Home Equity Loans, Lines of Credit, and Reverse Mortgages

What it is: Home Equity Loans and Home Equity Lines of Credit (HELOC) and Reverse Mortgages allow you to borrow against your home equity.

- A home equity loan is for a fixed amount of money that is secured by your home. The lender also takes into account your income, credit history, and the market value of your home.
- A HELOC is a revolving line of credit much like a credit card and the lender takes into account your income, credit history, and the market value of your home.
- A reverse mortgage is available to those 62 years or older and allows you to convert your home equity into cash.

How it works: Your home equity is determined by the market value of your home minus any mortgages and liens. For example if your house is appraised at $150,000 and your mortgage (and any other outstanding lien) amount is $75,000 then you have $75,000 of equity in your home.

A home equity loan is a lump sum distribution that is repaid with monthly payments and usually no more than 85% of your **equity** in your home. So in the example above you could borrow 85% of $75,000, or $63,750. A HELOC is a little different; instead of taking one lump sum it allows you to borrow for a specified period of time known as a "draw period", usually 3-7 years. During that time you must make monthly minimum payments and when the draw period ends you will no longer be able to borrow money from the account. A reverse mortgage is a home loan that provides cash payments based on home equity. Homeowners normally defer payment of the loan until they die, sell, or move out of the home.

Why it matters: Pay close attention to fees, including the application or loan processing fee, origination or underwriting fee, lender or funding fee, appraisal fee, document preparation and recording fees, broker fees, and balloon payments. Always ask for annual percentage rate (APR) and compare loans from several lenders.

Who should care: Home equity loans, HELOCS, and reverse mortgages are complicated financial instruments and could put your home and equity at risk. If you miss payments the lender could foreclose on your home to recoup their costs and you could lose your home. It is important to work with a reputable lender that you know and trust.

For more information

- AARP.org
- Consumer Financial Protection Bureau at www.consumerfinance.gov, “What You Should Know About Home Equity Lines of Credit.”, consumerfinance.gov/f/201401_cfpb_booklet_heloc.pdf.
- Federal Trade Commission at www.FTC.gov
- Iowa State University Extension and Outreach website at www.extension.iastate.edu/humansciences/