Using the Bridge Mortgage

If you anticipate purchasing a second home before the sale of your first, you may require a "bridge loan."

Banks generally will work closely with valued customers in order to provide bridge loans. The loan is handled just like any other extension of credit. Usually, however, the loan is unsecured; neither house is taken as collateral. As a result of the new tax law, the interest on the loan is not tax deductible in 1990. Remember, the new tax law eliminates deductibility of interest on all loans except mortgages (and investment loan expenses applied against investment income).

Banking procedures require that you submit a personal financial statement. If your credit warrants it, the loan can usually be processed in a very short time. Generally, rates are associated with the prime rate, and there may be a small fee for originating the loan. A bridge loan is typically made for 30 to 90 days but may extend up to 6 months in some cases. Interest is often payable when the loan is repaid.

In some cases your bridge loan may cost more than a mortgage loan, take longer to process, and involve more paperwork.

You must be prepared to prove that the proceeds will indeed be used to bridge a home purchase and sale. A real estate broker listing of your property or an actual contract for its sale will suffice as proof. The maximum you can borrow is based on the value of the property itself and your equity in it. The interest on the bridge loan doesn't qualify for a tax deduction unless you can prove that the funds were applied toward the purchase of a new home.

What about a simple home equity loan which you could arrange long before you even find your new home? It's easy and convenient and the interest may be fully deductible. But closing costs are usually higher, and you have to make monthly interest payments immediately.

Some individuals are using loans from brokerage firms based on the value of their stock or bond portfolios. You can usually borrow up to 50% of the market value of your stocks or 93% on government securities. Rates can vary depending on the amount borrowed, and they can fluctuate quickly. You might also be able to borrow up to half the value of any qualified company pension plan, but only up to a maximum of $50,000.

A pension expert points out that most pension plans have non-alienability clauses in them. That means you're actually borrowing the $50,000 from the plan itself not from your own pension. Some companies are more liberal than others on such loans.

Another alternative method of borrowing for a bridge loan is to borrow against the equity in an insurance or annuity policy. This method provides an easy way to raise the capital necessary for a bridge loan and to do it at the lowest possible rates.

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