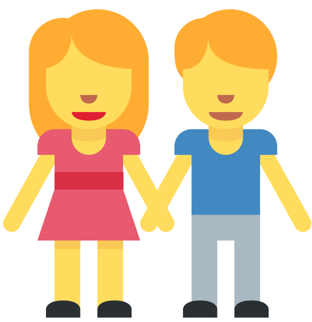

# Parental & Limited Guarantees

GETTING HELP FROM YOUR PARENTS TO GUARANTEE YOUR LOAN IS BY FAR THE MOST EFFECTIVE WAY OF BORROWING 100% OF THE PURCHASE PRICE. HOWEVER, THERE ARE MANY THINGS TO CONSIDER

## Table of Contents





# Parental & Limited Guarantees

Have you struggled to save a deposit for your home?

Getting help from your parents to guarantee your loan is by far the most effective way of borrowing 100% of the purchase price.

However, there are many things to consider when deciding whether this arrangement is appropriate for both you and your potential guarantor/s.

# Parental & Limited Guarantees

### WHAT IS A PARENTAL GUARANTEE?

A parental guarantee is where the guarantors of a loan are the parents of the borrower. As guarantors, they provide a guarantee to the bank that if their child defaults or fails to pay back the loan amount, they will cover any short fall or loss that the bank may incur.

Typically, this arrangement is by way of a security or serviceability guarantee, however in most cases it is a security guarantee. This means that the guarantors will either offer their property as security for their child's loan or offer a portion of their surplus income to pay towards servicing the loan amount.

### HOW MUCH CAN I BORROW?

With the support of your parent's guarantee, you will be able to borrow 100% of the purchase price.

This means that you do not need to evidence any genuine savings and can fund the entire purchase price through the bank loan. Additionally, you will not have to pay Lenders Mortgage Insurance (LMI) which can amount to thousands and thousands of dollars!

### HOW DOES A PARENTAL GUARANTEE WORK?

Generally, the child will not have a sufficient deposit to meet the genuine savings requirement. As a result, their parent's will be required to offer their home or property as security. This helps protect the bank against the risk of lending 100% of the purchase price.

**Example:**

Natalie wants to buy a property that is valued at $400,000. She works as a nurse, earning $55,000 a year. She does not have the 5% deposit ($20,000) that is required to meet the genuine savings requirements of most banks. Natalie's mother and father have paid off their family home. They agree to provide their home or property to the banks as security for their daughter's bank loan.

This will enable Natalie to borrow the total $400,000 needed to complete the purchase. The bank now has the parent's home as additional security for the loan, as well as the property that Natalie is purchasing. This means that if Natalie defaults on the loan, the bank can first recover the debt from her either through payment or by selling her home. If there is still any short fall that is not covered, the bank can then turn to Natalie's parent's to cover the debt.

### WHY DO LENDERS PREFER PARENTAL GUARANTORS?

Lenders prefer the parents of a borrower to be a guarantor for the following reasons:
- They have the closest relationship with the borrowers.
- They know if their child is good with money and are unlikely to guarantee the loan if they doubt their child's financial capacity.
- They know the nature of the relationship with their child and would not guarantee the home loan if they believe that the relationship might break down.
- The parents are usually in a much stronger financial position.

# Parental & Limited Guarantees

If you know that your child will not be able to service the loan or has had a history of bad credit, defaults or difficulty making timely repayments, then it is best not to enter into this arrangement.

The risk that the guarantee will be exercised is exacerbated in these circumstances. If you have any doubts, it is best to speak to our team who can better advise you.

### ARE PARENTAL GUARANTEES COMMON?

Yes! In fact, there has been a steady increase in the number of guarantor loan applications over the past few years.

Young couples and families often struggle to save for a deposit, especially with the rising cost of housing. With a guarantor home loan, there are no upfront costs to the guarantor. The risk of the arrangement is also minimised if the borrower is financially responsible. Where the borrower's financial situation is unstable, the bank is most likely to decline the guarantor loan application. It is important to consider this before lodging a parental guarantee application.

### WHAT IS A LIMITED GUARANTEE?

A limited guarantee is a type of security guarantee where the guarantor's liability is limited to only part of the home loan. As with a normal guarantor home loan, the guarantor will have a mortgage or second mortgage on their home or property from the lender as additional security for the borrowers loan. The difference is that the guarantor is not liable for the entire loan amount.

### WHEN IS THE LIMITED GUARANTEE RELEASED?

This depends on the type of limited guarantee arrangement that you have in place. If the guarantee is limited to a certain amount, it will be released once the loan falls below a certain percentage of the property value, say 80%. The limited guarantee is not in place for the full loan term, however it may take some time before 20% of the property is paid off by the borrower.

It is important that you get the property valued regularly to see when it reaches this level.
You will then be able to apply to the bank to have the guarantee released.

### WHAT IS A LIMITED GUARANTEE?

With the help of a limited guarantee, you will be able to borrow 100% of the property value.
There are also many other benefits, such as no Lenders Mortgage Insurance (LMI) and no upfront costs.

### BENEFITS OF A LIMITED GUARANTEE

There are many advantages of getting a limited guarantee, some include:

- Borrow 100% of the purchase price!
- The requirement of Lenders Mortgage Insurance (LMI) is waived.
- The liability of the guarantor is restricted.
- Both you and your parent's will not have to pay anything up front.

Specialist Advice Network

LIFE IS A FAMILY SPORT
GIVE YOURS AN EDGE

+07 4633 9888
www.edge.net.au
189 Herries Street, Toowoomba
info@edge.net.au