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GUARANTOR LOANS

WHAT IS A GUARANTOR LOAN?

A Guarantor Loan is where a borrower uses a guarantee from a family member to help get approval for a loan. The Guarantor offers their own property (or an investment property) as security against the borrower's loan. As a Guarantor you are then legally responsible for a portion of the borrower's loan.

BENEFITS OF HAVING A GUARANTOR

There are several reasons why having a Guarantor benefits potential borrowers:-

1. The borrower can save money by avoiding Lenders Mortgage Insurance. When a customer is borrowing more than 80% of the property's value the bank charges a fee known as Lenders Mortgage Insurance. The fee can be quite high and can mean the difference between a borrower being able to afford a loan or not.
2. The borrower is able to lend more of the property value when using a guarantor and can get into a property sooner
3. Deposit is not required – the borrower can lend 100% of the purchase price plus associated costs. Please note that it is best to have a partial deposit saved to show the lenders the borrower has the ability to save. If paying a deposit at the start it also helps release the guarantor sooner.

WHO CAN BE A GUARANTOR?

- The most common Guarantor is parents. Some lenders will consider other immediate family members such as grandparents, siblings, spouses, de facto partners or adult children
- In some circumstances it is possible to use friends but there are extra requirements which make this option take longer. The bank may also ask to see what the benefit is for the Guarantor which can be hard to prove.
- If the Guarantor has an existing loan on their property then the total debt on the property including the existing loan plus the Guarantee cannot go above 80% borrowings. The existing lender will also need to approve a new lender taking a second mortgage. This is generally not an issue.
- Most lenders will not accept a retired Guarantor. There are a limited number of lenders who do so it may still be an option

HOW MUCH IS GUARANTEED?

- The Guarantor will only be liable for a portion of the loan. The size of the guarantee is calculated by
  - Limited Guarantee = (Loan amount / 80%) – value of the purchase property
  - E.g. the borrower is purchasing a property for $285,000 and the loan will be $300,000 to cover buying costs. The calculation will be ($300,000 / 80%) - $285,000 = $90,000
- The next step is to check if the Guarantor has enough equity in their property to secure the guarantee amount. The current debt on their existing loan plus the guarantee must be less than 80% of their properties value.
  - E.g. The Guarantor still owes $150,000 on their existing mortgage. Add on the $90,000 guarantee and now the total debt secured against their property is $240,000. Their property must be valued at $300,000 or more for the Guarantor loan to be approved.

WHEN CAN THE GUARANTOR BE RELEASED FROM THE LOAN?

Standard loan terms are 30 years. Guarantors do not want to be giving a guarantee for this length of time. A standard guarantee term is between 2-5 years from when the loan is taken out. This time frame will vary depending on the amount borrowed when the loan was originally taken out, property growth and the amount of extra repayments the applicants are contributing towards the loan. If 105% of the house value is loaned then it will take longer to pay down the loan and build equity in the new property.

What needs to happen before the Guarantor can be released:-

- The property would be revalued by the bank. The total loan needs to be for less than 90% of the property value (Borrowers would have to pay mortgage insurance at this level of borrowings). To avoid mortgage insurance the loan would need to be for less than 80% of the property value
- The applicants must not have missed any payments in the last 6 months.
- If the above criteria is met then a partial release is sent to the lender and a small discharge fee is paid to release the Guarantor from the loan

WHAT HAPPENS IF THE GUARANTOR WANTS TO SELL THEIR HOME?

The Guarantor can sell their home while they are giving a guarantee. However the lender will have to agree to this and an alternative guarantee must be given. If the Guarantor does not have a new property yet quite often the lender will secure the guarantee against a term deposit that they hold for the guarantee amount. Then when a new property is purchased by the Guarantors the guarantee will be transferred onto the new property.

LEGAL & FINANCIAL ADVICE

Going Guarantor is a major commitment and so you should always seek advice from the appropriate professionals such as your solicitor before deciding to proceed. Many of the lenders will have a form for you to sign to confirm that you have either seen a solicitor or you waive you right to do this.

BORROWERS UNABLE TO MAKE REPAYMENTS

In the unfortunate circumstances where the borrower can no longer make repayments the first step would be for the borrower's property to be sold. Any remaining debt that was unable to be paid out will be secured against the Guarantors property. The debt will be in the borrowers and the Guarantors name. It is important to discuss this scenario to put a plan in place in case this should happen.

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