



Should You Use Your Home Equity for Tuition?

If you have a son or daughter about to start college, you may be wondering how in the world you are going to pay for it. After all, tuition prices have been rising about 10% each year for the past several years, while inflation and incomes have only been growing at about 3% per year. College is expensive, no doubt about it. So if you haven't been saving up for this big event, what is the best way to finance the costs? Many people are turning to their home equity for help. Is this really a good idea? Take a look at the pros and cons of using a home equity loan to pay for your child's college expenses.

The Pros

A home equity loan is a loan in addition to your original mortgage that allows you to borrow a certain amount of money based on how much equity you currently have in your home. (Equity is the difference between what your home is worth and how much you still owe on your mortgage.) You can do this with a fixed rate home equity mortgage or with an adjustable rate home equity line of credit. Currently you can get the fixed rate type with an interest rate of about 7.5%, while your original rate on an adjustable rate home equity credit line will be roughly 6%.

The advantage of taking out a home equity loan to pay for college tuition is that rates on these loans are typically much lower than you can get on other types of loans. They are certainly lower than the rates you would pay for charging that tuition to a credit card.

Another advantage is that the interest on your home equity loan is deductible. While this certainly is more helpful to those in higher tax brackets, it provides nice financial assistance to those in lower tax brackets.

Using a home equity loan is also a good strategy if your other option is to dip into your retirement funds in order to pay for college. This should usually be your means of last resort, especially as sending a child to college generally means you have less than 20 years until you reach retirement age.

The Cons

There may be some situations where using your home as collateral may not be the soundest way to finance your child's tuition. One of the biggest risks you face is that you are putting a greater debt burden on yourself through mortgage loans. If for any reason you are unable to repay this debt, or start missing monthly payments, you could eventually end up defaulting on your loan, ruining your credit, and even lose your house. You should definitely consider this risk before taking on a home equity loan.

You may also find that you can avoid getting a home equity mortgage, by simply helping your child apply for student loans. These often carry low rates as well, even as low as 5% in some cases. These loans do not put your home in danger and a certain portion of the interest is also tax-deductible. Tax rules for 2006 and 2007 stipulate that you can deduct a maximum of \$4,000 for college tuition payments if you are single and making \$65,000 per year or less, or if you are married and have a combined salary of \$130,000 or less. A traditional



student loan may be a better way to go if you can get a low interest rate, especially considering that you will have to pay at least minimal closing cost fees to open a home equity loan.

Your specific financial situation, interest rates, and risks are at the heart of this matter. Using a home equity mortgage may or may not be the best choice for you. Be sure to consult your financial advisor or a trusted mortgage professional to figure out it is makes sense for your tuition financing needs.