

# Financing your Home Purchase

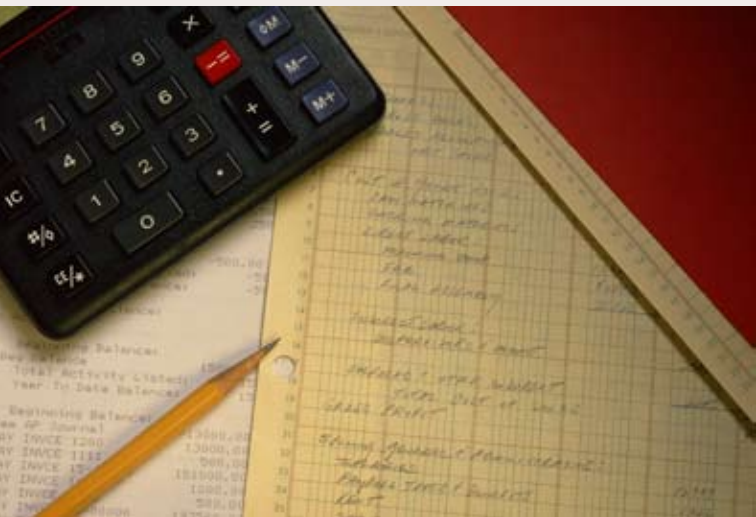


**Disclaimer**

This booklet is for information purposes only, and must not be relied on as a substitute for legal advice.

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## How Much Can You Afford?

Before you buy or build a home, find out about your financing options. Ask banks and other financial institutions:

- if you are eligible for a loan
- how much you need for a deposit
- if funds are always available and
- how much you can borrow.

The amount you can borrow will normally depend on:

- your income
- the interest rate
- the term of the loan
- your other commitments, such as credit cards and personal loans.

You may be eligible for a loan if you:

- have enough to pay a deposit on a property and sufficient funds for additional costs and
- are in regular employment and receive sufficient income to service the loan and
- meet the requirements of the lender.

### Consumer Credit Code

The Consumer Credit Code is a set of rules to ensure borrowers are aware of their obligations in credit transactions. Institutions providing home loans are required to truthfully divulge all relevant information about the loan in a written contract. The contract should include information on interest rates, credit fees and charges, and commissions. For further information on the Consumer Credit Code, contact the Office of Fair Trading.

## Other loan commitments

A housing loan is a long-term commitment and the home it provides will be important to your health and wellbeing. You should not jeopardise this by over-committing yourself with other credit. Other credit reduces the amount you can borrow and whether you are able to make your home loan repayments. The most common reason borrowers get into difficulties repaying their mortgage is over commitment to other credit.

## Deposit

The larger your deposit, the easier it will be to buy a home. You will not need to borrow as much. Generally, you will need between 5% and 20% of the purchase price of the property as a deposit. However, some lenders will lend 100% of the value of the property provided the borrower meets certain strict conditions. You will also need to budget for other costs, such as:

- legal expenses
- lender's fees
- government charges and
- inspection costs.

Refer to the brochure *A Guide to the Costs of Home Purchase* for further information on home purchase costs.

## Interest charges

Interest is charged to the borrower by the lender for the use of the lender's money. The interest rate is the annual percentage of a loan amount that is charged as interest. The interest rate can and will fluctuate with changes in economic conditions.

Rates of interest may be fixed or capped for a period of time, or alternatively may vary during the term of the loan in line with interest rates generally.

## What is a mortgage?

The mortgage is the legal document for the loan on a property, with the terms and conditions. Generally, if repayments are not maintained or the borrower otherwise breaches the mortgage conditions, the lender has the right to sell the property to recover the outstanding debt.

Second mortgages may be obtained if additional funds are needed to complete the purchase of a home, or for other reasons. The first lender has to agree. Generally, lenders prefer to lend all of the money and hold first and second mortgages.

## Mortgage insurance

This is needed if you borrow more than a set proportion of the valuation. The mortgage insurance premium is a once only payment. Mortgage insurance protects the lender if you default on the loan and the property is sold for less than the outstanding loan amount.

You, as the borrower, can take additional insurance such as income protection insurance to cover the mortgage repayment in the event of illness, accident, unemployment or death.

## Types of Lenders

There are many different types of home lenders. Each has different interest rates, terms, conditions and lending criteria. The most common types of lenders are outlined below.

### Banks

Banks have the primary share of the owner occupied home loan market in Australia. Banks can provide their customers with integrated banking packages (eg. lending products, financial services, transaction and savings accounts). Banks lend funds for housing up to a 30-year term. The deposit required can vary from 5% to 25%.

### Building societies

Building societies are cooperative organisations whose members are shareholders. Building societies are often referred to as mutual societies.

Building societies operate in much the same manner as banks, offering integrated financial services (eg. home loans, saving accounts, cheque accounts, credit card access and financial planning and investment services).

## **Credit unions**

Most credit unions lend funds for housing to members. Credit unions can be a good source of finance when additional funds are required.

## **Mortgage managers**

Mortgage managers organise funding for homebuyers from a variety of funding sources. The owner of the mortgage is not the mortgage manager but the provider of the funds, who operates through a trustee.

## **Mortgage brokers**

Mortgage brokers act as agents between borrowers and prospective lenders. The task of the mortgage broker is to find and arrange the most suitable loan for the borrower. They do not lend money or manage loans.

## **Cooperative housing societies**

Cooperative housing societies provide housing loans predominantly to low-to-moderate income earners. Customers of cooperative housing societies become members of the society by purchasing a share.

## **Superannuation funds**

Housing loans are sometimes available to people who contribute to certain superannuation schemes. Borrowers usually must meet membership and/or qualifying criteria.

## **Solicitors**

Some solicitors have clients' funds available for housing loans. Normally, these loans are for two or three years only and, at the end of this time, finance has to be obtained from another source. These loans can often be 'rolled over' for another set period of time before the loan has to be repaid. Interest only is paid on these loans, meaning the amount borrowed is not reduced.

## Finance companies

Loans from finance companies have higher interest rates than from other lenders so they are generally not suitable as first mortgage housing loans.

## Vendor finance

Sometimes the vendor (the seller) is prepared to lend part of the purchase funds to the buyer, usually over a two- or three-year term. Interest only is paid, meaning the amount borrowed is not reduced. At the end of the term, finance has to be obtained from another source.

## Types of Loans

### Standard variable interest rate loan

This is the usual loan offered by home loan lenders and the most popular type of home loan. The interest rate can go up or down throughout the term of the loan.

Repayments, usually monthly, are the same throughout the term of the loan, changing only with the rise and fall of interest rates. Normally, in the early years of the loan, each repayment is mostly paying interest charges and less of the loan principal. In later years, the opposite occurs.

Features, such as added flexibility in making repayments and a redraw facility, are often included in this type of loan.

### Basic variable interest rate loan

This type of loan offers a lower interest rate and repayment than a standard variable interest rate loan but has fewer or none of the features of standard variable loans.

### Fixed interest rate loan

This type of loan offers a fixed interest rate for a specific period (eg. six months to five years). At the end of the fixed rate period, the loan is renegotiated for a further fixed term or reverts to the variable interest rate current at that time. It may not be possible to pay extra amounts off the principal

without paying a penalty. A penalty usually applies if the borrower wishes to refinance the loan during the fixed interest rate period.

### **Part variable/part fixed interest rate loan**

Often referred to as split or combination loans, this loan allows the borrower to pay a fixed interest rate on a portion of the loan while paying interest on the remaining portion at the standard variable interest rate. This gives the borrower flexibility and interest rate certainty.

### **Capped or introductory interest rate loan**

Under this type of loan, the interest rate is fixed for the capped period, which is usually six to 12 months. During this period, the interest rate cannot go higher but it may go lower if the lender's standard variable interest rate falls below the capped rate. These loans are commonly referred to as honeymoon rate loans. Often, these loans offer the lowest interest rates and this can assist a new borrower to adjust to mortgage repayments. However, the borrower also needs to be prepared for an increase in loan repayments once the capped period ends.

### **All-in-one loan**

An all-in-one loan is usually a variable interest rate loan, which permits the borrower to place all their income into the one account, reducing the loan balance and the interest paid. The borrower can access the account to meet day-to-day expenses. Additional payments are permitted without attracting penalties. Due to its flexibility, there may be greater costs (eg. higher interest rate and/or higher monthly fees).

### **Home equity loan**

A home equity loan allows a borrower to use the equity in the home (the portion of the property the borrower owns) to gain access to an immediate source of funds. There are two types of home equity loans. Under the first type of home equity loan a borrower may borrow an additional lump sum amount which acts like a second mortgage.

The second type is an equity overdraft or line of credit. A line of credit is like an overdraft secured by the equity in the borrower's home. The interest rate on a line of credit is usually higher than for other home loans but less than the interest rate on a personal loan or credit card.

### **Consolidated loan**

A consolidated loan permits the borrower to combine several loans, such as a home loan, credit card debt and personal loan into a single variable or fixed rate loan. This can result in a lower overall repayment and interest rate for the borrower.

### **Interest only loan**

An interest only loan requires the interest to be paid during the loan term with the amount borrowed becoming due at the end of the loan. These loans are usually for one to five years and are often used by people buying investment properties.

### **Bridging loan**

A bridging loan is often used to buy a property while waiting for the sale of your existing property. A bridging loan is a short-term housing loan where repayments meet the interest only. The amount borrowed becomes due at the end of the loan term. As higher interest rates are usually charged for bridging loans, it is best to keep the term as short as possible.

## Other Loan Features

### **Fortnightly repayments**

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You can save money by making fortnightly rather than monthly repayments. This is done by dividing your monthly repayments in half and making these once a fortnight. This means that you will make one extra repayment a year. This is because there are 26 fortnights (or 13 sets of four weeks) in a year, and only 12 months. Making repayments fortnightly can reduce the term of your loan and save you a lot of money on interest repayments.

### **Extra repayments**

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Most variable and some fixed rate loans allow the borrower to make additional or lump sum repayments without penalty. If you can afford it, regularly adding a little bit extra to your repayments can significantly reduce the amount you end up paying over the term of the loan. If you can make a lump sum payment into your home loan account, this will also reduce the term of the loan and the total amount you repay.

### **Mortgage offset account**

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A mortgage offset account is a savings account combined with a home loan but as two separate accounts. Any interest earned on the savings account is applied to reduce the interest payable on the home loan.

### **Redraw facility**

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A redraw facility allows you to withdraw additional repayments, which have previously been made. Usually there is:

- a minimum redraw amount
- a maximum redraw amount
- a fee per redraw and
- an allowable number of redraws each year.

# Going for the Home Loan Interview

You should make appointments at various lending bodies to speak to a loans officer about a possible home loan. Take information to help the lending body assess how much they will lend you (eg. current bank statements, payslips or other proof of income and documents showing ownership of any property). Be prepared to furnish details of any financial commitments you have (eg. personal loans, credit cards).

Go to several lenders and compare the interest rates and loan conditions offered. If you are a first homebuyer, ask about any special concessions that may be available.

Once you have selected a property to buy, make a formal application to your chosen lender. You will be required to complete an application form and provide the lender with details of the property.

## Questions to ask lenders

When seeking information from lenders or attending a loan interview, it may be helpful to ask the loans officer the following questions:

Q. What fees apply to the loan application?

Q. Will any of the application fees be refunded if I don't proceed?

Q. Do these fees apply to this application only or can they apply partly to a subsequent loan application?

Q. How much can I borrow?

Q. What percentage of my income will be committed to loan repayments?

Q. How much deposit will I need, including approximate associated costs?

Q. What conditions apply to fixed rate, capped and introductory loans?

Q. What are the monthly repayments and can I pay fortnightly?

Q. Will I need to pay mortgage insurance, and if so, how much will that cost? Can I add this to the loan or do I have to pay up front?

Q. Is the interest daily or monthly reducible?

Q. If the interest rate increases, will the term be lengthened or will I have to meet the increased repayments?

Q. Are there further charges or any ongoing charges/monthly fees?

Q. How do I make repayments? Is there a repayment book? Can repayments be taken directly from my salary or bank account?

Q. How long will it take to receive formal loan approval?

Q. What legal fees will be charged for preparing documents, such as mortgages?

Q. Are there any penalties for repaying the whole loan before the full term or for making extra payments?

Q. Is there a mortgage offset facility?

Q. Is there a redraw facility?

## Useful Telephone Numbers

<b>Archicentre</b>	1300 134 513
<b>Office of Fair Trading</b>	
Credit Section	(02) 9895 0111
Real Estate Matters	(02) 9895 0297
Strata Schemes	(02) 9338 7900 1800 451 431
<b>Land and Property Information NSW</b>	(02) 9228 6666 1300 052 637
<b>Law Access NSW</b>	1300 888 529
<b>Landcom – Sales Office</b>	(02) 9629 2999
<b>Credit Ombudsman Service Limited</b>	1800 138 422
<b>Financial Ombudsman Services</b>	1300 780 808
<b>Office of State Revenue</b>	
First Home Plus/First Home Owner Grant Scheme	(02) 9685 2187 1300 130 624
<b>Real Estate Institute of NSW</b>	(02) 9264 2343
<b>Sydney Building Information Centre</b>	(02) 8303 0580 1300 884 876



## Further information

If you have any questions about the information in this brochure, please contact the **Home Purchase Advisory Service**:

**Telephone: Freecall 1800 806 653**

**TTY Service: 1800 628 310**

**Email: [advisory@housing.nsw.gov.au](mailto:advisory@housing.nsw.gov.au)**

Housing NSW's website has current information on home purchase issues and services, including all the Home Purchase Advisory Service publications.

Website: **[www.housing.nsw.gov.au](http://www.housing.nsw.gov.au)**

The information contained in this brochure was current as at February 2008.

## Interpreter Services

If you have difficulty understanding English, contact the Translating and Interpreting Service (TIS) on 131 450. The Translating and Interpreting Service will telephone Housing NSW for you at no cost.



**[www.housing.nsw.gov.au](http://www.housing.nsw.gov.au)**

Housing NSW  
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