RICHARD JEFFERIES

APPROVED

A SIMPLE GUIDE TO HOME LOANS
FOR BUSY PROFESSIONALS

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DEDICATION

Dedicated to my parents, Philip and Anne, who taught me taking care of your financial welfare, allows more time with your family.

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ACKNOWLEDGMENTS

Like most small business owners, I've found starting and building a business full of ups and downs. It can be exciting, challenging, incredibly frustrating and satisfying.

There has been a huge number of people who have made my journey possible. Without the help of these people, I would not be where I am today.

Firstly, I'd like to thank my parents, Philip and Anne, who provided unwavering support over the years. They have always been there to encourage and listen when times were difficult and also to embrace the successful times.

To my brothers Jon and Andrew (who now works with me in the business), thank you for your ongoing support and friendship. I feel incredibly lucky to have two brothers who are also my closest friends.

To my good friends Rob Douglas and Steve Cadell, thank you for always being a sounding board. Both of you have great business insights that I value greatly.

I'd like to thank all of the staff at the various banks who have provided much needed guidance and training on how banks assess home loan applications.

Robyn Yould, thank you for five wonderful years of service when the business was in its infancy. Your work ethic and customer service were exemplary. Andrea Welsh, thank you for your initiative and enthusiasm – it is infectious.

To Rob Lyndon, for providing me with the opportunity to assist so many clients, and Eric Reid, who assisted me in my early years as a mortgage broker, providing so many learnings around finance and credit and listening when I would invariably hit brick walls when working towards results for clients.

Finally, thank you to our clients and referral partners. Naturally, this business journey would not have been possible without the trust you have placed in me and the team to handle the process on your behalf.

WHY I WROTE THIS BOOK

In 2001, at the age of 21, I was working part-time and completing a degree in business when an opportunity came up to buy a block of land on the Sunshine Coast. I knew very little about property at the time (our family had talked more about shares as a way of investing rather than property), but when I was told about how fast the blocks of land were selling, I became naturally interested in possibly purchasing one.

So, I went to the sales office, spoke to them about what was involved to purchase a block of land and the sales agent turned to me and said, "Now, you do have your finance sorted out, don't you?"

To which I replied, "argh, no I don't actually" (in a nervous voice).

I then felt like a fool; of course, I should have thought about how I was going to finance the purchase. But I hadn't given it much thought at all.

The sales agent then kindly recommended a mortgage broker. I had no idea what a mortgage broker really did, but I phoned the gentleman and we arranged to meet at a local coffee shop.

Upon meeting, he asked me about my financial position. I was only working part-time and my young brother, who was happy to buy the block of land with me, was studying. So, our financial position wasn't overly strong, to say the least.

He then asked me if my parents could assist as a guarantor. I wasn't too sure what that involved, but I finally convinced my mum that it was a good idea (I started with mum as dad would have been a little tougher to convince).

We lodged an application to rely on her income to support the repayments on the loan, should we not be able to make them. We didn't have much in the way of a savings, so the broker suggested we take a margin loan against some shares we owned to cover the deposit (a margin loan is similar to a mortgage, but instead of the bank holding your house as security, they take security over shares that you own).

I don't remember a lot of the details, and looking back, I think how risky the purchase was. Borrowing money against shares to use for a deposit is certainly not something I would recommend people do, and on top of that we had our mother as guarantor for the loan.

Needless to say, the loan was approved and we settled on the block of land. For those of you who can remember, property prices were increasing very quickly in the early 2000s, and within six months we managed to sell the block of land and make a substantial profit.

I look back now and realise how little I understood about the whole process, and how, without the mortgage broker's advice, we would have never been able to complete the purchase.

It wasn't until a few years later, when I was working for a building company, that the opportunity came up for me to try mortgage broking for myself.

I enrolled in the necessary course to become accredited and was just fascinated about how much I could do to help people in this area, particularly in understanding terms that they just don't come across in day-to-day life, that initially can seem quite intimidating.

Fast forward 17 years and I've been very lucky to help many people with finance applications.

The greatest enjoyment comes from breaking down confusing concepts and making them easy to understand.

If I, along with our team, can make the finance part a less stressful one, and empower people to understand and make confident decisions about their finance, we'll feel like we have done our part in the process.

HOW THIS BOOK WORKS

The book is designed to take you through what you need to know when buying your first home and arranging finance approval.

It is in a chronological order that will take you through the stages of approval and purchase, as they would occur when you come to buying property.

There are also approval tips throughout the book, which will increase your chances of quick approval.

We have done this via what we refer to as the Newbridge 4 L's of lending:

1. Level
2. Loan type
3. Lender
4. Lodgement

Section 1 is about how much you can borrow based on your income and expenses, your deposit and the stability of your employment.

Step 1 – Deposit and Repayments.

It is crucial to get a good understanding of this so you know what your level of savings needs to be, what loan that means from the bank and in turn what your repayments will be.

There are also now some great resources to use for budgeting and working towards saving for a deposit, if you're not in a position to purchase now (see saving for your deposit on page 15).

Step 2 – Borrowing Power

Borrowing power refers to how much the banks will lend you based on your household income and your current outgoings and expenses. By having an understanding of your borrowing power, you can plan ahead to see what properties are within your range.

Step 3 – Stability and conduct

Banks will want to understand stability, with regards to how long you have been in your current position of employment.

They will also want to see that conduct on your everyday accounts and any loans you have in place, have been kept up to date and that conduct on your credit file (often referred to as your credit score) is satisfactory.

If you follow these 3 steps – you can determine

a) What your price range is.
b) What your repayments will be.
c) Whether your employment history and account conduct is satisfactory for a successful approval and be ready to purchase your first home.

Section 2 covers the type of loan that will be best for you.
It is important to align the right type of loan to your circumstances, as this ensures you are

a) Able to make sure you have the right features in a loan you require.
b) Not paying for features in a home loan you don't need.
c) Not locked into a type of home loan that, should your circumstances change, will not charge large penalties for changing your loan or closing it completely.

Determining which type of loan is right involves following a simple process of elimination.

By following and answering these questions, you will be able to arrive at the right type of loan for your situation.

Section 3 looks at choosing the right lender or bank for your home loan.

Whilst most banks have the same types of home loans (making it easy to compare), they all offer different interest rates at various times.

Once the correct loan type is selected, you simply sit down with your broker and compare the interest rates and fees offered by each bank to find the most competitive offering for you.

If you follow the process of starting with the right loan type, then selecting the bank, this will ensure you are

a) Not paying a higher interest rate than necessary.
b) Not paying more fees than needed.
c) Not locked into a loan type that has a high interest rate and is costly to get out of.

Section 4 covers the lodgement of your application.

Lodging your application is the final step in obtaining approval, and this section walks you through what happens once your application is submitted.

This section gives you a clear understanding of the various steps involved so there are no nasty surprises when buying your first home, which can be quite overwhelming in itself.

By going through this section, you will gain confidence as you understand the process.

It will save you unnecessary time and energy in worrying about finance-related matters, allowing you to direct time and energy towards finding the right property.

Frequently asked questions

Finally, a number of frequently asked questions are covered in the final section of this book.

We often find that the same questions come up for people buying property and this section answers them.

By covering off on the FAQ's you will be able to find answers to questions you have, as well as answers to questions you may have not thought of.

Determining what property you can afford

We often get asked by clients what price they should aim for. Whilst the bank may lend you a certain amount, its best to make that decision based on your own budget and circumstances.

I would suggest the following steps to determine what price range you can afford:

a) Complete a comprehensive budget (usually required as part of the application process).
b) Work back to determine what repayments you can afford. If you can afford $2,600 per month, this equates to a loan of $545,000 (based on an interest rate of 4% p.a and loan term of 30 years).
c) Be sure to check that it is realistic (taking into account what you're currently paying in rent).
d) Add your deposit to the loan amount you can afford to arrive at your purchase price. For example, if your loan is $545,000 and your deposit is $100,000 (after allowing for stamp duty and other purchasing costs) your target purchase price is $645,000

We find that people who spend the time researching their finance and property options at the beginning usually have a much more enjoyable experience when buying.

SECTION ONE – LEVEL
CHAPTER ONE – DEPOSIT

The first question banks will ask when you apply for a loan is, "What amount of deposit are you contributing to the property?".

The deposit refers to the amount of funds/savings you are putting towards the property, as opposed to the amount you are relying on the bank to provide.

It's essential to get a good understanding of what deposit is required, as this is one of the main criteria banks use to assess whether to approve your application.

If you can grasp exactly how much deposit you require and whether what you have now is sufficient, you are well on your way to ensuring your approval is successful and stress free.

How much deposit is required?

In this section we cover exactly how much deposit you will require, based on the price of the type of property you are interested in purchasing.

Knowing this will highlight

a) Whether you have the required deposit and are ready to apply for finance now, or;
b) What amount of deposit you need to be able to make a purchase in the future.

Having the right deposit amount will mean a greater chance for a successful and fast approval.

The minimum deposit required by most banks we have on our panel is currently 5% of the total property value.

For example, if the price of the property you are intending to purchase is $500,000, the minimum deposit you would require would be $25,000.

Having a deposit that is less than 20% will mean that you attract 'lenders mortgage insurance', which is insurance that covers the bank, not the borrower, but that the borrower pays for.

Approximately 30 years ago when my parents, and possibly yours, were buying property, they needed to come up with a 20% deposit to get a home loan approval.

Property prices pre-1990's certainly weren't what they are today, but a 20% deposit of the property price was still a considerable amount of money to come up with.

As a result, banks then decided that to assist more people to be able to get into the property market, they would accept less than a 20% deposit.

However, accepting a deposit of less than 20%, meant the banks were taking on more risk (as there was less of a buffer if they had to sell the property in the future).

Therefore, banks took out insurance to cover themselves for this additional risk.

Whilst the banks are protected through lenders mortgage insurance (LMI), it is the borrower who has to pay the cost of the insurance.

Still today, this is one the great misunderstandings, that mortgage insurance is paid by the borrower and protects the bank, not the borrower.

Working out whether you have to pay mortgage insurance is usually quite straight forward. It's crucial to get a good understanding of mortgage insurance and whether it will affect your application, as it can be one of the major costs when purchasing property.

By understanding it, you can either come up with a greater deposit to reduce the mortgage insurance, or at the very least, understand why you are being charged mortgage insurance.

You can then weigh up the benefits as to whether you should buy now and pay mortgage insurance or hold off and increase your deposit further to reduce or remove the cost of the mortgage insurance.

For example, if you were to purchase a property for $500,000 and you had a 5% deposit towards the property, the bank would be lending you $475,000.

The mortgage insurance in this instance would be $16,500 approximately.

Note, mortgage insurance is only charged once, it's not something you need to continually pay for.

Consider the below example.

Steve was a successful guy in an executive senior role that was paying well. Steve had minimal deposit because he had been through a divorce, and as such could only come up with a 5% deposit.

In Steve's case, we were able to work with a bank who would allow Steve to add the mortgage insurance to the loan. This meant it wasn't additional funds he would need to come up with. (This is now becoming quite rare for clients with a 5% deposit.)

In most cases, borrowers with a 5% minimum deposit are required to pay the mortgage insurance upfront (once only).

The table that follows is designed to give you an estimate of how much mortgage insurance you will pay based on your deposit.

Purchase price

Percentage of deposit	$300,000	$500,000	$750,000	$1,000,000
5%	$8,000	$16,600	$33,500	$45,900
10%	$4,400	$9,500	$17,500	$23,600
15%	$2,300	$4,900	$9,000	$12,600
20%	$0	$0	$0	$0

<u>Approval Tip:</u>

Banks like to see customers show consistent savings, particularly over a three month period. If you can set up an automatic savings pattern ($100 per week for example) that is consistent and regular this will greatly enhance your chances of approval.

Most people go astray in the finance process because they have not gone through the above steps and fully understood what is required.

Often these people have signed contracts on homes that they are unable to finance due to a lack of deposit and borrowing power.

This means they may need to pull out of the contract and withdraw from the purchase.

And whilst there is usually a finance period in place to allow them to do this, there are often costs involved with their solicitor, who assists with the signing and preparation of the contract.

On top of this, they are often left feeling deflated and emotionally exhausted, after being excited and looking forward to purchasing their first home – only to find it's out of their reach.

This could have been avoided if they had first properly determined their financial level.

First Home Buyers Grant

The First Home Buyers Grant was introduced around Australia to assist first-home buyers to get into the property market. Currently a $15,000 grant is available in QLD for people who buy or build a brand new home (houses, townhouses and units).

A brand new home is referred to as a home that has never been lived in before. The grants available in each area are regularly changing, so keep an eye on your relevant state or territory for further information.

How long to save for your deposit?

If you're feeling a little overwhelmed or intimidated by saving the required deposit, this is completely understandable and very common among first home buyers.

Since 2000, house prices in Australia have increased dramatically making it a real challenge for young people in Australia looking to get into their first home.

As such, a common question we are asked is, "How long should I be saving before purchasing my first home?".

Most banks will want to see that you have saved your deposit over a three month period. This can be done via

a) Building up your savings gradually over a three month period; or
b) Simply having your deposit balance sitting consistently in your account for three months.

However, if your deposit is more than 10% or 15% (depending on the banks individual lending rules) the banks waive the need to see that you have savings over a three month period (which is referred to as genuine savings).

If you can establish a solid three month savings pattern building up to a 5% or 10% deposit, it provides the bank with a lot of confidence that you will be able to handle the mortgage repayments.

Especially if you can demonstrate you can save consistently each month whilst also paying rent (the case for most people).

If you're in a position where your deposit is more than 10% or 15%, the bank will not insist on seeing savings over a three month period, but it will certainly strengthen your application if you can show this.

We have often had clients who have been weak in certain areas of their application (new to their job for example), but because they have been able to save consistently and demonstrate this, banks have chosen to look past such weaknesses.

How much deposit should you have before purchasing?

There are lots of different views on how much deposit you should have before purchasing. For example, the '*Barefoot Investor*', Scott Pape, suggests having a 20% deposit as a minimum before purchasing property.

This recommendation certainly makes a lot of sense, as

a) You avoid mortgage insurance.
b) Banks often provide better rates for people with a 20% deposit.
c) You immediately have equity in your home.
d) It helps you develop the habit of saving.

These first two factors alone can mean a huge difference in savings over the course of your home loan.

Consider the following example – two couples are both looking to purchase a $600,000 home to live in.

Couple (A) has a 20% deposit saved, plus funds to cover stamp duty and other associated costs.

Couple (B) has a 10% deposit saved, plus funds to cover stamp duty and other associated costs.

	Couple A 20% deposit	Couple B 10% deposit
Savings required (Deposit+Costs)	$136,830	$76,830
Lenders Mortgage Insurance (LMI)	$0	$13,100 (approximately)
Loan amount	$480,000	$563,100
Repayments per month (based on 4% p.a. interest rate over 30 years)	$2,291 per month	$2,688 per month

When most people see this calculation, they see that there really isn't a great difference in repayments, which often leads to the argument of buying as soon as you get a deposit together, just so you can get in.

Below are some of the advantages and disadvantages to delaying your purchase until you have a 20% deposit.

Advantages

1. Lower interest rate
2. No mortgage insurance cost
3. Easier approval criteria

Disadvantages

1. Can take significant time to save, whilst also having to pay rent
2. Property market may increase at a faster rate than your savings
3. Rent money is dead money

Each person's situation will be different and as such needs to worked out on its own merits.

One point I would leave you with is, whilst we have experienced unprecedented property growth in the last 15 to 20 years, property is like any other type of asset – in can go up and it can go down.

A great piece of advice that was given to me was to purchase property when it's the right time for you, based on your circumstances. I warn against trying to buy property on the basis of trying to pick the market.

Types of deposit

It's important to know and understand the different types of deposit available when buying property. Whilst most people would naturally think of savings as their source of deposit, other forms can be

a) Shares.
b) Cash via a gift.
c) Sale of an asset (such as a car).
d) Using a guarantor instead of coming up with a deposit.

It's important to understand these various forms of deposit, as each is treated differently by the bank for approval.

Below, we will look at each in more detail.

Shares

Shares, or stocks, are a small ownership in a much larger company. These small "shares" within a company are traded on the Australian Stock Exchange (within Australia).

Shares are an asset and as such are looked on favourably by banks. If you do own shares you can sell them and have the money in your bank within a matter of days. For this reason, banks treat shares the same way they would savings in the bank.

Holding shares for a period of three months or more will meet the bank's genuine savings policy and demonstrate that you have an ability to save and maintain savings.

Saving for your deposit

If saving for a deposit to buy a home feels daunting and unreachable, that is certainly understandable, and you would be among the majority of Australian's looking to purchase their first home.

When saving for your deposit I would suggest starting with 4 easy steps:

1. Complete a budget based on your circumstances now, to see how much you are able to save each month.
2. Determine the purchase price of a few different properties you would like to buy in suburbs you would like to live in. (I would suggest looking at three options, #1 An optimum place to live, #2 being where you would be happy to live and #3 being where you "could" live.)
3. Work back from that purchase price to determine the deposit required, based on a 10% or 20% amount (adding an amount for any property and government fees such as stamp duty).
4. You will then be able to work out a time frame to reach your target, based on your current ability to save from the budget you completed, coupled with any other savings you currently have.

A helpful budget can be found at www.moneysmart.gov.au.

Once you have a budget established, you may wish to set up a system that will make it almost "automatic" for you to stay on track.

A good strategy can be to utilise some of the budgeting apps that can sync in with your bank accounts and categorizes your spending. Some of these include:

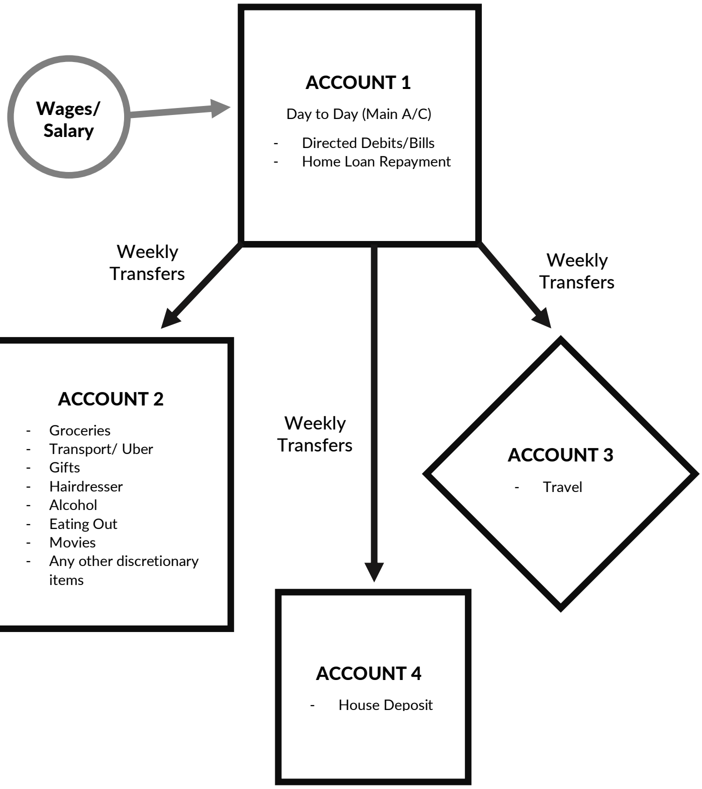
Pocketbook
Trackmygoals
Trackmyspend
MoneyBrilliant

Some of the above may be free and some come at a cost.

Another popular strategy I use and show our clients, is to set up different accounts (often referred to as *buckets*) to allocate an amount each week for your spending.

For example:

Income
Bills
Food/Hobbies
Holidays
House deposit



This helps you monitor how much you spend and makes it easier to track, particularly given that bills will usually be a fixed amount, whereas food and hobbies could vary.

Industry benefits

The field of employment you are in can have an impact on your finance application. It is therefore beneficial to be aware of the benefits that exist for some professions. For example, if you are currently in the medical, legal or accounting fields, some banks may allow you to put only a 10% deposit towards your purchase (rather than a 20% deposit) to avoid mortgage insurance.

These professions are considered to be quite secure by banks and therefore represent a low risk of a borrower being unemployed for a long period of time. This is crucial to bank credit managers.

If you do work in one of these fields, it could help you to save thousands of dollars in mortgage insurance.

For example, if a borrower was a surgeon purchasing a house for $900,000 with a 10% deposit, he would be able to save over $15,000 in mortgage insurance, as opposed to a borrower who didn't work in the medical, legal or accounting fields.

If you do fit into this category, it's important to remember that currently only a handful of banks do offer this.

It's important to shop around and look at a number of options from your broker to ensure you have the right lender for you.

If you're like most of us, however, and work in a field of employment other than the above, you are part of the majority and there is certainly no reason to despair.

Using a Guarantor for your Purchase

It is important to understand how using a guarantor works, as it can be a great way to avoid having to come up with further savings.

Instead of being required to have savings and putting a deposit together yourself, using a guarantor involves using someone else's property, usually a family member, and using equity in their property for the bank to hold as security.

This way, the bank is not lending the full amount against the value of the home you are purchasing. The bank also has equity in another property to rely on, so should you not be able to make the repayments, the bank has another property to seek to recoup the money lent.

For example, if a couple looking to purchase a property for $500,000 had $10,000 in savings they would be short of the required 5% deposit and as such, on their own would be unable to purchase the property.

If however, they had parents who were happy to provide their property for the bank to use as security, then the bank would take a hold against the property the clients are purchasing for $500,000 and they would also take a hold against the property that the parents are providing.

Note the bank would assess the eligibility and equity position of the guarantors to ensure the loan was not likely to place them in financial hardship.

The benefits of using a guarantor:

A. You can avoid mortgage insurance if there's sufficient equity in the guarantor’s property.
B. It also may enable you to obtain a better interest rate, because the bank isn't taking out mortgage insurance for your loan.
C. You don’t need to come up with a full 20% deposit.

The disadvantage to using a guarantor is that there is another property involved. Your family member or the person providing the guarantor needs to be aware of the risks involved.

If you are unable to make the repayments, the bank will eventually sell your property, but they can also look to sell the guarantor's property should they not be able to recoup all those funds owed to them from the sale of yours.

There can also be some additional charges with using a guarantor, however, these are often no more than $500 (although these change regularly, so please double check at the time of working with your broker).

CHAPTER TWO – BORROWING POWER

In this chapter we'll address your borrowing power and specifically how banks determine how much you can borrow based on your income and your expenses.

It's another crucial step in the approval process, as it determines how much the bank will lend to you and consequently what property you can afford to purchase.

Getting a good understanding of your borrowing power will allow you to quickly establish the properties that are within your price range, and therefore prevent you from wasting time looking at properties that are below or beyond what you're capable of purchasing.

We often speak to people who start looking at properties before they establish their borrowing power. Consequently, they can be looking at certain properties that are more than they can afford.

Alternatively, we have clients who thought that certain properties were out of reach for them, when in fact the bank was actually able to lend them the money required to purchase those properties.

Your income is the first part the banks will use to assess your borrowing power when processing your application. Income can be broken down into one of the following categories:

- Base income
- Casual employment
- Overtime
- Income from allowances

- Bonus income
- Commission income
- Self-employed income

Approval Tip

Banks differ significantly on the amount of income they will allow that is not part of your base income.

It is best to find out well before purchasing which bank will be best for you, based on the type of income you earn.

Base income

The most common type of income that banks consider for people who are employed is base income. Base income is simply the amount of income that you receive on a regular basis for standard hours worked.

This is usually quite an easy thing to calculate for most people who work full-time or part-time. If you are paid on a monthly basis, banks simply multiply your income by 12 months to establish your annual income. This is the figure they will use for their calculations.

Casual employment income

If you are in a casual role, the banks will look at your income over a much longer period to see the consistency in your earnings. Some banks like to see borrowers in a casual role for more than 12 months.

Other banks are happier to accept a three or six month period.

Banks and mortgage lenders require a greater length of employment for casual employees, as opposed to full-time or part-time employees. This is due to the uncertainty of casual employment, that it may not continue in the future, and the uncertainty of working hours available.

Overtime income

Income earned from overtime is something that banks will usually consider in addition to base income.

This is often relevant for people in full-time and part-time roles. Banks can consider it when they can see consistency of that overtime income over a period of time.

The length of time that banks will want to see that income being earned will vary from lender to lender (usually three to six months). They will look at your earnings in the previous financial year, so they can see the consistency of your income.

We have clients who are employed as nurses; overtime income makes up a big portion of their earnings.

Understanding how much overtime income banks will allocate towards your overall income figures can be crucial, and it can have an enormous impact on your borrowing power. Often, once your overtime figure is established, banks will only use 80% of this amount.

Here's an example. Your base income is $50,000, and last year, with overtime included, you earned a total of $80,000. We assume $30,000 of your earnings was from overtime (assuming you didn't earn any income from other sources such as allowances etc.).

Because your base income of $50,000 is viewed as being reliable and consistent, 100% of this income will be used towards your overall income figure.

However, because overtime income can fluctuate, only 80% of your gross income ($30,000 x 80% = $24,000) will be allocated to your overall income figure.

It's important to note that this is the case in most instances, however, when dealing with a smaller financial institution or if you work in certain industries, such as essential services (nursing, ambulance or police, etc.), 100% of overtime may also be taken into account.

This is because people working in essential services often have their overtime as a regular part of their employment.

<u>Commission Income</u>

Commission income is relevant for people in sales roles, where their earnings are usually determined by how much they are selling or producing for the company they're working for.

Again, because this sort of income fluctuates so much, the banks may want to look at the last one to two years of earnings to try and establish what the consistent figure is over a 12 month period.

If this is the type of employment you are in, the best thing you can do is find out how much of your income the banks will allocate towards their calculations.

This way you can determine if now is the right time to purchase, or if you should wait until you have a chance to show a higher income figure from the commissions earned.

<u>Self-employed income</u>

Self-employed is defined as being one of the following:

a) A sole trader
b) A partner in a partnership
c) Trusts

Someone who is self-employed is someone who is responsible for paying their own tax (or are an owner or director of the entity which pays tax). Someone who is employed has an employer who pays tax on their behalf.

If you are self-employed, traditionally banks have always wanted to see your last two years of tax returns and financial statements (business profit and loss and balance sheet) to try and establish what your earnings are.

Self-employed income is considered the most variable and most unpredictable type of income. Therefore, banks often request 2 years of earnings to try and establish what the consistent income figure is for you.

Sole trader

A sole trader is referred to as someone who runs their business as an individual. Therefore, they themselves are responsible for all income and losses associated with the business and any tax payable.

An example of this may be a hairdresser who chooses to work from home.

They may register a business name such as "Wonder Hairdressing" and with this they will be given an Australian Business Number (ABN).

If this is the structure you use, it's quite straightforward to work out the income the banks will use; it will simply be your total income less your expenses.

Partnership

A partnership is similar to a sole trader, except it involves two individuals or more.

However, unlike a sole trader, partners will have their own tax returns, and the income distributed to each individual will be represented in their individual tax returns.

This income in your individual tax return is what the bank will use to determine your borrowing power. The easiest way to identify this figure is to look for the "taxable income" figure on your tax return.

Trusts

Trusts are entities within their own right. They usually have a trustee involved, who is in charge of the decision making in relation to the trust.

Many people will use a family/discretionary trust to trade and operate their business and then have the income distributed either directly to themselves or to a company of which they are a director.

The important thing to note with a trust is that they must distribute income at the end of each financial year – usually to a company or an individual.

A company is also an entity in its own right. Usually, if you're operating with a company structure, you will, as the majority owner, also be the director (or possibly your spouse).

It's important to note that the bank will first use the income that has been distributed to you and that is shown on your individual tax return.

Most banks will also allow you then to use the net profit that has been retained in your company (revenue less expenses) after income has been distributed to you.

It's important to understand the income figure the banks will use for your particular situation, as this will determine the amount you can borrow and the property you can afford.

Approval Tip

Often accountants will try to reduce your income figures by as much as possible to try to decrease the tax payable at the end of the financial year.

While this is a great strategy to reduce your overall tax bill, it can go against you when you apply for finance approval.

If this sounds like your situation, I suggest speaking to a broker about what your income figure needs to be for the loan you wish to apply for.

Then work with your accountant to see how you might be able to demonstrate this level of income.

While most banks do require two years of tax returns and financials, currently some banks are looking only at your most recent year's income, which can be advantageous for people who are building a business and may be experiencing growth.

Again, it would be beneficial to speak to a broker about this so they can understand which banks may be suited to you, based on what your earnings are.

<u>Other income sources</u>

For most people, the income they earn from their work will form the major part that bank's use to establish their borrowing power, however, there are other sources of income that can be used, which include:

- Rental income – from an investment property
- Income from investments (e.g. shares)

- Income from family assistance (family tax A and B)
- Other government payments
- Income from maintenance/child support

Rental income

Should you be in the position where you already hold an investment property that is tenanted, the banks will usually allocate 80% of this income towards your overall income figure. They use 80%, as opposed to 100%, to allow for expenses relating to the property and also for any period the property may not be rented.

It's important to note that if this property is owned with someone else who is not a part of your current finance application, the bank will only assign your portion of the rental income (often 50%, if you hold a 50% share in the property).

However, often banks will assign the whole debt on the property when calculating your ongoing liabilities and ongoing commitments.

This is something that can drastically reduce your borrowing power. If this is a situation you find yourself in, it may be best to see how much this reduces your borrowing power, as currently there are a few banks available who will only assign your share of the debt in their calculations.

Income from investments (e.g. shares)

Regular income such as dividends from shares or other investments can be also be considered. Again, lenders will want to see consistency in this income and will often look at how much you received in the previous year.

If you do plan to sell shares to form part of your deposit, naturally the banks won't use this as income, as that income will no longer be there in the future.

Income from sources other than shares will be considered on a case-by-case basis, and acceptance will largely depend on the reliability of this income and how long it has been received.

As with rental income, often banks will only allow 80% of the income received (or less) to be used towards your income figure. This is to reduce their perceived risk that this income may not continue in the future.

<u>Income from family assistance (family tax benefits A and B)</u>

Family tax benefits are government financial assistance provided to families who meet the criteria.

This is quite a common source of income used when applying for home loans. If you are in this situation, it's good to understand how banks view this to be aware of how it might affect your borrowing power.

Banks will often use this income but will look carefully at the age of the children in the household to establish if that income will continue for a number of years or if it is nearing completion.

In most cases, banks will allow family assistance income to be used if the children are under the ages of 13 or 14, so the lenders can be comfortable that this source of income will continue for another 5+ years (as family assistance ceases when children are 18 years of age).

Other government sources of income

Income from other government sources may be considered. They include:

1. Pension income/widow's allowance – however, banks may look closely at the age of applicants to establish if a loan is suitable, and they may look for other sources of income to support the overall income figure.

2. Disability support pension – again, this will vary from bank to bank as to whether they will use this income towards calculations. Often banks will only do so if other sources of income are present.

Child support income/maintenance

This is categorized as income a parent of a child may receive from the other parent, whom they are no longer in a relationship with and no longer living with.

If the arrangement of the income has been formalised through the Child Support Agency (CSA), this increases your chances of the banks accepting this form of income.

CHAPTER THREE – YOUR LIABILITIES

One important factor that the banks will want to understand is what loans you currently have in place, and that will exist once you purchase your new home.

Loans such as personal loans, car loans, and any other credit facilities that you're paying for on a monthly basis, will be taken into calculation when assessing what your borrowing power is.

If you do have these loans in place it's beneficial to sit down with your mortgage broker and see the workings of how they affect your borrowing power.

We often find that when people realise how significantly car loan payments of $600 a month (for example) reduce their borrowing power, they find ways to try and eliminate that debt or pay it off as soon as possible.

For example, consider the two different couples below, one couple who each have a car loan and the other who do not.

	Couple 1	Couple 2
Income for each applicant	$75,000 each	$75,000 each
Number of children	2	2
Credit card limits	$20,000	$20,000
Car loan repayments	$677/mth (x2)	$0
Maximum borrowing	$602,043	$800,233

***Note the above is an estimate and car loan repayments are based on a loan balance of $35,000, interest rate of 6% p.a. and term over 5 years. Borrowing power has been determined using calculator from the Commonwealth Bank. Note, when you apply for a loan your own living expenses will be assessed and as such your borrowing power will likely differ to the above.*

A lot of banks will also insist on seeing statements on your current loans.

The reason for this is that they want to ensure that you've been paying the loans on time.

If you can show this to the banks it helps strengthen your application and increase your chances of a fast approval.

Approval Tip

Any late payments on your existing loans will go against you greatly when it comes to assessing your application.

If you can ensure that repayments for existing loans are on time for the 3 months before submitting your application, this will enhance your chances for a quick approval.

Credit Cards

Like loans that you have in place, your existing credit cards are something the banks will want to review.

Again, if you can get a good understanding of how the bank will view your credit cards, it's a great way of understanding how you can maximize your borrowing power.

An important fact to be aware of is that banks actually work off the credit limit of your credit card, not the balance.

We've found that this is something that most people aren't aware of, and that when they do, they realize that it is actually very easy for them to reduce their credit card limits and thereby increase their borrowing power.

Consider the following applicants' circumstances.

	Applicant 1	Applicant 2
Annual income	$100,000	$100,000
Living expenses	$3,000	$3,000
HECS	$200 per month	$200 per month
Credit card limit	$20,000	$0
Max. Borrowing	$727,000	$815,000

***Note the above is an estimate. Borrowing power has been determined using calculator from the Commonwealth Bank. Note when you apply for a loan your own living expenses will be assessed and as such your borrowing power will likely differ to the above.*

In this instance, having a credit card with a $20,000 limit available reduces the applicant's borrowing power by $88,000.

This is regardless of what is owing on the credit card. The limit will be the only amount the banks refer to in their calculations.

As with personal loans or car loans, banks want to see statements on your credit cards, to check you're not spending over your credit card limit.

They will strongly penalize you for any missed payments if you spend over your credit card limit, which can in itself be enough to decline your application.

And this would mean you may have to wait another 3 months before applying.

We recently assisted one couple who were looking to pay out their credit cards and personal loans by increasing their home loan and thereby reducing their total repayments.

They weren't aware there was an account they had that they were overdrawing on. When they realised this, they noticed they were being charged fees of $10 each per month.

As such, they needed to wait 6 months before submitting their application, to ensure that the payments were now up to date.

Had we submitted the application initially, it most certainly would have been declined and this would have made it much harder for the couple to obtain a loan from that bank next time around.

It's also good to be aware that when you do apply for a credit card it shows up as an enquiry on your credit file. This is your credit report that all lenders can see and will view whenever you make a home loan application.

The banks use this as another method of scoring your application. Therefore, every time you apply for a credit card, an enquiry goes on your credit file, that will then be reflected in the score the bank gives you.

If you have too many enquiries on your credit application, this can go against you. If you can limit the number of credit cards you hold and apply for, this will greatly enhance your chances of approval.

Approval Tip:

It’s best to keep your credit card limits to a minimum, as this is what the bank uses to calculate your borrowing power.

It’s also best to keep the number of credit cards to an absolute minimum. The fewer credit cards you have, the greater score the bank system will give you and the greater chance for a quick approval.

CHAPTER FOUR – STABILITY AND CONDUCT

Stability and conduct refer to

1. Your level of experience in your current employment.
2. How your conduct has been on your existing loans and accounts.

With regard to employment, banks do vary on this, but understanding how long you need to be in your job is another crucial step to ensuring the success of your finance application.

Most banks will want someone working full-time to be in their current role for at least 3 to 6 months.

However, if your previous place of work was in a similar industry and position and you have extensive experience in your field, this requirement may be reduced to as little as 2 weeks.

Currently some lenders only require your first pay slip to provide an approval (regardless of whether you are on probation), assuming you are in a permanent position.

This is similar for people in permanent part-time roles. If you're in a casual position, banks will want to see you in your role for a longer period of time, due to the greater uncertainty that comes with casual positions.

We were recently working with a client who was in his role for only 2 weeks (full-time position), who had found a house that he wanted to buy.

He was quite unsure whether he was going to be able to get approval, but we were able to align him with a bank that accepted his income when they could see that his work role, in IT, was very similar to work he had done previously.

That gave the bank the confidence that he was likely to be successful in his current role, but if things didn't work out and he was forced to find a new job, he had the experience that would assist in finding new employment quickly.

Banks generally require applicants who are self-employed and business owners to be in that role for two years.

The reason is that a large number of people who go into business for themselves aren't successful. Starting a business, or working for yourself, is very challenging, particularly if you're in an industry that is new to you.

For this reason, if you're able to show consistent income for a two-year period, this gives banks confidence that you should be able to sustain, if not grow that level of income for yourself.

If you are in a self-employed role for less than a year, there may be some non-bank lenders who can assist with finance, but this will often come at a higher interest rate.

If you are self-employed, or the owner of a business, again it's good to be able to plan ahead and get an idea of

A) How long you need to be in your role; and
B) What your earnings need to be in order to obtain approval.

This way, when you do come to make your application, you're prepared and the whole process will be a lot easier and more straightforward.

Finally, conduct on your accounts is of great importance in determining the success of your application.

The banks will review statements on your everyday accounts and your existing loan accounts, to make sure

A) they're up to date and you've been paying them on time; and
B) you haven't spent over the designated limit.

Banks do not like to see overdrawn fees, or that you've gone over your limit on a credit card or personal loan. These can be enough for your application to be declined.

So, if you do have any overdrawing fees or are late on any payments, or over your limits, it's best to wait for 3 to 6 months, when you can show a clean history of all your accounts being in order.

This will help your application score much better when applying for loan approval.

Your credit history is also something that will be important for banks to review. To do this, they review your credit file, which gives them a view of any finance applications you've made in the past.

It also shows them any defaults, judgements, or bankruptcies that have occurred on your credit file in the last seven years.

If you do have any defaults on your credit file, it's best to speak to your broker to get an understanding of how the banks are going to look at these.

If they are less than a thousand dollars, this is something the banks may be able to look past, depending on the size of your deposit.

Everyone's situation will be different in this regard, and there also may be other non-bank lenders who can assist, often at a higher interest rate.

If you have been bankrupt, most banks will, at the very least, need you to be discharged before lending you money again. You may find the provider is a non-bank lender, who has a higher interest rate due to the perceived higher risk.

If you are unsure about how your credit file might look, you can visit www.mycreditfile.com.au to obtain a copy so you can review with your broker prior to submitting your application.

Purchasing Costs

Purchasing costs refer to all costs that are involved when you purchase a property. Stamp duty and mortgage insurance (if applicable) are the most significant costs you will have to consider.

Stamp duty is simply a tax that is payable when purchasing property. There are also other fees to consider, such as transfer fees, mortgage registration, and your own legal fees.

The bank may also have an application fee you need to factor in as well (these usually range from $100 to $600).

One important thing to note is that you will usually have to cover the purchasing costs when buying property; this is not something that can be added to your loan.

So, if you are purchasing a property for $500,000, you have $100,000 saved for a deposit, and the purchasing costs are $15,000, your contribution towards the property will be $85,000 and you will require a loan of $415,000.

Overleaf are some examples of what the purchasing costs may typically be.

It's important to note that currently in Queensland there is no stamp duty for existing house purchases up to $500,000 for first-home buyers.

For purchases between $500,000 and $550,000, a discount will be available.

Above $550,000, there are no discounts provided for first-home buyers.

Purchase Price	$500,000	$650,0000	$800,000
Stamp Duty	$0 – if first-home buyer $8,750 – if not first-home buyer	$15,100	$21,850
Transfer Fees	$1,307	$1,832	$2,357
Mortgage Registration	$187	$187	$187
Conveyancing Fees	$2,000	$2,000	$2,000
Total	$3,494 – if first-home buyer $12,244 – if not first-home buyer	$19,119	$26,394

**** Please note, costs above are based on property purchases for the state of QLD, Australia. They are subject to change.*

We recently had one couple who decided on the type of loan based solely on the lowest repayments.

Unfortunately, they didn't ask the above questions and chose a loan that was interest only. They weren't reducing the principal on their home loan. Several years after being in their home, whilst they were managing their repayments comfortably, they hadn't reduced the debt on their home loan.

They had been paying interest only, every month. After going through the questions to identify the best loan type, they were aligned with a home loan that was principal and interest every month.
This allowed them the capability to pay off their loan ahead of time should they have additional funds to do so. Two years later, the couple has now reduced their home loan and are well on the way to owning their own home before they retire.

SECTION TWO – LOAN TYPES

CHAPTER FIVE – CHOOSING THE RIGHT LOAN

In this section of the book we look at the different loan types that banks and mortgage lenders offer.

Most banks offer the same types of home loans, so that makes it quite easy to compare them.

To understand the right type of home loan for you we have designed a series of questions to ask that allow you to follow a process of elimination.

If you follow this process, you will have the right type of features you require, and you will also avoid paying for any features you don't need.

Question 1
The first thing to establish is whether you're buying the property to live in or as an investment.

This will determine the interest rate you receive. In Australia, owner-occupied loans (loans for people residing in the property) currently have a lower interest rate than investment loans.

This is due to some of the restrictions that have been put on banks in recent times, with regards to the amount of investing lending they're able to provide.

Question 2
Once you determine the purpose of the loan that you're looking for, the next step would be to ask yourself how long you intend to be in the property.

If you only intend to be in the property for a few years, you don't want to have a loan that has large exit fees if you need to pay it out early.

Question 3
The next question would be what features are you likely to require. To

understand what features you require, first ask yourself how quickly you intend to pay down the loan.

If you are in a situation where you only want to make minimum payments for a period of time, a fixed-rate home loan may suit you.

A fixed-rate home loan has an interest rate that is locked in for a period of time, usually 1 to 5 years, and for that period your repayments and interest rate will not change.

Fixed-rate loans are also quite restrictive in that there are often large break fees if you pay them down or close them completely whilst still in the fixed-rate period.

This could be because

a) You have sufficient funds to payout your loan.
b) You refinance your loan.
c) You sell your property and close the loan.

So, if you are looking to close your loan within 5 years, it may not be wise to take a fixed-rate loan.

A variable-rate home loan, however, has an interest rate that can move up or down, and as such so will your repayments, usually.

If, however, you are looking to pay off the loan ahead of time (via making extra repayments) a variable-interest rate loan will usually allow you to do this – as opposed to fixed-rate loans, which often come with restrictions on the extra amount you are able to pay towards your home loan.

By paying a small amount extra every month you can pay your home loan off well ahead of time.

For example, if you have a $500,000 loan at an interest rate of 4% p.a. and you were to pay an extra $400 per month, you would save $96,119 in interest and 7.2 years on your home loan. Owning your home 7 years sooner could provide a lot of freedom and choices for you to make about your future.

Variable-rate loans also have a redraw facility.

A redraw facility simply allows you to access any extra payments you have made on your loan, and you can use these funds at your discretion.

It's important to remember that a redraw facility is only on extra repayments you make, not the minimum payment that is required.

Question 4
Do you require an offset account? Within some variable-rate home loans, there is also an option to have an offset account.

Offset accounts work whereby the money you have in your everyday account reduces the amount of interest you pay on your home loan, by the amount that is in your everyday account.

For example, if your home loan is $500,000 and $10,000 is in your offset account, you would only pay interest on $490,000.

It's important to note that a basic variable loan, which most banks offer, will allow you to make extra payments and redraw, whereas a fully packaged loan or professional package will allow you extra payment, redraw and an offset account.

However, these loans will often come with an annual fee. So, you need to weigh up how much benefit an offset account will give you and if it's worth paying that ongoing fee.

Line of credit home loans are another type of loan you may come across.
These types of loans usually come with a higher interest rate and are often designed for investors.

They allow people the ability to set a limit on their credit facility and then access those funds at any time. This often suits investors who may wish to access funds quickly for share investments or to purchase another property.

The table below provides a summary of all loan types.

	Basic Home Loan	Standard Variable	Professional Package	Line of Credit	Fixed
Application Fee	Yes	Yes	No	Yes	Yes
Redraw Available	Yes	Yes	Yes	Yes	No
Extra Repayments	Yes	Yes	Yes	Yes	Restricted
Ongoing Fees	In most cases	Yes	Yes - Annual	Yes	In most cases
Available for Construction	Yes	Yes	Yes	No	No
Offset Account Available	No	Yes	Yes	No	No
Reduced Fee Transaction Account	No	Yes	Yes	No	No
Maximum Loan to Value Ratio	95%	95%	95%	90%	95%

Interest rates

Interest rates are the rate at which the bank will charge interest on the money they lend you.

If you can understand interest rates, you can compare home loans and also get an understanding of what you are to repay each month.

Interest rates are influenced largely by the Reserve Bank of Australia (Australia's Central Bank, owned by the Australia Government), however, banks are free to issue interest rates at their own discretion.

Bank profits come from people who put their savings with them, in the form of deposits. Banks then lend these funds out at a higher interest rate than they themselves are paying.

For example, a bank may pay an individual who has savings with them an interest rate of 2% p.a., then lend that money out to people as loans, such as mortgages, at an interest rate of 4.5% p.a. This 2.5% difference contributes to the bank's profit (along with fees and charges that may apply).

Interest rates are certainly not something to be intimidated by. The main decision you will need to make regarding interest rates is between

A) A variable interest rate home loan, which can move up and down at the bank's discretion and is usually dictated by the current state of the economy, or

B) A fixed interest rate loan, which is locked in for a period of time. In Australia that's usually 1 to 5 years.

Whilst interest rates are currently very low, variable rates back in the 1980s were as high as 18% p.a. More recently, during the Global Financial Crisis, they reached 9% p.a. in some cases.

Currently, interest rates sit closer to 4% p.a, and for this reason it makes sense to see what the effect would be on your repayments if interest rates started to increase.

SECTION THREE – LENDER

CHAPTER SIX – UNDERSTANDING BANKS

Understanding banks and mortgage lenders, the providers of home loans, is a major piece of the home-loan process and is addressed in this section.

The greatest advantage a mortgage broker provides for you is that they can bring a range of banks and mortgage lenders for you to choose from.

Whilst it can seem overwhelming initially, given there are more than 25 banks and mortgage lenders to choose from, by following the Newbridge 4 L's of lending you can understand

a) Your level – made up of your deposit, borrowing power and stability/conduct.
b) The correct loan type for you.

It then becomes a process of elimination as to which lender will be right for you, based on

a) Banks that you will qualify with (for the loan amount required) and;
b) Banks who offer the most competitive mortgage for the type of loan you require (taking into account fees and interest rates).

Currently, the home loan market is very competitive, and banks are often jostling to attract new home-loan customers.

Therefore, the bank that has the lowest interest rate will vary from month to month, so it's crucial that you see a broker to get an idea of who is providing the lowest interest rates (for the type of loan you require) at the time that you're making an application.

Banks and mortgage lenders

Major banks

The big four banks in Australia (Westpac, NAB, ANZ, and the Commonwealth Bank) have the major market share for home loans.

A lot of people have accounts with one of these banks and therefore it's a natural choice to first speak to them about a home loan approval. Unfortunately, by only seeking one provider, people are often paying a higher interest rate than is being offered elsewhere by other institutions. One client had been banking with one of the major banks for over 15 years and their interest rate was over 1% higher than was being offered by other institutions.

After rearranging their home loan, we were able to move them to a lower interest rate and a saving of over $700 per month or $8,400 per year.

A major bank is popular for some people, as there is a perception of certainty and safety with large institutions. They also offer the convenience of having a branch network throughout Australia.

However, as banking becomes more digital and accessible via the internet and apps on smartphones, this becomes less of a necessity for the majority of people.

Second-tier banks

Other banks that exist are often referred to as second-tier lenders or second-tier banks.

A number of these are actually owned by major banks and a number are publicly listed on the Australian Stock Exchange. These include (but are not limited to) Suncorp, St George, Bankwest, ING and Macquarie Bank.

Whilst it may be convenient to stick with ANZ (for example) if you've been banking there for a long time, it's not a guarantee that ANZ will offer you a better interest rate or lower fees than other providers, just because of your history with them.

Because of the number of home-loan applications that banks receive daily, they treat each application on its own merit and score each application accordingly.

Very little benefit is given to people who have history with that particular bank, with regards to obtaining a lower interest rate or lower fees.

Therefore we recommend shopping around, speaking to a broker, and seeing what all your options are from a number of banks, rather than just going directly to your bank.

Credit unions (customer-owned institutions)

Credit unions have also become a popular choice for people.

A credit union is an institution that exists to benefit its members (customers).

They are not listed on the Australian Stock Exchange, and any profits generated by a credit union go back into improving the organisation itself.

Some current examples of credit unions are People’s Choice Credit Union, Credit Union Australia and Gateway Bank.

Because they don't need to provide dividends and returns to shareholders, credit unions can offer very low and competitive interest rates.

Many of them also have a branch network and therefore are worth considering when applying for a home loan.

Non-Bank Lenders

Finally, non-bank lenders are another option.

These are lenders existing with just an online presence (no branch network). They provide loans to people but do not hold a banking license. They are still tightly regulated by the Australian Securities and Investment Commission (ASIC).

Non-bank lenders are privately owned; rather than sourcing funds to lend out from savings placed with them, they obtain money from other large finance institutions.

Some of these currently are Bluestone Mortgages, Pepper Loans, loans.com.au and La Trobe Financial.

Many of them offer home loans to people who are not able to get approval with banks or credit unions. Because they provide more specialized loans, and there is a perceived higher risk, these loans usually have a higher interest rate.

A good mortgage broker will be able to give you an idea of what is on offer from major banks, second-tier lenders, credit unions, and non-bank lenders, and find a solution that is tailored to you.

Approval Tip

Whilst it's good to shop around and see your options, it's best to get a broker to look into your options with different banks and do so before submitting an application. Every time an application is submitted to a bank, an enquiry is made on your credit file.

Too many applications with different banks can go against you on your application.

It's best to shop around and understand your options and then make one choice when lodging for approval.

SECTION FOUR – LODGEMENT

CHAPTER SEVEN – THE DOCUMENTATION

Documents generally required for banks to assess your application relate to your income, your savings and any loans and expenses that you currently have.

This is so that banks can establish exactly how much you can afford each month towards a mortgage repayment, and so they can see evidence of your existing financial commitments.

If you are aware of what documents are required, (which a mortgage broker will usually assist you with), then it goes a long way to ensuring a fast and quick approval.

If you do not have all the required documents when your application is submitted, it will delay your approval and can cause difficulties meeting the finance approval date when purchasing a home.

This in turn may mean you need to request an extension for your finance approval, and if the seller is unwilling to grant you additional time, you may lose the property to another purchaser.

Income

Income documents required are typically pay slips and a PAYG summary (also referred to a as a group certificate) if you are paid wages.

If self-employed, your most recent two years tax returns, financial statements (profit and loss and balance sheet) and notice of assessment are required.

If you have additional income from overtime allowances or bonuses, then banks may ask for further history of this income, to show the consistency of your earnings.

Expenses and liabilities

Banks will usually also want to review statements on your existing loans, such as personal loans, car loans and credit cards. These show a number of things:

- The amount of debt that is actually owing and what repayment is due each month.

- Your conduct on these accounts, i.e. have you been up to date with your repayments and stayed within the limit (particularly relevant for credit cards) on these facilities.

Deductions

Banks will want to know about any deductions that your employer is making on your behalf, usually evident on your payslip.

These may include your salary package deductions (often managed by Remserv or another provider), HECS/HELP debt (university debt), or any other ongoing commitments that you have. It's also common for banks to request statements relating to these deductions.

Identification

Banks will usually also want to see your identification, to meet both anti-money laundering laws and identification requirements.

Usually your driver's license, Medicare card, and passport will suffice in these instances.

How banks assess your application

Your broker will submit your application by completing a process (usually via an online system) which includes all your personal details, your income and expenses and a summary of your financial position.

In addition to this, your broker will provide

- Copies of your supporting documents, such as ID, income documents, documentation for any loans you currently have in place and evidence of your ongoing expenses.
- A copy of the purchase contract, if you have located a property.
- Any further documents as required, relating to your individual situation.

Once your application is received by the bank, the first step they will take is to ensure that all the documents they require to complete their assessment have been received.

They will match your income details and expenses and input that data into their calculations to establish your borrowing power.

They'll then review your savings and available funds for your deposit to make sure that you have what's required to complete the purchase for the required amount.

Valuation

If you've already located the property you wish to purchase, banks will arrange an independent valuer to conduct a report on what they believe the property is worth.

They do this to ensure that you're not paying more than a registered valuer believes to be the market value of the property.

If a bank has to repossess the property in the future (due to repayments not being made and a customer being in default) they will want to ensure they can sell the property for at least the amount they are owed.

It’s important to note that it is not a bank’s preference to sell the property if you fall behind, as it is a time-consuming and costly exercise for them.

If you do find yourself behind in repayments, it's always best to notify the bank as soon as possible, as they have dedicated teams set up to assist and work with customers in financial hardship, to ensure the best possible outcome for both you and the bank.

Banks will also have a property valuation conducted to ensure your loan remains within their guidelines.

We've often had clients whose applications have not proceeded because the valuation returned for the property they were purchasing was less than they were buying it for.

In such an instance, the application often exceeds the loan to value ratio that a bank would find acceptable, and the borrower is unable to arrange additional funds to meet the shortfall that now exists.

For example, consider the below scenario where a bank is willing to lend a maximum of 90% of the valuation amount.

***Note that we have assumed the client has already allocated funds for purchasing costs (stamp duty, etc.) in addition to their deposit, which in this instance amounts to $15,000.*

Purchase price	$500,000
Initial maximum loan to value ratio (purchase price assumed as the property value prior to valuation)	90% = $450,000
Required funds from customer at initial stage of assessment	$65,000
Valuation amount (Arranged by the bank via a registered value)	$460,000
Revised maximum loan amount available based on loan to value ratio of 90%	$414,000
Revised required funds from borrower	$86,000

As you can see, because the valuation was returned at $460,000, not the purchase price of $500,000, the bank has revised the amount they are prepared to lend from 90% of $500,000 to 90% of $460,000 = $414,000.

However, whilst the loan amount has reduced, the purchase price has not, and the borrow is now required to come up with $500,000 less $414,000 = $86,000.

Unfortunately, there isn't any way of finding out how high the bank will value the property you're looking to buy until you've signed a contract and provided that to the bank.

They require this contract to conduct the valuation. As such, if you're looking to purchase at auction, banks are usually unable to value the property beforehand. Therefore, when buying at an auction, your only option is to have a pre-approval subject to valuation in place.

There is a risk that the bank will value the property at less than you have paid for it, and you'll need to come up with any shortfall or further deposit (as in the above example).

CHAPTER 8 – THE APPROVAL

Once the bank is happy that you have met their criteria for the loan amount you are seeking, they will issue you with a pre-approval.

A pre-approval is a commitment from the bank that they are initially happy with your application, but there may still be some criteria to meet before a final approval is obtained.

These criteria may include:

a) The bank arranging a valuation on the property you are purchasing (contract of sale required for this to occur).
b) Obtaining approval from the mortgage insurer (if applicable).
c) Further documentation to satisfy the requirements before issuing formal approval.

Pre-approval will typically be valid for three months (some lenders may offer a longer period).

Having your loan pre-approved provides you with a number of benefits, including

- Having comfort in knowing what your borrowing limits are, and therefore what your price range is for properties you search for.

- Being able to suggest a shorter finance period as part of the contract negotiations, indicating to the seller that you require less time to have your finance formally approved (the only remaining step often being the bank's valuation of the property).

This shorter time frame is often very appealing for people selling and may result in your securing the property over another buyer or being able to negotiate a lower price.

If you fail to find a property before your pre-approval expires, there is usually no cost involved.

Having your pre-approval reinstated usually just involves providing the bank with your updated documents – such as payslips, bank statements and existing loan statements.

Purchasing an existing home

Purchasing an existing home (or established home) involves the following steps, typically in this order:

	Property	Finance
STEP ONE	**Sign Contract** Sign contract of sale – subject to finance and building and pest (not possible if buying at auction). We suggest allowing 14 or 21 days for finance and 5 days for building and pest.	**Pre-approval** Obtain pre approval by going through Newbridge's 4 L's of Lending • **Level** – your borrowing power and the deposit required • **Loan type** • **Lender** • **Loan application**
STEP TWO	**Valuation** Upon ordering your valuation, the bank will assign a valuer to inspect the property you are purchasing.	**Valuations Ordered** Your bank or broker will arrange for the contract of sale to be sent to your bank, so that a valuation can be ordered.
STEP THREE	**Formal Approval Required** A second deposit paid may also be required at this point (usually 5% or 10% of the purchase price), which will go towards your overall deposit.	**Formal Approval Issued and Deposit Paid** Your bank or broker will liaise with your lender to ensure all conditions of your finance approval have been satisfied.
STEP FOUR	**Settlement Booking** Your solicitor will liaise with your bank and the vendor's solicitor to book in settlement on the nominated date.	**Mortgage Documents** Your lender will send out mortgage documents once formal approval is received.
STEP FIVE	**Settlement** The settlement is attended by your solicitor along with your lender and the vendor's solicitor. You are not required to attend.	**Repayments begin** Once settlement is completed, it is important to confirm when your repayments will start.

***Note, any deposit payments you make when signing the contract at the date of finance approval go towards your overall deposit required at settlement.*

For example, let's assume you are purchasing a property for $600,000, that you are contributing $80,000 and borrowing $520,000 from the bank.

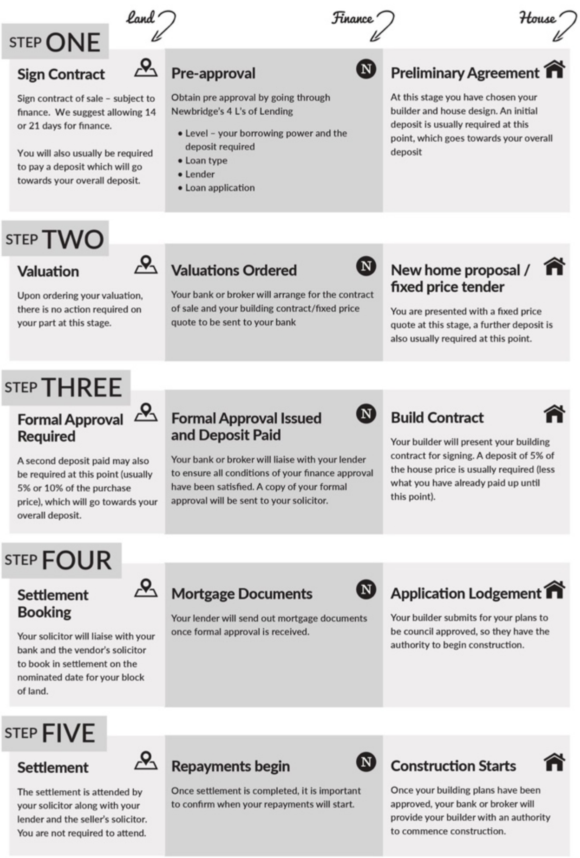
It's quite possible that you may be required to pay $1,000 on the date of signing the contract and a further $9,000 on finance approval.

As such, only $70,000 would be required at settlement, as $10,000 has already been paid by you towards the purchase.

Buying land and building

When building a new home, you have two ways to finance both the land and construction of your new home.

A) As one loan – with the land and house loan being approved in one application.



B) As two loans – one for the land purchase and one for the building of the house.

	Land	Finance
STEP ONE	**Sign Contract** Sign contract of sale – subject to finance. We suggest allowing 14 or 21 days for finance approval. You will also usually be required to pay a deposit which will go towards your overall deposit.	**Pre-approval** Obtain pre approval by going through Newbridge's 4 L's of Lending • **Level** – your borrowing power and the deposit required • **Loan type** • **Lender** • **Loan application**
STEP TWO	**Valuation** Upon ordering your valuation, there is no action required on your part at this stage.	**Valuations Ordered** Your bank or broker will arrange for the contract of sale to be sent to your bank, so that a valuation can be ordered.
STEP THREE	**Formal Approval Required** A second deposit paid may also be required at this point (usually 5% or 10% of the purchase price), which will go towards your overall deposit.	**Formal Approval Issued and Deposit Paid** Your bank or broker will liaise with your lender to ensure all conditions of your finance approval have been satisfied. A copy of your formal approval will be sent to your solicitor.
STEP FOUR	**Settlement Booking** Your solicitor will liaise with your bank and the vendor's solicitor to book in settlement on the nominated date.	**Mortgage Documents** Your lender will send out mortgage documents once formal approval is received.
STEP FIVE	**Settlement** The settlement is attended by your solicitor along with your lender and the vendor's solicitor. You are not required to attend.	**Repayments begin** Once settlement is completed, it is important to confirm when your repayments will start.

	Finance	House
STEP ONE	**Pre-approval** Obtain pre approval by going through Newbridge's 4 L's of Lending • **Level** – your borrowing power and the deposit required • **Loan type** • **Lender** • **Loan application**	**Preliminary Agreement** At this stage you have chosen your builder and house design. An initial deposit is usually required at this point, which goes towards your overall deposit.
STEP TWO	**Valuations Ordered** Your bank or broker will arrange for the contract of sale and your building contract/fixed price quote to be sent to your bank. This way the valuer can determine what your house value will be once the construction is completed.	**New home proposal / fixed price tender** You are presented with a fixed price quote at this stage, a further deposit is also usually required at this point.overall deposit.
STEP THREE	**Formal Approval Issued and Deposit Paid** Your bank or broker will liaise with your lender to ensure all conditions of your finance approval have been satisfied. A copy of your formal approval will be sent to your solicitor.	**Build Contract** Your builder will present your building contract for signing. A deposit of 5% of the house price is usually required (less what you have already paid up until this point).
STEP FOUR	**Mortgage Documents** Your lender will send out mortgage documents once formal approval is received	**Application Lodgement** Your builder submits for your plans to be council approved,so they have the authority to begin construction.
STEP FIVE	**Repayments begin** Once settlement is completed, it is important to confirm when your repayments will start.	**Construction Starts** Once your building plans have been approved, your bank or broker will provide your builder with an authority to commence construction.

The reason many people choose to progress with two loans, is that when they find the block of land they wish to purchase, they do not yet have their building contract and quote from their builder.

As such two loans are required to allow them to

a) Meet the finance date of their land contract
b) Allow time for their builder to prepare their quote and contract which in turn is then used to value the property

Note that during construction you will usually only be required to make repayments on the amount the bank has paid out to the builder.

Once you have moved in

Once in your new home, whether you have built it or purchased an existing one, repayments will usually begin one month after moving in.

They will be set up as weekly, fortnightly or monthly depending on what you selected when signing your loan documents.

Paying off your home loan can be a daunting task and it may feel like you are not getting anywhere.

Consider this, on a $500,000 loan, at 4% p.a. interest, by paying $400 extra per month extra ($100 per week approximately) you will save 7.2 years on your mortgage and $96,199 in interest.

The secret for most people who pay their home loan off ahead of time is regular consistent amounts above the minimum repayment.

Reviewing your home loan

It is certainly worth reviewing your home loan on a regular basis. This can be done by simply looking at the interest rate you have been given (usually referenced on your internet banking) and comparing this with what other banks are providing.

It's important that you compare loans that are of the same type as yours. Your broker can usually assist with this process.

We suggest reviewing your interest rate every 6-12 months.

CHAPTER NINE – FREQUENT QUESTIONS

What happens if my finance is declined?

When you make your finance application, the bank assessing it will look into your credit file, and this will show up as an "enquiry".

If your application is declined, typically this won't be listed on your credit file, so, in theory, if you were to go to another bank, they would not know that your application has been declined, only that you had made an application.

Therefore, it's often not detrimental to your chances of buying property if your application is declined; it simply means you may need to reassess and either

a) Try a different mortgage provider who is likely to look at your application more favourably, or
b) Work on improving (over time) the aspects of your application that the lender felt held you back from an approval

How are brokers paid?

Mortgage brokers are paid for introducing home loans to banks and mortgage lenders. Currently, a broker will be paid an upfront remuneration of between 0.5% to 0.75% of the loan amount.

In addition to this (but not always), brokers are paid a trailing commission of between 0.1 to 0.4% of the loan amount, whilst the loan remains in place with the lender. This is usually paid on a monthly basis.

For example, on a $400,000 loan, a broker may receive an upfront payment of 0.6% – which would equate to $2,400 – and a trailing remuneration of 0.25%, which would be $83 per month based on the current outstanding loan balance.

There are no additional fees for borrowers to pay to cover this remuneration and as such, they are not disadvantaged by engaging a broker, as opposed to dealing directly with a bank.

How long does it take it to get pre-approved?

Getting pre-approval involves the bank assessing your borrowing power and how much you can afford to borrow and repay each month.

Once submitted, it takes 2 to 5 business days for pre-approval, but it may be longer if your application is more complex or if the bank requests further documentation.

Is a fixed or variable-rate home loan best and what is the difference?

Just as it sounds, a fixed-rate home loan involves locking in a certain interest rate for a fixed period of time, usually 1 to 5 years.

The advantages of a fixed rate are:

a) It provides you with the certainty of exactly what your repayments will be for the fixed-rate period.
b) Your home loan rate is locked in at the agreed interest rate even if interest rates increase.

The disadvantages of a fixed-rate home loan are:

a) You are usually limited in paying off extra during the fixed-rate period (often $10,000 extra per year) and charges may apply if you exceed this amount.
b) Offset accounts are usually not available.
c) Large break/exit fees can apply if you end the loan within the fixed period – usually by selling or refinancing.

A variable-rate home loan is based on an interest rate that can move up or down, which is at the bank's discretion and can often follow movements of the Reserve Bank of Australia, but not always.

Advantages

a) Variable rates are usually quite flexible, allowing you to pay extra at any time and redraw on extra funds you have paid.
b) Often an offset account is available.
c) Only limited fees apply if you pay the home loan out early and ahead of time (often between $300 to $400).

Disadvantages

a) If interest rates go up, your interest rate will likely go up, as will your repayments.
b) There is no certainty as to what your repayments will be in the future.

What is mortgage insurance?

Mortgage insurance is taken out by the lender/bank when lending to a borrower who has less than 20% of the purchase price of the property.

Typically, this can be added onto the loan.

Once I purchase a property, how long until my repayments start?

Typically, your first repayment will be one month after settlement of your property.

Your repayments will then be weekly, fortnightly or monthly depending on what you have chosen in your loan documents.

When do I receive the First Home Owners Grant?

Typically, if you have your bank/broker organise the first-home buyer forms the funds will be paid on settlement of your property.

Note that at the time of writing, in QLD, the First Home Owners Grant is only available for brand new properties that have never been lived in before (either just constructed or in the process of building).

CHAPTER TEN – BUYING TIPS

I had the pleasure to interview James Freudigmann from PMC Property and Pete Wargent from Allen Wargent about what they believe are crucial things to be aware of before buying property.

They are both buyers' agents, operating in Brisbane, which means they are paid by people purchasing property to locate property and often negotiate on their behalf.

We asked them the following questions. Note, for ease of reading some answers have been amended.

Question 1: What are some of the suburbs that you think represent good value at the moment in South East QLD, particularly for an investment property purchase?

[James] We think in the Brisbane area primarily there is not much discount at this point in the cycle. For Brisbane, we think the $600,000 to $900,000 price range is a pretty good price point for investors to be going into the market for.

Specifically, if you are heading out to the west, we're looking at Oxley, along the train lines. If we're heading out to the north, we're looking around the Mitchelton area, Gaythorne, and around the army barracks, as there's always plenty of tenants in those areas. And then if we're looking to the south side of Brisbane, Mount Gravatt for bus lines, and if people really want to follow the train model, looking towards Wynnum-Manly.

[Richard] Pete, where are you finding suburbs that you think represent value?

[Pete] If you're looking for an investment property, we try to stick to the train lines, generally. Because you'll always have a ready supply of tenants, increasingly so as the city becomes denser, because people need the public transport links.

As such, in the north of Brisbane, places like Keperra and Mitchelton. To the southwest, Oxley is a great pocket, and if your budget goes a bit further, then some of those suburbs like Corinda-Sherwood, and if your budget's high enough, Indooroopilly’s a great suburb with a state high school, amenities and connectivity.

So, it depends on personal circumstances, but generally speaking, train lines and close to the city.

[Richard] James, what are three things that you think people should be aware of when choosing a property?

[James] Number one is really do zoning checks; make sure that if you're buying a character-style home that it's a character area, where the properties surrounding you aren't suddenly going to be demolished and you end up with townhouses, as this can lose the appeal.

And the feel of the street will change, and that will then play on future emotions when you have to sell the property, so I definitely think zoning checks are very important, and checking for things like easements and caveats as well is part of that.

One of the other things to really check would be the future infrastructure projects. So, are you in an area where people are going to want to live in the future?

Are you really considering the next generation? You might not be in the property for the next 15-20 years; you might only be there for 5, but you need to work out, who is your property going to appeal to when you go to sell? Because it's your home, but it is an investment property at the end of the day.

And you don't want to buy your property now and sell it 7 years on for the same value. It's just considering who the next buyer is going to be. Thirdly, I'd tell you, just really considering why you're buying, and keeping your emotions in check, I think is a really big one.

A lot of people seem to get to that stage where they get frustrated if they've been looking for a while, so I think it's really important to consider your own motives and why you're doing it and take your time.

[Richard] Pete, for you, three things that you'd suggest?

[Pete] Yeah, very difficult, as you implied, to narrow it down to just three things. I think from a holistic point of view, it's really about having a plan.

You're not just buying a property for the sake of it, it's got to fit into your life goals, it's a holistic thing. I think secondly, because money for property is often borrowed, there's a sense of easy come, easy go for some people, because it's not money that they've earned, but it's still money.

So I think, don't borrow more than you can afford, and just because the money is borrowed, still spend it wisely. And I think, thirdly, just have the exit strategy, so it is all part of the plan. And then, as James mentioned, always do your due diligence. I think it goes back to that thing, borrowed money, but it's still a big life decision.

[Richard] Pete, what would be some common mistakes that you see people make when purchasing property?

[Pete] Well I think it generally comes back to that due diligence. I think people often get buyer's remorse anyway when they buy property, but you'll definitely get buyer's remorse if something happens that you weren't expecting. So it's really making sure to cover off all of the potential unknowns, making sure that you've done all your comparable sales, as James has already mentioned.

You don't want there to be future changes in the suburb that you don't know about, certainly not adverse ones. I think the other thing as well, is just to make sure you get all of your searches and checks done by somebody who's licensed to do it.

[Richard] James, any common mistakes that stand out that you've seen?

[James] For investors, I think it's that rushed mentality. If you look at what happened in Sydney, you had a lot of investors just wanting to jump into the market.

They haven't bought something and so they just let their emotions take over. The thing is, when buying property, whether it's your home or an investment, the real estate agents are trained to bleed every dollar out of you, that's their job, and some of them do it very well.

So, if you show your emotion, the invested people are naturally going take advantage of that. We see people just get caught up, they get frustrated, they've been looking for some time, so they just want to get something done with. And because they fail to do all the checks, they end up paying a premium for the property.

The valuation might not get supported, and it can end up getting them into a lot more trouble, rather than coming out with a good result.

The other thing is, a lot of people buying are considering their own circumstances, when, really, they should be considering who's it going to appeal to?

As a home, we see a lot of people thinking, great we'll buy it for now, and they're not thinking for the future, and we're just a young couple now we're married. We're buying our first home, but we are going to have kids.

So we see a much higher changeover of the stock-standard three-bedroom one-bathroom home. If you can get a house with a second bathroom, as your family grows that becomes far more appealing to the broader markets.

I think people just considering purely where they are right now, is probably one of the biggest mistakes.

[Pete] Interesting question though, you mentioned with investment property, because there's always that rule of thumb in investment books: don't buy real estate emotionally, but in a sense that's what people actually do.

So I think sometimes, if you're looking at investment properties, I think, well, if that will appeal to me, then it's likely that it will appeal to other people in my cohort.

So yes, don't buy emotionally, don't get caught up in the frenzy, but also use some common sense; if it's appealing to you then it's probably going to appeal to similar people.

[Richard] Finally, James, any resources that you'd suggest people use before buying property, to try and help them with that planning stage of the purchase?

[James] Yeah, I think in Southeast Queensland especially, if you're planning, and doing your due diligence properly, before deciding to buy in a suburb, use realestate.com.au

I think going to the sold section and having a look at the most recent sales, is really important. Also, Open Door and Price Finder can lag a few months, so if you can get some very up-to-date market evidence, that's quite handy to have and then be able to look at those things. I also think it's worthwhile, especially for investors, considering the demographics of a suburb, which you can get through reports on realestate.com.au.

Places like SQM (www.sqm.com.au) will give you things like vacancy rates, which is very important from an investment perspective. And then also a lot of the council sites will have great information to review as well.

Here in Southeast Queensland, all of their sites have interactive mapping where you can see floods, easements, neighbouring development applications, things like that, so they're probably a few of the major resources people can look at from a due diligence perspective.

The other big one, though, is a lot of people tend to go to their mortgage broker after they've put a contract together. I think it's very important to know what your budget is, what you can afford, before you go out and start looking at properties.

We always say to our clients, go and talk to a mortgage broker, because it's probably the most pivotal part of what they're doing.

[Richard] Pete, resources you'd suggest?

[Pete] Yeah, I suppose, as a biased agent, I'm almost duty-bound to say getting access to a subscription database and checking off the most relevant information, especially comparable sales.

Queensland, more than any other state, investors are from elsewhere.

So generally, if you go around the country, the number of investors in the other states equates to the number of investment properties, but not in Queensland.

It's the one state where people buy from elsewhere, so I think there are a few things that people should understand if they're buying from interstate, that are different.

James mentioned flooding, and for Brisbane, there are some areas that are flood prone. It shouldn't put you off buying, but you do need to do your due diligence on that.

In Queensland, it's very different from the buying process in Sydney. Much more favourable to the buyer, so that's a good thing, but do understand how you can make conditional offers, conditional on your finance and your building and pest.

I think that's probably the third thing, is that if you're going to buy property in Queensland, we've got some really high-quality housing stock in Brisbane and we've got some really bad, decrepit, post-war and pre-war stock.

So do your pest and building inspections, because you don't want to pick up white ants or termites, something that's damp or something that's not structurally sound.

[Richard] Any types of properties or areas that you suggest people steer clear of?

[Pete] Yeah, it's a case-by-case basis, it depends on your strategy. If your strategy is to add value, to renovate or raise a Queenslander into something that appeals to the upgrader and the professional market, then you probably wouldn't be too scared off by certain older types of Queenslander properties.

I think if you want to demolish, then you have to be careful about some types of property that can't be removed or demolished, but it depends; if you're looking to buy at all just be wary of things like asbestos. Additionally, some types of weatherboard housing can have very high maintenance costs, so it comes back to what's your strategy.

You needn't be scared off by older housing, if your end goal is to develop.

[Richard] James, any properties or suburbs that you'd avoid at the moment?

[James] Property-wise, I think I personally love the character home.

I don't live in a character home, but I do love them, and I think a lot of people when they come to Queensland, they see character homes and go wow that is beautiful, and it's incredible the emotion that it stirs up in a lot of people.

So, I think it's really important that if you are looking for that long-term investment, for something that's going to appeal to the broader market, then traditional Queensland homes are good properties, but there is an element of maintenance when it's a timber home vs a brick home.

So, there is always going to be a bit more maintenance, but as Peter said, they are a lot easier to renovate, especially if you want to add in an extra bathroom, as all plumbing is accessible, whereas on a ground home it's much harder, and it will come at a greater cost.

But other than that, I don't think there's necessarily any homes, it really is a strategic matter, that if you like timber and you want to be able to demolish and build a new home in the future, then you might look into post-war areas, or semi-modern areas where there are single-level brick homes that you can knock over.

But if your strategy is for demolition in the future, you want to be making sure you're buying the property at the right price, without paying much for the improvements you're going to be knocking over.

If it was a $600,000 property, you'd want most of that to be in the land value and that's very important, but otherwise, I don't think there's necessarily any areas we'd be avoiding right now.

We're quite selective about what suburbs we will and won't buy in, regardless, but it's just very important to understand where you're buying, what the demographics are, what's the future appeal of that property sale, such as entertainment, education, employment and transport; they're the big ones.

Transport's probably number one. But from an education perspective, private schools are getting more expensive as well, so school categorising zones are becoming a very big thing.

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ABOUT THE AUTHOR

Richard grew up on the Gold Coast and spent his time there until completing his university studies in business, majoring in management and finance.

After travelling to Canada to spend a year on the slopes in Banff, Alberta, he accepted a role with Adenbrook Homes in a sales support position.

Through the Adenbrook mortgage-broking arm, Richard was able to see how people could benefit from having a mortgage broker working for them.

Richard then gained his qualification and became a mortgage broker himself, working for Palladium Financial Services, Adenbrook Homes' mortgage-broking business. Richard then decided to go into business for himself.

Steadily Richard has built a loyal client base over the past 15 years, and in that time has had stints working in London for Royal Bank of Scotland and Bank of America, whilst also traveling through the USA and South America.

Richard still gets great satisfaction and joy from meeting new people and helping them understand finance concepts when purchasing their first home.