

Your Real Estate Advisor



Should you prepay the mortgage principal?

There are two faces to the answer of this question, just like for most answers. So, to obtain the correct advise for your situation, some additional considerations must be evaluated.

There is one school of thought that interest and property taxes on a person's home are one of the few income tax deductions still available and a taxpayer needs as many deductions as possible.

A deduction does not reduce taxes dollar for dollar but simply by the marginal tax rate of the taxpayer. For instance, if you had a \$10,000 deduction and were in the 20% tax bracket, it would save you \$2,000 in taxes. The net effect is that you still spent \$8,000. The question is: did you get \$8,000 worth of economic benefit?

As an example, let's say you have a mortgage at 6% interest. You have an extra \$100 per month available and want to put it where it will do the most good.

If you put it in a savings account, it may only earn 3%. If you make an additional \$100 principal payment on your 6% mortgage, you will have a 3% net gain without any tax considerations. Regardless of what tax bracket you are in, you will save money in this example.

The answer to the original question is determined by asking if you can earn more in an alternative investment than the rate being charged on your mortgage. Maybe paying off a personal loan at 14.95%, or a credit card at 9.95% is a better investment than the 6% mortgage pre-payment. If not, then in most cases, you will be better off pre-paying your mortgage.

There is one other consideration that should be made. If you will need the money in the near future, the equity in the home may not allow the liquidity needed. Today many financial institutions make it very easy to have a home equity loan but economic conditions can always change, which may make it difficult to get at the equity.

De La Guardia Group combines many years' experience, a thorough understanding of the real estate market, and cutting-edge technology to provide buyers and sellers with competent advice and proven results.

