reports – from Experian, TransUnion and Equifax – once a year for free. You can do so by ordering them at http://www.annualcreditreport.com/. Yet don't order all three at the same time. By staggering receipt of each of your credit reports at different points in the year, you'll get a continuous picture of how your credit picture looks. Also, you'll have the opportunity to focus on possible errors in a single report, which will give the other two credit agencies time to update their files.

Consider biweekly payments on your current loan… Your current lender might have sent you an offer for a biweekly mortgage loan program that will save you considerable money over the life of that loan. Discard their offer – many lenders make big fees off these programs – and see if you can do it yourself. Some lenders won't allow it, but see if you can break up your payments in a way that will equally divide the principal and interest payments so you're whole by the end of the month. Otherwise, they might apply the first half-payment to principal and still insist on the full monthly payment by the due date.

…or consider adding a 13th payment for the year: Either by adding the equivalent of 1/12th of what you typically pay per month to principal or simply double-paying your mortgage one month a year when you're flush, you'll pay your loan off faster.

Fixed or variable? Given the recent uncertainty in the mortgage market and the current loan environment, it makes sense to try and go for a fixed rate since rates remain at historic lows. Higher rates mean higher payments if rates go higher.

Second mortgages can be problematic: As many lenders have gotten stricter about doing business, they may not be as willing to take second-fiddle status behind an older second mortgage, which happens in a refinancing process if not addressed. If the borrower can't roll the two loans into a single loan during the refinancing process, it may delay or kill the deal based on what the two lenders are willing to do.

Are you on top of your tax issues? Remember that lenders are looking as broadly as they can these days for signs of financial trouble. If you have any late payments of current property taxes or any other potential disputes with state or federal tax authorities, those issues can complicate matters. Make sure you're current.

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