By Russell Wild, MBA

SHOULD YOU PAY DOWN YOUR MORTGAGE?

To be free of debt is a worthy goal, but it may not always be the right thing to do.

Just shy of one-third of American homeowners own their home outright, according to Zillow Real Estate Research. Many others – perhaps you – have the option to either accelerate their mortgage payments, or cough up enough cash to wipe out the entire debt. But just because you *can* doesn't necessarily mean you *should*. And that's especially true if you got your mortgage within the past few years when interest rates have been at historical lows. "The most curious thing I've seen throughout my years in real estate is the number of people who pay down their mortgages, or exchange a 30-year mortgage for a 15-year mortgage, and then take on credit card debt to cover the bills," says Phil Moore Sr., principal with Moore & Ryan Real Estate, a Pennsylvania firm. The interest rate on a credit card, Moore points out, is, at a minimum, three to four times the interest rate on a home mortgage – and whereas mortgage interest is typically tax-deductible, credit card interest is not. And so we come to the first of the Big Five questions you need to ask yourself before paying down or paying off your mortgage:

1. Do you have the liquidity? If you start to pay down the mortgage, will you still have enough cash to pay your regular expenses without taking on higher interest, non-tax-deductible debt, such as credit cards and car loans? If your answer is "no," you needn't finish this article – don't pay down the mortgage.

2. Do you have a contingency fund? In addition to paying regular bills, do you have enough cash to cover unforeseen crises, such as getting laid off? "You should have an emergency fund sufficient to cover three to six months of living expenses," says Helen Huntley, CFP, of Holifield Huntley Financial Advisers, St. Petersburg, Florida. If your answer is "no, I don't have an emergency fund," paying down the mortgage is unwise.

3. Can you keep up your 401(k)? If eligible for your company's 401(k), you are not only getting a tax break on some of your income, but in many cases getting a match from your employer. That's free money you really don't want to pass up. You absolutely do not want to take on bigger mortgage payments if it means cutting out your 401(k), says Huntley. If your answer is "yes," then proceed to questions 4 and 5.

4. How does your mortgage rate compare to investment returns? OK, this question is a little tricky, but the principle is that keeping a low-interest mortgage may make perfect financial sense if you are invested aggressively, mostly in stocks, and you expect, say, an 8 percent long-term return from those investments. It would hardly make sense to pull your money out of those investments to spare you from paying, say, 3.5 percent on your mortgage. But if you are invested mostly in CDs, earning 1.5 percent, then paying off the mortgage could be a winning proposition. "You need to compare your mortgage rate to the rate of return on the investments you actually hold," says Huntley. If young and invested mainly in stocks, you may want to hold on to a low-interest mortgage; if you are nearing retirement, invested mainly in conservative financial instruments, paying off your mortgage could be a good idea for you.

5. Will paying off the mortgage give you serenity? After you're done with the number crunching, look into your heart, says Huntley. "Some people get great peace of mind from having the mortgage paid off, and even though you can't put a numeric value on that, it is certainly worth a lot." If your final answer is "yes," use an online mortgage calculator like Bankrate's (bankrate.com/mortgages/mortgage-calculator.aspx) to find your interest savings and calculate monthly payments to be free and clear by a certain date.

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