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Pay Mortgage in Full or Monthly?

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Q: Washington: My mom retired, sold her house and bought a condo. She's debating whether to pay for it in full or pay the mortgage monthly to get the tax benefits. Her income will be interest from investments, Social Security and a pension, for about \$60,000 a year. The average return on her investments is about 5 percent, and the interest on her mortgage is 6 percent. Wouldn't it be better to not have any interest payment rather than getting a bit of it back April 15?

A: Lisa Kirchenbauer, a financial planner in Arlington: At \$60,000 a year, her tax bracket must be rather modest, and so is her tax break from the mortgage. If her investments are really only yielding 5 percent -- that seems a bit conservative -- then it makes more sense to pay cash rather than pay someone else 6 percent. Also, not having a mortgage can be a real emotional relief to more-conservative retirees and their families -- no worry about missing a payment. A reverse mortgage could always be considered later to tap into the property's equity, if needed.

If paying off the mortgage on the condo will leave your mother with enough liquid assets to cover unexpected expenses, such as a car or medical expenses, then pay it off. If her assets aren't that robust, then perhaps making extra principal payments is a better alternative, allowing her save on interest in the long term while keeping the deduction for a little while.

Peg Downey, a financial planner in Silver Spring: While her taxes with both a mortgage and investable income will likely be lower than they would be without a mortgage and some of the investment income, the key additional consideration is the loss she experiences because her assets have been removed from the market. If her investments are increasing in value and also paying a dividend or interest, the total return, less taxes, must be added to the tax benefits of having a mortgage.

Then, how her investments are allocated and the costs of liquidating those investments to pay off the mortgage come into play. Also important is whether she will have adequate liquidity if she ties up her funds in the house. This is the crunch folks run into that leads them to use a reverse mortgage, which also has substantial costs associated with it.

Lastly, there is the emotional question of how it will feel to your mom to move accessible funds into an illiquid investment. While some folks feel safer without any debt, many others feel most secure if they have a lot of assets readily available.

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