

May 2006 Newsletter

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How we saved a client over \$17,000 in mortgage insurance costs

There are many stories in the press about how competitive the mortgage market is and how the banks are experiencing a reduction in net interest rate margins (because they are being pressured by competition to offer lower rates). However, this competitive pricing has stabilised in recent months. Instead, we have noticed that lenders are preferring to compete on credit policy issues such as waiving lenders mortgage insurance (LMI) for very strong clients (i.e. large incomes). LMI is normally payable if you borrow more than 80% of a property's value and can be a very costly upfront fee. Obtaining a waiver of mortgage insurance can save borrowers literally thousands of dollars.

How much does mortgage insurance cost?

LMI is a one-off upfront cost that is charged when you borrow more than 80% of a property's value. This cost can be added to the loan. Generally, this fee is paid to a third party mortgage insurer (it's not necessarily a fee charged directly by the lender). LMI covers the lender's risk, not the borrower's, in the circumstance where the sales proceeds from selling the security (i.e. if the lender has to sell the property due to defaulting on the loan contract) are not enough to repay the loan in full. LMI covers the shortfall. LMI can be very costly. For example, if you borrowed 90% of a property worth \$650,000 (i.e. loan amount of \$585,000), generally LMI would cost over \$10,000.

Waiver of mortgage insurance in return for extra repayments

Many lenders will consider waiving LMI, if borrowers commit to an accelerated repayment program. That is, borrowers would be required to make regular extra repayments so that the loan to value ratio is reduced quicker than what would be required with a standard 30 year loan term. Normally, these

options are only workable for loan to value ratios of less than 90%. Some lenders will require the loan to value ratio to be reduced to 80% within 2 years and others will give borrowers a lot more time.

One of our lenders has a standard policy where they will lend up to 90% of a property's value, if the loan term is reduced from 30 years to approximately 20 years. This would result in the client's committing to repay an extra \$650 per month (on top of standard 30 year loan term repayments of \$3,840) on a loan of \$585,000 and this would save the borrower \$10,000 in mortgage insurance.

Borrowers will not necessarily have to make these extra repayments for the whole loan term. As soon as the loan to value ratio is 80% or less, the borrower can ask the lender to reset the repayments back to normal. The loan to value ratio will naturally reduce as the borrower reduces the loan amount (via repayments). In addition, hopefully the property's value increases (particularly if improvements are made). Therefore, extra repayments may only be required for the first couple of years.

Last week we obtained an approval for a client who needed to borrow a total of \$940,000 to purchase a new home. He needed to borrow 90% of the property's value. We were able to get LMI waived, saving this client over \$17,800 (in LMI costs). The client had to commit to repaying an extra \$1,035 per month, on top of normal 30 year loan repayments of \$6,170 per month.

Waiver of mortgage insurance without extra repayments

In some situations, extra repayments will not be required to get a waiver of LMI. This option is generally only available for very strong applications. A strong application may involve very strong incomes, stable employment, a strong net asset base, etc. Often, we find greater success if the applicants have been customers of the lenders for a reasonable period of time. It's unlikely that we could get LMI waived, if the loan to value ratio is over 85%. This option is really only achievable if the client needs to borrow between 80% to 85% of the property's value. However, that might change over time.

In April 2006, we obtained a waiver of mortgage

insurance for a client who needed to borrow \$720,000 to purchase a new home. The client's overall loan to value ratio was just under 85%. The clients did not have to commit to make extra repayments. In addition, we were able to negotiate additional interest rate discounts. As a result, we saved these clients over \$9,000 in LMI costs and more in interest.

Waiver of mortgage insurance for medical practitioners

There are a couple of lenders that have special deals for medical practitioners. Some of these include allowing them to borrow up to 95% of their first property purchase without having to pay for LMI. Other lenders will lend 90% of the medical practitioner's home (for their first and subsequent purchases) without LMI.

Experience and competitor knowledge is the key

Whenever I write articles for our newsletter or other magazines, I always try to be impartial and not promote mortgage brokers or ProSolution Private Clients. With that in mind, I will make one important statement. An experienced and knowledgeable mortgage broker is best placed to negotiate a waiver of LMI. There are two reasons for this. Firstly, the broker will be able to provide the lenders with evidence that other lenders are waiving LMI. You may think that they would already be aware of this, but that's not always the case. As recently as last week, I was asked by a lender to provide this evidence. It is easier for lenders to get internal authorisation for LMI waivers, if they can cite competitive pressures (i.e. if they don't approve the waiver then they will lose the client). Secondly, an experienced broker will be able to prepare a written submission outlining the strengths of the application and why LMI should be waived. Often, the quality of this submission can make or break the likelihood of the LMI waiver being approved.

Explore all avenues

I doubt that the mortgage market will get anymore competitive in terms of price (i.e. interest rates and fees). I think that the next round of competition will be fought in the credit policy arena. As stated, we have already seen this occur in our professional market. If you think you'll have to pay for mortgage insurance, think again! We might be able to negotiate a waiver.

6.54% p.a. Fixed for 3 Years (Interest-in-advance)

Our original offer of 6.40% fixed for 3 years (interest-in-advance) has been fully subscribed to. That's not surprising. It was an extremely low rate.

Due to a change in wholesale money markets, we could not negotiate the same rate. Instead, the lowest rate offered by the 35 lenders on our panel is 6.54% p.a., fixed for 3 years (interest-in-advance) by the Commonwealth Bank of Australia. This is still a very competitive rate, given that the standard variable rate is 7.57%. This fixed rate of 6.54% might not last for long, so if you are considering using an interest-in-advance product, then you should act today.

Tax benefits of interest-in-advance: You can prepay interest on your investment debt 12 months in advance (i.e. interest from 1/7/06 to 30/6/07) and claim the full tax deduction in your tax return for the year ending 30 June 2006. You can continue to do this every 12 months. This can provide significant tax savings. Of course, speak with your accountant or advisor to ensure this product is appropriate for you.

How do you finance the interest payments: Normally, borrowers would finance repayment from rental and other income on a monthly basis. However, with this product, you will have to pay 12 months of interest in advance. One way to achieve this is to borrow an amount equal to 12 months of interest for the first payment. You can then save the next 12 months of interest from your rental or other income for the next prepayment in one year. This is achievable, subject to borrowing capacity and having sufficient security.

We must lodge your application by 1 June 2006 to ensure that your loan is set up before 30 June 2006. [Click here to send us an email requesting a product fact sheet \(e.g. lender, fees, features, etc.\).](#)

Best Rates

Discount Variable	6.74%
Offset (Pro Package)	6.87% (for > \$250k)
Line of credit	6.87% (for > \$500k)
1 Year Fixed	6.29%
3 Years Fixed	6.74% (lower for > \$600k)
5 Years Fixed	6.84% (lower for > \$600k)
10 Year Fixed	7.20%
15 Year Fixed	7.32%

Comparison rates available by request.