The Complete Guide to

Getting and Using a Home Equity Line of Credit in Hawaii

Bank of Hawaii

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HELOC

Home Equity Line Of Credit

Owning a home in Hawaii is a major life accomplishment. Not only does it give you a secure place to live and build a family, it can be an effective way to build wealth and improve your personal finances.

For example, once you've built up some equity in your home, you can apply for something called a home equity line of credit (HELOC). This line of credit leverages your home's equity to give you access to funds with an affordable rate and flexible terms. Whether your goals include consolidating debt, making home renovations, financing education expenses or paying for a major life event such as a wedding, a HELOC could be the solution.

Given the advantages, and the current low interest rates, it's no wonder that an increasing number of homeowners are taking out HELOCs. Property research company ATTOM Data Solutions reported that almost 350,000 HELOCs were originated for U.S. residential properties in just one quarter in 2018, up 14 percent compared with the prior year.

The median price of a single-family home on Oahu has risen by $140,000 in the past five years, meaning you may have a lot more equity in your home than you think.

To get a HELOC, you'll need a good credit history and equity in your home. That equity may come from the mortgage payments you've made since buying the property or appreciation in your home's market value. The median price of a single-family home on Oahu has risen by $140,000 in the past five years, meaning you may have a lot more equity in your home than you think.

However, although HELOCs can offer substantial benefits, they also come with some very specific requirements and restrictions, as well as the inherent risk involved with borrowing money. Before you apply for a HELOC, you should think about how you want to use it, read the disclosures so you understand how it works and make sure you're comfortable with the risks. If you plan carefully and take the right steps, a HELOC could give you a big boost toward achieving your goals.

We're here to help! This resource guide will walk you through everything you need to know about HELOCs, from understanding introductory rates to the documents you'll need to apply.

CHAPTER 1

Introduction to HELOCs

What is a HELOC?

A HELOC is a credit line that's secured by your home. It works somewhat like a credit card, in the sense that you can borrow various amounts at different times and, when you've hit your limit, you can repay those amounts and borrow again. Your limit is determined by your lender, based on your income, the amount of equity you have in your home and your creditworthiness.

You can generally borrow up to 85 percent of your home's value, minus the amount you still owe on the mortgage loan. For example, if your property is appraised at $400,000 and you owe $150,000, you would calculate 85 percent of the total value, which comes to $340,000. Then subtract $150,000, giving you a maximum line of credit of $190,000.

Have Questions?
Ready to Apply?

Visit boh.com or call 808-693-2222 to get started.

How You Can Use a HELOC

Since a HELOC is secured by your home, it should be used for purposes that could improve your financial situation or quality of life, such as debt consolidation, home renovations and education expenses.

1

DEBT CONSOLIDATION lets you combine your credit card accounts, personal loans, car loans and other debt into one monthly payment, often at a lower interest rate than you would have otherwise paid. Using a HELOC this way could potentially save you money and help you pay off your debt with one monthly payment instead of managing multiple bills. Be careful not to take on new credit card debt while doing this, as you could end up with an even larger total debt.

2

HOME RENOVATIONS include repairs, like fixing an older roof or replacing a damaged sewer pipe, and major improvements, such as building an addition, remodeling your floor plan, installing new windows, updating your kitchen or bathrooms or adding a backyard deck or a swimming pool. Repairs and improvements can boost the value of your home by quite a bit, making a HELOC a sound investment.

If you use your HELOC to repair or improve your home, you may be able to deduct the interest you pay on your HELOC when you file your income tax returns. Consult a tax advisor to find out the details.

3

If you'd like to **REFINANCE YOUR MORTGAGE**, a HELOC can be a cost-effective way to not only take advantage of low rates but also turn your mortgage into a flexible line of credit. Even though you're taking out a line of credit rather than another closed-end mortgage, you can benefit from many of the same features as a conventional refinance would offer, including:

- Interest rates that are competitive with current mortgage rates.
- Repayment terms that are more convenient for your goals and budget—anywhere from 3, 5 or 7 years up to 15, 20 or 30 years.
- The ability to access cash by applying and qualifying for a HELOC larger than the remaining balance on your mortgage

And, since it's a line of credit, you can also take advantage of all the features that come with this kind of financing. For example, as you start to pay down the balance of your HELOC, you'll gain access to that cash to use for whatever you'd like, at a lower interest rate than you'd likely be able to get with a credit card or unsecured personal loan. With this method, you also may be able to refinance with no application or appraisal fees, and virtually or no closing costs (depending on your line amount, lien position, property type and property location).

4

When it comes to **TUITION LOANS**, there are a few instances in which a HELOC makes sense (if, for example, you're able to pay off the loan while interest rates are still low), but in most cases there will usually be other loan vehicles, including financial aid and structured student loans, that make for better options. Consider using a HELOC for other education expenses, such as books, school supplies, student fees, travel to and from campus and so on. A HELOC may also be a good option to help finance the cost of private elementary and/or high school education.

A HELOC typically shouldn't be used for daily living expenses, such as groceries or utility bills, luxury goods, family vacations, stock market investments or risky business ventures. This is because a HELOC uses your house as collateral, unlike credit cards or other unsecured debt. If you don't repay the loan, the lender can take your house.

Who is a HELOC Right For?

A HELOC might be what you're looking for if the following applies to you:

- ☐ **You have a good credit history.**
- ☐ **You have equity in your home.**
- ☐ **You want to consolidate other debt, make home renovations or you have other financial needs.**
- ☐ **You want the flexibility of a credit line.**

You should also have a good understanding of how a HELOC works.

- ☐ **You're comfortable with the concept of a variable interest rate, and are able to handle potential higher payments in the future.**
- ☐ **You understand that, if you don't repay your HELOC, your lender could foreclose and you could lose your home.**

CHAPTER 2

How HELOCs Work

To get the most out of your HELOC, it's important to understand how it works and what you can expect from it. Let's run through the basics.

Monthly Payments

Depending on where you are in your HELOC's term, your monthly payment may be composed of a mix of interest and principal, or only interest.

PRINCIPAL is the amount of money you have borrowed.

INTEREST is what the lender charges for lending you the money. It is usually disclosed as a percentage rate (daily periodic rate and/or annual percentage rate) for what you borrow.

Some HELOCs feature a final payment called a **BALLOON PAYMENT** because it is usually much larger than a normal monthly payment. It can be tens of thousands of dollars, or more. This balloon payment generally occurs because your HELOC's amortization period is longer than its term, so your monthly payment doesn't pay off your balance even during your repayment period. This structure gives you the flexibility of a smaller monthly payment, but can result in payment shock when the balloon payment is due if you haven't prepared for it.

Draw and Repayment Periods

A HELOC typically features a draw period and a repayment period. The duration of each period varies, depending on the term of your HELOC.

DRAW PERIOD: During your draw period, you can borrow from your HELOC up to your credit limit. Each time you draw funds, you may be able to draw as much or as little as you want or you may be required to draw at least a minimum amount. A minimum initial draw may also be required.

If you repay all or part of your principal during your draw period, your available credit will be replenished and you can draw against it again if you choose to. This flexibility is a key feature of a HELOC.

Draws usually can be made:

- Through online banking
- By phone
- With a HELOC transaction card
- With a line-of-credit check
- By transfer to a checking or savings account

During your draw period, your required monthly payment will most likely be interest-only; however, you can also repay principal during this period if you choose. Paying principal as well as interest during your draw period could help you avoid a large final payment, known as a balloon payment, when your HELOC ends. It can also reduce monthly payments during the repayment period.

REPAYMENT PERIOD: At the end of your draw period, your HELOC enters a repayment period, which may last as long as 10 or 20 years.

During the repayment period, you will no longer be able to withdraw funds and your required monthly payment will increase (if you were making interest-only payments) to repay your balance. Depending on how your monthly payments are structured, you may also have a balloon payment at the end in order to completely repay your balance.

Interest Rates

Most HELOCs start with a low introductory rate for the first 12, 24, 36 or 48 months. You may be offered an introductory rate for one period or a choice of introductory rates with a corresponding time frame. The lowest rate will usually expire the soonest while the highest rate will likely last the longest.

You may get an additional rate discount if you agree to have your monthly HELOC payment withdrawn automatically from your checking account. An **AUTOPAY RATE DISCOUNT** is a great way to save money with your HELOC, and will help ensure that you're making each payment on time.

When your introductory rate ends, your HELOC rate will increase to a fully indexed variable rate that's based on an index, such as the U.S. Prime Rate, plus a margin. The variable rate will fluctuate up and down as market rates change. Whenever your rate changes, your monthly payment will also change.

An **autopay rate discount** is a great way to save money with your HELOC, and will help ensure that you're making each payment on time.

There may be a periodic rate cap that limits the amount of percentage points that your rate can increase during any given adjustment. You may also have a lifetime cap that defines the maximum interest rate that can be applied to your HELOC. You may also have a lifetime cap that defines the maximum interest rate that can be applied to your HELOC, as well as a minimum, or floor rate.

Even after they convert to the variable rate, HELOCs generally feature lower rates than other types of loans, such as credit cards. That's because a HELOC is secured by your home as collateral, reducing the risk to the lender.

The low introductory rates that come with HELOCs can be very enticing, but you should also consider the fully indexed rate that will apply after the introductory rate period ends. Closing costs, fees and balloon payments may also differ, sometimes substantially, from one lender to another. It pays to do some comparison shopping before settling on your lender.

HELOCs generally feature lower rates than other types of loans, such as credit cards. That's because a HELOC is secured by your home as collateral, reducing the risk to the lender.

Fixed-Rate Loan Option

A HELOC fixed-rate loan option allows you to convert all or part of your credit line into a fixed-rate loan. Your monthly payment for this portion of your debt usually will be higher after you convert it because your payment will be composed of both principal and interest instead of only interest.

A fixed-rate loan option may be helpful if you want to lock in a fixed rate and payment for a portion of your HELOC. It could also help you shrink or avoid a balloon payment at the end of your repayment period.

If you convert your entire HELOC to a fixed-rate loan option, you may not be able to draw additional funds. If you convert only a portion of your HELOC, your subsequent draws on the remainder will still be at variable rates.

Your lender may limit how many fixed-rate loan options you can have at one time. The limit, if there is one, is usually three to five.

You may be charged a fee to convert all or part of your HELOC to a fixed-rate loan option.

CHAPTER 3

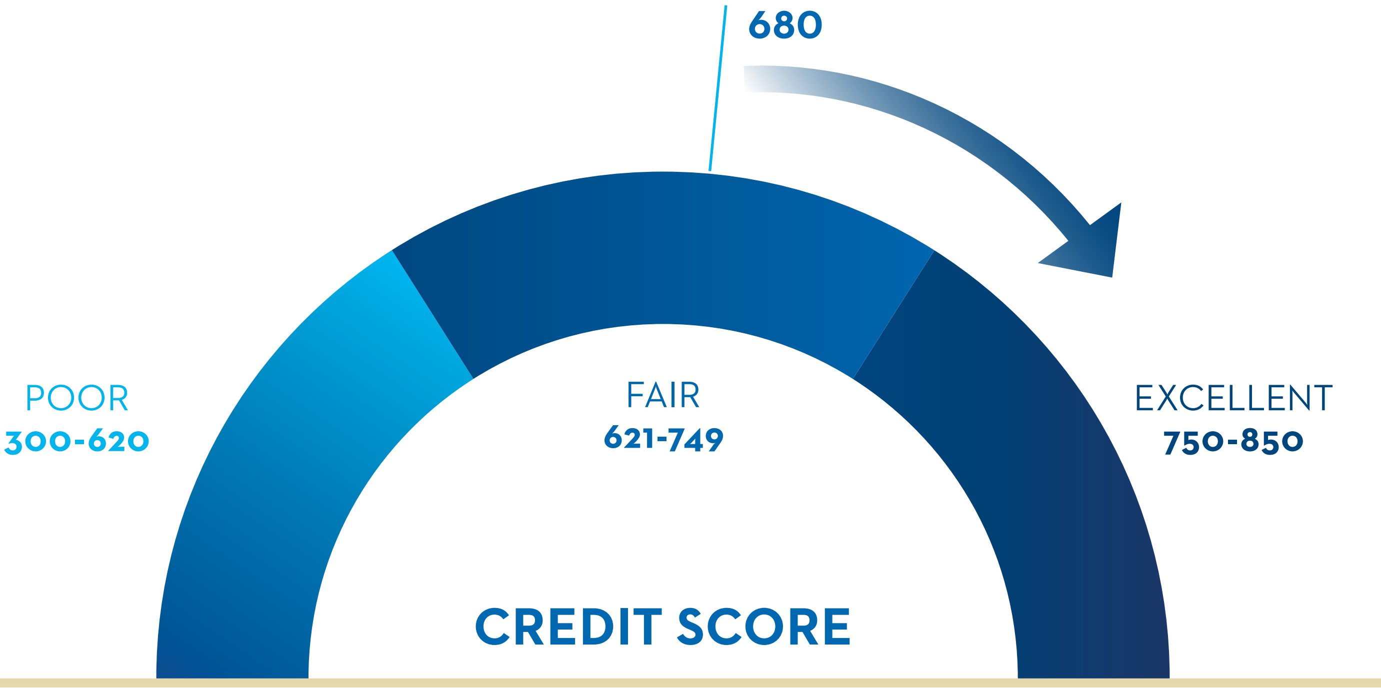
Planning for Your HELOC

To qualify for a HELOC, you'll have to meet the lender's minimum requirements for your credit score, debt-to-income ratio, home value and other factors. You'll also want to plan ahead through the lifespan of your potential HELOC, to make sure you're prepared to use and repay it. Here are the basics you need to know when preparing to apply for a HELOC.

Understanding Your Credit Score

When you apply for a loan, your loan officer typically will pull your credit score to assess your creditworthiness. When it comes to applying for a HELOC, generally speaking, lenders require a score of at least **680 or higher**, although this may vary from lender to lender. If you've got excellent credit, say **750 or higher**, you may qualify for more attractive HELOC interest rates, or possibly higher limits.

If you have a low credit rating, click here for a guide that explains the best ways to raise your score.



Your Debt-to-Income Ratio Explained

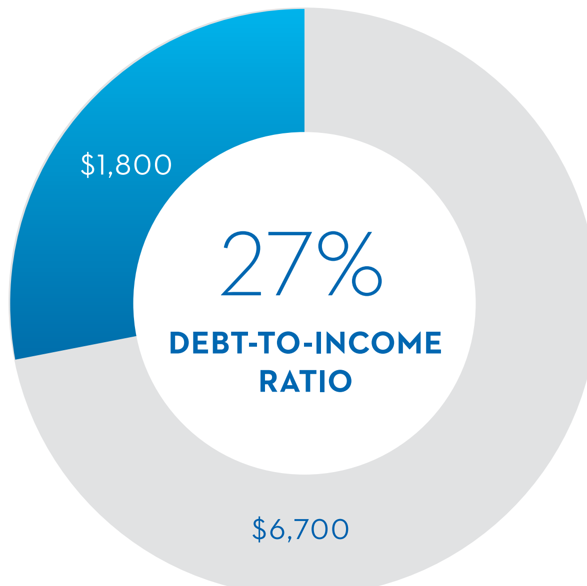
Your debt-to-income ratio (DTI) compares your monthly income to your monthly debt obligation, which includes payments for your mortgage, car loans, student loans, credit cards, personal loans and any other debt you have. Your monthly living expenses, such as groceries, utility bills, gasoline, and cellphone and Internet services, are not usually included in your DTI.

To calculate your DTI, add up your monthly debt payments and divide that total into your monthly pre-tax income. The result will be a percentage.

Here's an example:

DTI CALCULATION

MONTHLY DEBT PAYMENT	**$1,800** ÷
MONTHLY SALARY	**$6,700**



Lenders use different standards to evaluate your DTI, but, generally speaking, if it's higher than 43 percent, you may have to pay off some of your existing debt before you can qualify for a HELOC. Paying off debt with the highest monthly payment first will improve your DTI the fastest, since it's your payment, not the total amount of debt that you have, that counts toward your DTI.

Understanding Your Home's Value

Your **combined loan-to-value ratio** (CLTV) compares the amount you owe for your mortgage and your proposed HELOC credit line to your home's value. Your home's value is important because your home secures your HELOC.

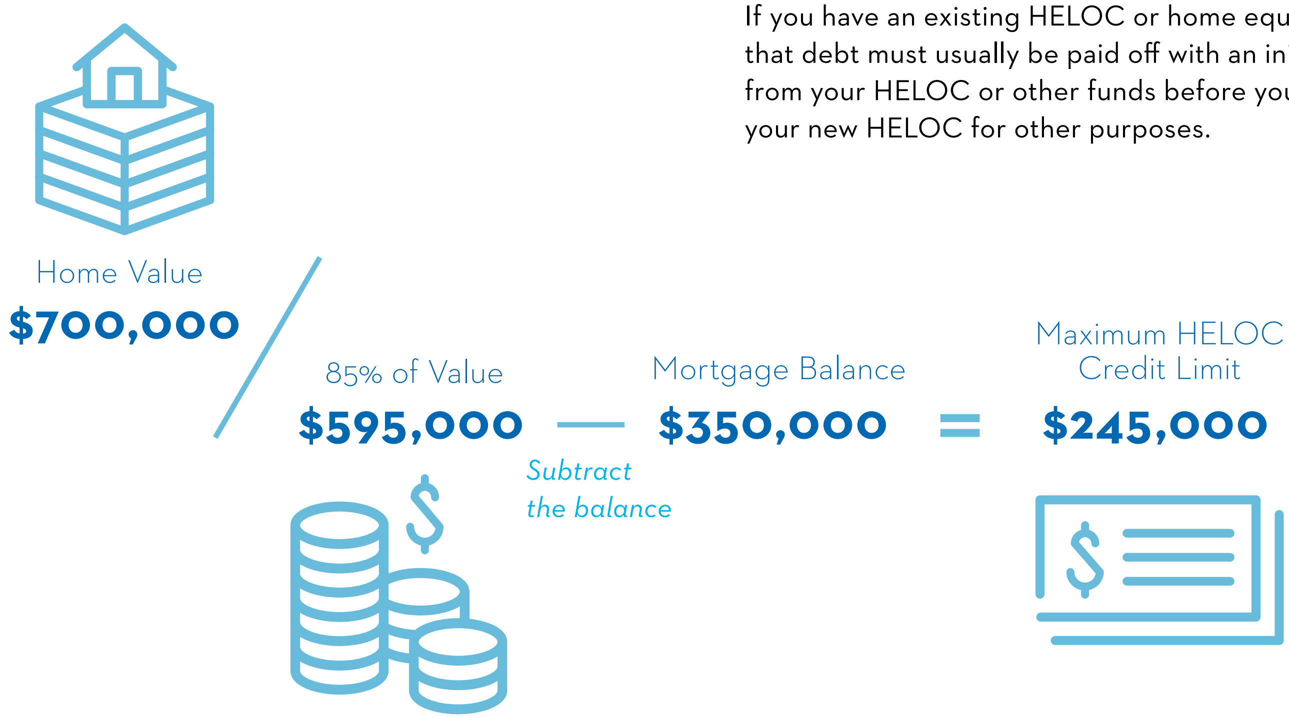
When you apply for a HELOC, your CLTV generally cannot be more than 85 percent of your home's value. That means your mortgage balance, plus your HELOC credit limit, cannot exceed 85 percent of your home's value.

To calculate how much you may be able to borrow with a HELOC, take 85 percent of your home's value and subtract the amount you owe for your mortgage.

For the purposes of calculating CLTV, your home's value isn't the price you paid for it. Some lenders will use the "tax assessed value (TAV)," meaning the value that's listed on your property tax bill. Other lenders will use a market value determined by recent sale prices of nearby homes that are similar to yours and home sales trends in your local area. Your lender may have your home appraised by a professional to determine its value.

Most owner-occupied detached houses and condos can be used to secure a HELOC; however, there may be restrictions on the use of other property types, such as rental homes, condo-tels, agricultural properties and leasehold properties. To obtain a HELOC from Bank of Hawaii, your property must be located in Hawaii or Guam.

If you have an existing HELOC or home equity loan, that debt must usually be paid off with an initial draw from your HELOC or other funds before you can use your new HELOC for other purposes.



If you have an existing HELOC or home equity loan, that debt must usually be paid off with an initial draw from your HELOC or other funds before you can use your new HELOC for other purposes.

Choosing a HELOC that's Right for You

To choose a HELOC that's right for you, think carefully about how you want to use your HELOC, how much you intend to draw, and when and how you'll repay the sums you borrow.

For example, perhaps you'd like to keep your monthly payments as low as possible and make those payments for a longer period of time. Or maybe you'd rather have a longer introductory rate period, or the option to fix the rate with a fixed rate loan option. A loan officer can help you compare your options and choose a HELOC that will work the way you want it to.

One way to compare HELOCs is to look at the current fully indexed variable annual percentage rate (APR), which gives you an example of what the cost of your HELOC may be at the start of your draw period if your introductory rate didn't exist. Since HELOC rates are variable, you might never pay that exact rate, but it's still useful for comparison purposes. The fully indexed variable APR that will apply when your introductory rate ends depends on market rates at that time and other factors.

If a HELOC doesn't fit your needs, you may want to consider other options, such as a home equity loan, a mortgage refinance with cash out or a personal loan.

The fully indexed variable APR that will apply when your introductory rate ends depends on market rates at that time and other factors.

Planning for Rate Increases

Since HELOCs usually feature a variable interest rate, your monthly payment could go up if market rates rise.

To reduce the risk that you won't be able to afford your HELOC at some point down the road, think carefully about how high a limit you want before you apply. Just because you can borrow a certain amount doesn't mean you should. In many cases, a smaller HELOC is more prudent, since it gives you some financial leeway when rates change.

Planning for Repayment

From the first day that you're approved for your HELOC, you should be thinking about the end of your draw period and how you'll handle making the significantly higher payments that kick in during your repayment period. Mark your calendar far in advance and check with your lender periodically so you won't be surprised by higher payments when your repayment period begins.

If you're planning to use a future increase in income, such as a raise, a commission, a bonus or an inheritance, to pay off your HELOC, you should make a contingency plan in case you don't receive that windfall when you expect it.

If you're planning to pay off your HELOC by selling your home, calculate whether your anticipated sale price will be enough to repay your HELOC as well as your mortgage and closing costs.

You may be able to avoid a balloon payment if you make bigger payments during your draw and/or repayment periods. The more principal you pay off early, the more you may be able to shrink or even eliminate your balloon payment.

An online mortgage calculator can help you figure out how much principal you want to pay. Enter your loan amount, rate and term to find out how much you'd need to pay each month to pay off your HELOC by the end of its term and then work backward from there to determine how much you want to pay.

Making larger payments means you won't have the low monthly payment you may have wanted when you got your HELOC, but repaying principal can give you peace of mind that your balloon payment will be smaller or even zero.

The more principal you pay off early, the more you may be able to shrink or even eliminate your balloon payment.

End-of-Draw Options

If you're not comfortable with the higher payments during the repayment period, or cannot pay the large balloon payment at the end of the HELOC, you have several options to consider.

OPTION
1

Talk to your lender

If you believe you won't have the money to make a balloon payment, your first step should be to contact your lender as soon as possible and ask about options. The lender may offer a special promotion to move to a new financial product so they can keep your business, work with you to refinance the outstanding balance or lengthen the term of the loan to provide you enough time to pay it off.

Of course, if you have the cash available, you can pay off your HELOC rather than making the higher payments and possibly a balloon payment as well. You can call your lender and request a payoff quote that will show the exact amount you'll have to pay to close out your HELOC.

OPTION
2

Refinance into a new HELOC

Refinancing into a new HELOC gives you more flexibility to repay your principal because you'll get a fresh draw period with interest-only payments and possibly a new introductory rate for a limited time. You'll also have the ability to draw additional funds.

You'll need good credit and equity in your home to refinance into a new HELOC.

Keep in mind that your new HELOC probably will have a variable rate, so your rate and payment could rise if market rates go up.

If you refinance into a new HELOC with a fixed-rate conversion option, you can convert your existing HELOC balance into a fixed-rate loan and draw any additional remaining funds, up to your new limit. Again, you'll need good credit and equity in your home to make refinancing your HELOC viable.

OPTION
3

Refinance into a home equity loan

Refinancing into a home equity loan, instead of a line of credit, will give you a fixed monthly payment and term with no balloon payment. You'll need good credit to qualify and you won't be able to draw additional funds.

OPTION
4

Refinance into a new mortgage

Rather than make two home payments—one for your mortgage and one for your HELOC—you might prefer to refinance both your mortgage and HELOC into a new mortgage. If you refinance with a 15-year term, you'll probably have a higher payment than you would with a 30-year term, but you'll pay off your mortgage sooner and may reduce your interest expense thanks to a lower interest rate.

You'll have to pay closing costs to refinance into a new mortgage. The closing costs for a new mortgage will likely be higher than they would be for a new HELOC, but there may be situations in which refinancing makes sense, such as if you can lock in a lower interest rate than your original mortgage.

If you currently owe more than what your home is worth, refinancing may not be an option for you.

CHAPTER 4

How to Apply for a HELOC

How to Get Started

The first step to getting a HELOC is to figure out why you want a line of credit and whether you're ready to apply based on your credit score, DTI and equity in your home. You can do this on your own, using reputable online resources, or enlist the help of a financial expert, who can review your plans and double-check your calculations.

After that, you'll need to complete a loan application. Your relationship banker can walk you through it or you can apply online on your own.

When you fill in the application, you'll need to state how much you want to borrow, whether you're applying alone or with a co-borrower, and how you intend to use your HELOC. You'll need to provide your name, home address, mailing address, if it's different from where you live, Social Security Number, date of birth, email address, telephone numbers and employment information.

The rest of the application is designed to give your lender a snapshot of your financial situation, including your monthly income, assets (e.g., stocks, bonds or retirement accounts) and existing mortgage or other home loan, if you have one. You'll also need to list any debt you plan to pay off with your HELOC, such as a car loan, personal loan or credit-card accounts.

Documentation

Along with your application, you'll have to provide documentation as you would for most other types of home loans.

If you're a wage earner, you'll need to supply copies of your pay stubs for the last 30 days and your W-2 form for the last year.

If you're self-employed, you'll need to provide copies of your signed personal income tax returns, current-year General Excise Tax filings, current-year profit-and-loss statements and other documents related to your business.

Examples of other documentation requirements include:

- **If your home is in Hawaii:** Copies of your fire and hurricane insurance policies.
- **If your home is in Guam:** Copies of your fire and typhoon insurance policies.
- **If your home is in a designated flood hazard zone:** A copy of your flood insurance policy.
- **If your home is a condominium:** A copy of your homeowner's or condo association insurance policy.
- **If your home is held in a trust:** A copy of your trust documents.
- **If you purchased your home or refinanced your mortgage within the previous six months:** A copy of your HUD-1 Settlement Statement.

Disclosures

Like other types of home loans, HELOCs come with disclosures that you should read to make sure you understand how your loan works.

Pay close attention to:

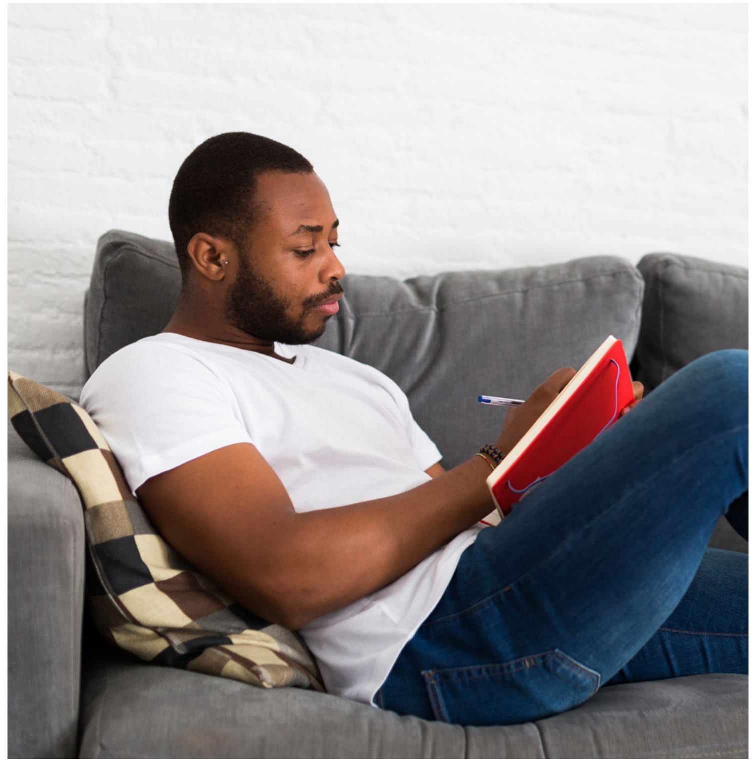
- [ ] **Your introductory rate**
- [ ] **The date when your introductory rate ends**
- [ ] **The current fully indexed APR**
- [ ] **The margin, or amount above the index rate that you'll pay**
- [ ] **The minimum and maximum interest rates**
- [ ] **The terms of your fixed-rate loan conversion option, if your HELOC has one**
- [ ] **Your draw period**
- [ ] **Your repayment period**
- [ ] **Your closing costs**
- [ ] **Fees you will or may be charged**
- [ ] **Whether you may have a balloon payment when your HELOC ends**

Closing Costs

There may be closing costs for your HELOC. These can range from half a percent of the total line of credit to 2 percent or more. (So if you qualify for $100,000 in credit, you could pay between $500 and $2,000 in closing costs). Some of the costs are lender's fees; others are paid to third parties.

Examples of HELOC closing costs include:

- **Application fee**
- **Notary fee**
- **Escrow fee**
- **Title search and insurance fees**
- **Property valuation or appraisal fee**
- **Trust review fee**
- **Condo review fee**
- **Documentation fee**
- **Recording fee**



Most of these costs should be familiar to you from when you originally purchased your home. It's also possible that your lender may waive some of their fees as part of a promotion.

You can pay your closing costs in cash at closing or you can choose a no-closing-costs HELOC. Be aware, however, that these kinds of HELOCs simply package your costs into the line of credit, potentially with higher interest rates. Ask your loan officer for details.

Ongoing Fees

In addition to your closing costs, you may be charged a variety of fees while you have your HELOC or if you want to cancel it before the term ends.

Examples of HELOC fees include:

ANNUAL FEE

This fee compensates your lender for keeping your HELOC open and active. Annual fees may vary from zero to around $100.

LATE PAYMENT FEE

This charge may be added to your HELOC if you don't make your payment within 10 to 15 days of the due date.

TRANSACTION FEE

You may be charged a fee each time you draw funds from your HELOC. It may be a flat amount or a percentage of your draw.

EARLY PAYOFF OR TERMINATION FEE

You may be charged this fee if you choose to close your HELOC before a specified date. The fee may be a flat amount or a percentage based on how long you had your HELOC before you decided to close it. You may also be charged this fee if you sell your home and pay off your HELOC early for that reason.

INACTIVITY FEE

If you don't utilize your HELOC, you may be charged a monthly or annual fee to keep it open.

LIEN RELEASE / PREPARATION FEE

This fee compensates your lender for the extra paperwork that needs to be completed to remove the recorded lien from your home when you pay off and close your HELOC.

Expert Help Is Available

As you can see, choosing a HELOC requires a fair amount of research. Fortunately, you don't have to figure it all out alone. If you're ready to consolidate debt, make home renovations, pay education expenses or use a HELOC for other reasons, we encourage you to contact us at Bank of Hawaii and find out how you can get a HELOC that's right for you.

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