INVESTOR TOOLKIT

5 things you need to know before taking out a home equity loan

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Beth Braverman, special to CNBC.com

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KEY POINTS

- TransUnion expects 1.6 million home equity line-of-credit originations this year, double the number seen in 2013.
- It's getting easier to qualify for a HELOC, but remember that tax laws have changed — so pay attention.
- Shop around, and remember that there are real risks to borrowing against your home.

As house prices continue to rise, home equity is becoming a more attractive — and more accessible — source of cash for millions of Americans.

One in four homeowners with a mortgage is now considered "equity rich," meaning that their outstanding mortgage balance is worth less than 50 percent of their home value.

An ad for a home equity line of credit at a Citibank branch in New York
Scott Mlyn | CNBC

"Whether you stuck it out through the crisis or you bought in the last five years, many homeowners are sitting pretty when it comes to home equity," said Daren Blomquist, senior vice president of communications at Attom Data Solutions. "It's a good time to leverage that."

Borrowing against home equity can be a convenient way to access cash, but it also carries risk, as millions of Americans learned in the housing crisis of 2008. If you're considering it, here's what you need to know.

1. It's getting (slightly) easier to qualify. Since clamping down on credit after the housing bust, lenders are starting to loosen up. More than 10 percent of large banks eased their credit standards somewhat for HELOCs in the first quarter. Still, you'll need to prove you've got the credit and income to pay off the loan.

some banks are letting consumers borrow 85 percent or more.

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2. The tax rules have changed. Under the new tax law, the home equity interest is only tax-deductible if you're using the money for home renovations on the property tied to the loan. The total amount of home equity debt (including your mortgage) that qualifies for the deduction can't total more than $750,000.

It may still make sense for you to use a HELOC for other purposes, such as debt consolidation or college tuition, but there's no longer a tax benefit to doing so.

3. You'll need to shop around. Get a quote from your current lender, as well as from at least two others, including a credit union and an online bank. Use those quotes to negotiate to make sure that you're getting the best deal. "You can find fairly wide variances in price, interest rates, accessibility and terms from place to place across town," said Keith Gumbinger, vice president at mortgage site HSH.com.

The typical HELOC has a 10-year draw period in which you can take out money as you need it, paying interest only on the money you use. At the end of the draw period, you'll have a 10-year repayment period on the outstanding principle. Since more HELOCs are variable-rate loans, you'll want to know the current interest rate as well as the lifetime cap — the maximum possible rate you'll pay if interest rates go up.

4. There are real risks involved. If you're unable to make payments, your lender could foreclose. While interest rates are relatively low now, they're on the rise. If you have a variable-rate loan, your monthly payment amount will go up along with interest rates. It could be significantly higher in 10 years when you must start repaying the principle. Minimize the impact of the rate increase on your budget by paying off principle before the rate resets.

Also, while home prices have been on a tear in recent years, there's no guarantee they'll continue to rise. If the housing market falters and the value of your home declines, you could end up underwater, owing more than your home is worth. The more equity you keep in your home, the more protected you are against market fluctuations.

"You need to take into consideration that it's possible home values could drop," said Nancy Seely-Butler, a certified financial planner with Ameriprise Financial. "A lot of times people think too short term.

"You need to think about how it's going to help you today, but also what it's going to look like in five or 10 years."

5. A HELOC isn't the only way to tap your home equity. While less common than HELOCs, home equity loans are another way of borrowing against the value of your home. Also known as "second mortgages," home equity loans typically allow you to take

Another option is a cash-out refinance. This may make sense if the interest rate you're paying on your mortgage now is higher than current rates, but refinancing often carries higher fees and a more complicated application process than getting a HELOC.

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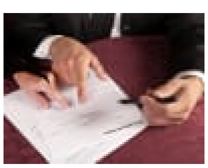

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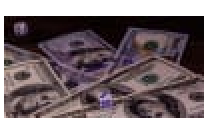

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