Understanding FINANCIAL JARGON

HELPING YOU BREAK DOWN TECHNICAL TERMS

There are some tricky terms used throughout the home buying process that can be confusing for first-time buyers. It's important for you to understand this terminology when navigating your home ownership journey to avoid having to make changes down the track which can be costly.

KEY LOAN TERMINOLOGY

An important indicator for you to consider when evaluating the cost of a loan from different lenders is the **comparison rate**. It is a percentage rate figure that evaluates the interest rate, taking into account the fees and charges associated with the loan. For a home loan, the comparison rate is usually calculated based on a standard loan amount of $150,000 for a 25-year term. Put simply, the comparison rate is intended to help you to compare the true cost of the loan across several lenders.

Line of credit (also known as revolving credit) is a flexible ongoing loan arrangement that allows you to borrow within a specified and agreed credit limit. Like other loans, a line of credit charges interest as soon as money is borrowed. Interest is added to the loan each month up to the loan limit, or you can make interest-only repayments during the loan term while the loan is within its credit limit. Lines of credit are often used for everyday transactions to cover any gaps in irregular monthly income or for costs that cannot be predicted upfront.

Lenders Mortgage Insurance (LMI) is insurance taken out by a lender to protect itself against the risk that a borrower defaults on their loan repayments. With LMI, a lender may accept a smaller deposit than the 20 per cent usually required which can accelerate the home ownership journey.

The Loan-to-Value Ratio (LVR) refers to the proportion of the loan amount to the lender's valuation of your property. LVR is used by financial institutions as an assessment of lending risk and will typically require that LMI be obtained for the loan if the LVR is greater than 80 per cent. This is calculated by dividing the loan amount by the assessed value of the property. This means a property valued at $500,000 and a deposit of $50,000 would require a $450,000 loan, equal to an LVR of 90 per cent.

Before switching loan products, making additional repayments to your fixed rate loan or repaying your loan in full during the fixed rate period, it is important to consider **break costs**. These fees are the calculated amount of loss incurred by lenders when your repayments exceed the fixed rate repayments due during the year, or if you repay your fixed rate loan early, which are passed onto the borrower. Some lenders may allow you to make a small amount of repayments above your fixed repayments annually without incurring break costs. Make sure you are aware of these costs and understand when they would apply to your loan to avoid any unwanted fees.

Your home loan can also be linked to an everyday banking or debit account which is called an **offset account**. Any savings deposited into this account will be offset against the balance of your home loan, meaning you only pay interest on the difference between the loan balance and amount in the offset account. This may help to reduce your home loan term.

A guarantor loan is a type of home loan that allows you to rely on third party's assets as part of your loan approval. If you don't have a 20% deposit, then generally a lender may accept a third party guarantor to support you to purchase a home of your own (usually a parent

or close relative). You still need to make your loan repayments, and the guarantor accepts the obligation to step in. Should you default on your loan they may by required to make the repayments or the bank may exercise their security interest over your property (and potentially the guarantor's) in order to recover their loss.

An **establishment or application fee** is charged by lenders when you take out a home loan. This fee is charged to cover the costs of setting up your home loan and its necessary documentation.

You will receive a **formal approval** in the form of a letter where the lender confirms that they have everything needed to proceed with your home loan. This is different to a **conditional approval**, which is generally obtained earlier and is subject to various conditions.

KEY PROPERTY TERMINOLOGY

It is important to protect yourself against **gazumping** when purchasing property. Gazumping can occur when an offer you make to buy a property is accepted and the price is agreed upon, but the property is then sold to someone else who makes a higher offer. Being gazumped is not only disappointing but can prove to be costly as the agent and seller are not obliged to provide compensation for any money spent on legal advice, inspections or application costs. You can protect yourself against this by:

- Exchanging contracts with the vendor as soon as possible: Once contracts are exchanged between the buyer and seller, the sale is legally binding
- Have your loan financing arranged to avoid any delay in exchanging contracts
- Purchase at auction where gazumping can't take place.

A contract of sale is the legally binding written agreement between the buyer and seller that outlines the terms and conditions for the sale of the property. This contract is often negotiated and prepared by solicitors or conveyancers.

Conveyancing is a key part of the property buying journey. It encompasses all legal work required to prepare and finalise the sales contract, mortgage and other property related documents. When purchasing a property, you have the option to do your own conveyancing or contact either a licensed conveyancer or solicitor.

Exchange of contracts is when a contract signed by the vendor is swapped with an identical contract signed by the property purchaser. This is a crucial part of the conveyancing process as it is the stage at which the sale becomes legally binding for both parties. When contracts are exchanged, you are also required to pay the deposit for the property being purchased.

After contracts have been exchanged, it is common to have a **cooling off period** ranging from 2 to 5 business days depending on the state. This allows you to change your mind and withdraw from the sale but may incur a financial penalty calculated as a percentage of the purchase price. However, it's important to know that a cooling off period does not apply for houses bought at auction. Please note: The length of the cooling off period can vary between states as some do not have mandatory cooling off periods.

Settlement is when you become the legal owner of a home and you're able to move in. It usually occurs 6 weeks after the exchange of contracts and is when your lender disburses funds for your loan that cover the remaining sale price.