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Does it Make Sense to Buy a Second Home?

It may sound sweeter than it actually is.

Before you apply for a second mortgage, keep these factors in mind.

Owning a second home may sound like something only the wildly rich do, but that isn't always so. Sometimes people buy a new house when they haven't had success selling the first. [Other homeowners](#) might like the idea of buying a second home to fix up and sell at a fat profit – or to rent out.

For the right individual, two homes may be a great plan. But for the wrong homeowner, plenty can go awry. If you're thinking of getting a second mortgage for practical or [profitable reasons](#), now is a good time to have second thoughts, because …

1. You need to have plenty of money. You don't have to belong to the 1 percent to pull this off, but for a bank to allow you to purchase a second home without plans to sell the first, you can't be just getting by, hoping a second house will fix your financial picture.

"Underwriters will want to know you have significant reserves – potentially a buffer worth six months of payments on both properties – before approving the loan," says Brian Seibert president of Michigan First Mortgage in Waterford, Michigan.

And while every lender will be different, as a general rule, you'll need to pay a higher down payment for a second home than you would a first, says Riccardo Ravasini, owner of Rava Realty in New York City. "Say, 30 percent or more," he says.

2. You shouldn't have too much debt. You're taking on more debt when you buy a second home – something lenders take into account. In fact, your debt-to-income ratio is usually the primary issue for lenders, says Stefani Markowitz, CEO and president of Charles Rutenberg LLC, a real estate agency in New York City.

"In most cases, the debt ratio can be 36 percent to 42 percent," Markowitz says. That means, of course, that your debt – including mortgages, credit card debt, car loans and student loans – shouldn't exceed that 36 to 42 percent.

Of course, if you're planning to offset some of that debt by bringing in monthly rental income from your second home, mention that to your lender, Markowitz says.

"Renting out a home certainly lowers the risk of being rejected by a mortgage lender … the general rule of thumb is to provide as much reassurance as possible," Markowitz says.

3. You have to spend money to make money. It isn't just that you'll need a hefty down payment. Your monthly mortgage may well be higher than it would be if you just had one home.

"Because investors are viewed by banks as riskier customers, they are often subjected to higher interest rates," says Rhonda Duffy, a Georgia-based real estate agent who owns Duffy Realty of Atlanta. "To avoid financing issues, many investors use cash financing or existing lines of credit to purchase investments."

You are also going to be maintaining two homes. You thought it was hard to make sure the bushes were trimmed for one house? Now, you get to double the fun.

"Most people grossly underestimate the carrying costs of the investment in real estate. It's more than just taxes and insurance," says Celandra Deane-Bess, a vice-president with PNC Wealth Management in the District of Columbia. Consider this scenario:

Eventually – assuming you are hanging onto the second house and not selling it soon – you'll have two roofs to replace, two homes to paint and twice as many appliances, such as hot water heaters and refrigerators, to purchase, she says.

If you're spending money and losing money on the house but are truly looking at the property as a long-term investment, it may not matter to you to do that for awhile, Duffy says. Some homeowners "are happy to take a loss on a property in the short term, and build up equity for a future period, such as retirement."

4. The buyers and renters may not come. Just because you have grand plans of renting out or selling a second home doesn't mean things will work out that way. If you're investing money into fixing up a property, that takes time – time that translates into money, Duffy says.

"Every day that an investment property sits empty means a loss in profitability to an investor," she says. "All repairs and renovations must be completed quickly in order to have the fastest turnaround … Even with quality contractors, investors typically spend a significant amount of time working on houses, selecting paints and flooring, purchasing appliances or attending to the other details required to transform a home."

Even if you bought a fixer-upper that's all fixed up, you have to hope a renter or seller signs on the dotted line as soon as possible. And then, if you're renting the place, you have to hope your tenant sticks around.

"Personally, I don’t recommend that my clients rely on sources of income that could suddenly stop. You have to be comfortable that if the property is not rented out, you’ll still be on solid footing," says Kurt Fillmore, president of Wealth Trac Financial Group in Southfield, Michigan. (And back to the having-plenty-of-money point – Fillmore recommends having six months of emergency funds to cover the mortgages of both houses, in case something goes wrong.)

5. All of this is harder than it looks. Even if you sell or rent out a second home fairly quickly, you could have plenty go wrong later.

Seibert isn't just the president of a mortgage company. He has been renting properties for 20 years.

“From my own experience as a landlord, I’ve learned that it’s critical to prepare for the worst," he says. "I’ve had tenants spray paint the insides of houses, start fires indoors and attempt to flush tennis balls down the toilet. It happens with both high-priced and low-priced properties. You have to be financially ready in case the damage goes far beyond the safety deposit.”

He also observes: “Municipalities that react slowly to delinquent renters – such as Wayne County here in Michigan – can cause significant headaches for landlords. Not only are you likely to lose at least three months of rent income before any changes can begin to take place, these renters often don’t do any favors in the upkeep of the house itself.”

Fillmore even goes so far as to discourage folks who are retiring or approaching retirement from acquiring a second home – especially if they're going to rent it out – simply because of the headaches tenants can bring.

"Real estate, even on a small scale, should be seen as another job or career," Fillmore advises. "While it may be the right fit for some, it's not for everyone."

It gets even harder if you're trying to flip houses and are solely thinking of them as investments. For instance, Deane-Bess warns that you should "understand the tax implications of short-term gains and non-primary-residence sales."

Michael Rosenberg, a financial advisor at Diversified Investment Strategies in Livingston, New Jersey, agrees that investing in real estate can get really complicated.

"I only would recommend a second home purchase if you are going to take advantage of the $500,000 for married couples and $250,000 for individuals deduction that you can make without incurring capital gains tax – as long as it was your primary residence for two years before the sale," he says.

Beyond that, Rosenberg says he wouldn't advise buying a second house unless you are a real estate developer: "I would warn the average person not to get involved unless they have a unique expertise," he says.