unsecured debts such as credit cards, remember that this will put the home at risk for not just the mortgage debt but also the unsecured debt. In addition, many refinancings have teaser rates that increase after a year or two. What may look affordable then becomes unaffordable. Some refinancing loans start the homeowner off with an artificially low monthly payment that may not even pay the interest on the loan. When the monthly payment increases after the initial period, the payment shock can be severe. These types of mortgage loans are discussed in more detail in Chapter 3, above.

Thirteen Refinancing Rules for Homeowners

1. **When in doubt, do not refinance or consolidate debts.** Refinancing deals almost always come with significant costs. These costs will usually just make matters worse in the long term.
2. **Do not let debt collectors pressure you into refinancing.** Debt collectors may try to scare you into refinancing because they have no other way to get their money. Better ways to address debt collection problems are discussed at the end of this chapter and in the NCLC Guide to Surviving Debt.
3. **Never (or almost never) refinance unsecured debt into secured debt.** Unsecured debt, such as medical bills and most credit card debt, should be lower priority for a homeowner than paying the mortgage. But if unsecured debt is refinanced into a mortgage loan, you face loss of your home if you continue to have financial problems. Do not refinance unsecured debt—that is, most credit card debt—into secured debt even if this allows you to lower the interest rate you are paying. The interest rate on a mortgage loan may be lower, but these are usually at least twenty- and, more commonly, thirty-year loans. Paying at a lower rate for such a long time will almost always cost you more than a higher rate on a shorter-term loan. Think of it this way: Would you ever want to pay off the pizza you bought for dinner with a credit card by stretching the payments out for thirty years? This is the result of adding your credit card debt to a mortgage loan.
4. **If you have an existing debt with a finance company or high-rate second mortgage lender, do not refinance that debt with the same lender.** Ask the company to agree to lower payments on the existing loan, but do not allow the lender to refinance that loan, which may involve new closing costs and perhaps even a higher interest rate.
5. **Do not turn your car loan into a second mortgage unless you would rather lose your home than your car.** If you are in danger of losing your car, you may be tempted to pay off your car loan by taking out a second mortgage on your home. You may save your car temporarily this way, but you are putting your home in danger. Although repossession is bad, foreclosure is worse. This type of refinancing adds the car loan into the mortgage loan, turning a five-year car loan into a thirty-year mortgage. This greatly increases the amount of interest you pay.
6. **Do not refinance low-interest debts with higher-interest loans.** You should always evaluate the interest rate on the new debt and look for a lower rate than on the old debts. You have already paid certain fees in the old loan, and you must make sure that a new lower rate is actually lower after both the old and new fees are accounted for. Furthermore, the APR (Annual Percentage Rate) of the new loan must be lower than the interest rate stated in the note of the old loan, or you will be losing money. The APR is the cost of credit as a yearly rate. It is often higher than the interest rate on your

promissory note because the APR takes into account both the interest plus certain fees that the lenders add to the cost of the loan.

The interest rate is not the only consideration when evaluating a loan. Other fees, charges, and expenses which are not considered interest may turn a loan which looks cheaper into one which is actually more expensive.

7. **Do not include your long-term first mortgage in a refinancing package.** Do not let potential lenders pay off your first mortgage and give you a new mortgage equal to the first mortgage plus the new loan amount. The only exception is if the new mortgage is for the equivalent length of time and the APR is significantly *lower* than the interest rate on the old first mortgage—to offset prepayment penalties and fees and charges.
8. **Be careful about variable rates.** Variable-rate refinancing loans can be tricky. In any variable-rate transaction, the monthly payment can increase drastically when you can least afford it. Some loans have artificially low rates (and payments) during the first months or years, called "teaser rates." Other variable-rate loans provide that the rate will only go up, never down.
9. **Do not refinance a debt if you have valid legal reasons not to pay it.** If you have a legal defense to repayment of a debt, such as lender fraud, you can raise that defense in court. If you refinance with a new lender, the defense may not be available against the new creditor. If you need legal help to determine if you have a defense, you should get that help *before* entering the refinancing deal.
10. **Be wary of claims that you will get a tax advantage from a debt consolidation loan.** Many lenders offering bad refinancing deals talk about the benefit of the tax deductibility of mortgage interest. Make sure you understand how your personal tax situation will be affected. For example, if you do not itemize deductions, the tax deductibility of mortgages interest is worthless.
11. **Avoid refinancing deals that are scams.** Refinancing involves great potential for hidden costs, fees, and other unfair loan terms. Even some reputable lenders make unfair refinancing deals. When in doubt, get help in reviewing the loan papers *before* you sign anything. You can walk away from a bad deal even at the last minute. A lender that is unwilling to let you get outside help should not be trusted. Another way to avoid scams is never to let a contractor or salesperson arrange financing for you and be wary of mortgage brokers. Unfortunately, some brokers find you refinancing deals which involve big commissions for them rather than good loans for you.
12. **If your home is collateral in a refinancing deal, remember that you have three days to cancel.** In most refinancings in which you give the lender a mortgage, federal law gives you the right to cancel for any reason for three business days from the date you sign the papers. If you wish to cancel, make sure you do so in writing before the deadline. The lender is required to give you a form for this purpose. You can, but need not, use the cancellation form provided by the lender. You may cancel the loan by sending a signed, dated letter indicating your desire to cancel the refinancing. You should keep a copy of this letter and be sure to send it by registered or certified mail.
13. **If it seems too good to be true, it is not true.**