

# Home Financing



Paul Woodley



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Doesn't time fly by quick? It seems like only a couple of months ago I was making predictions about how the Reserve Bank (RBA) would act through 2007.

Since my last newsletter we have had a change of Federal Governments, the US sub prime fiasco has forced a credit crunch resulting in across the board increases in Australian lending rates, 2 RBA increases in cash rates (Nov 07 & Feb 08), with speculation of a March or April rise to follow. That said, all signs seem to point to a strong year for Sydney property prices (especially in the eastern, northern and inner west suburbs).

Have a great 2008 and feel free to call me any time for a chat.

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## Holiday House or Investment?

How many of us have gone on a holiday and then dreamt of buying a holiday house? But before you take the plunge there are many factors to take into account, so keep a level head and consider your options carefully.



A holiday house on the coast seems to be a growing Australian dream as we try to get away from the stresses of working in the city, as well as prepare for future retirement.

The purchase of a holiday house, however, can often be a more demanding property investment. Here is some information to help you in making an informative investment choice.

### Location

Location is always a critical factor in purchasing property, and holiday homes are no different.

Prices have soared in recent years in areas on the coast within a couple hours of the capital cities, so look a little further and choose an area that has not yet peaked and still possesses growth potential.

Ensure the area is attractive to holiday goers with restaurants, facilities and attractions nearby. There

is no point in buying a place by the beach if it's not within close proximity to those luxuries we all enjoy on holidays. Also, try to choose an area that is attractive all year round.

Don't go for areas that have been over developed and are full of brand new apartment buildings as often they will be overpriced and it will lack uniqueness.

Also check with the local council if there are plans for major developments in the near future.

### Rental Income

As the property will be rented out on a short term basis there will be times when the place will be unoccupied.

While you are searching for a particular area, make sure you find out from the local agents what the average occupation percentages are. This will help you to determine what the rental income per night/week needs to be, and whether this is within the typical rental prices of the area.

### Rental Expenses

The advantage of a holiday house is you get to enjoy it for a portion of the year and then claim expenses for the remainder of the year as tax deductions.

As prescribed by the ATO, you can claim expenses such as advertising for tenants, bank charges, body

corporate fees, borrowing expenses, council rates, depreciation of items such as furniture, gardening, insurance, land tax, pest control, property agent fees, repairs and maintenance, stationery, telephone, water charges and even travel undertaken to inspect the property.

You can also deduct some expenses from the selling price, which reduces your capital gains tax. These expenses include interest, rates and trips to the property to carry out maintenance.

It should be remembered, though, that annual running costs for a holiday house can be much higher than for other property investments.

In order to attract good short term tenants you need to keep the house and its contents in good condition, as the property needs to be fully furnished.

This means replacing furniture and white goods regularly, painting internal areas, as well as the initial significant investment required on fully furnishing the house.

Therefore, in order to gain significant returns, this should be a 10 year plus investment plan.

Also don't forget that when you do manage to use the place yourself for holidaying, there will probably always be jobs to do on the place – so this is by no means a passive investment.

# Constructing Your Dream

Most of us have dreamed of building our own home. Some of us go one step further and turn the dream into reality. So, how easy is it to get suitable finance, and how does it work?

Construction loans help you purchase land, construct a residential property on land already held and/or complete the land purchase and construction. Financing a major renovation or building a new home is very different from buying a property.

A construction loan allows you to make minimum repayments until construction or renovation is complete. They do this by limiting the borrowing at each stage of construction, plus they are often interest only during the construction phase.

There are typically five loan stages.

## 1. Pre approval

The first step is to arrange suitable finance, which is where I come in.

I will need a clear understanding of your current financial position and future plans.

I can then assess the numerous lenders and loan products to help you select a suitable home loan.

I will then help you to complete the application forms and collect the supporting documents, and submit it on your behalf to your chosen lender. The lender will assess the application and hopefully give a conditional approval. When this approval is received, you are ready to purchase the land and start construction.

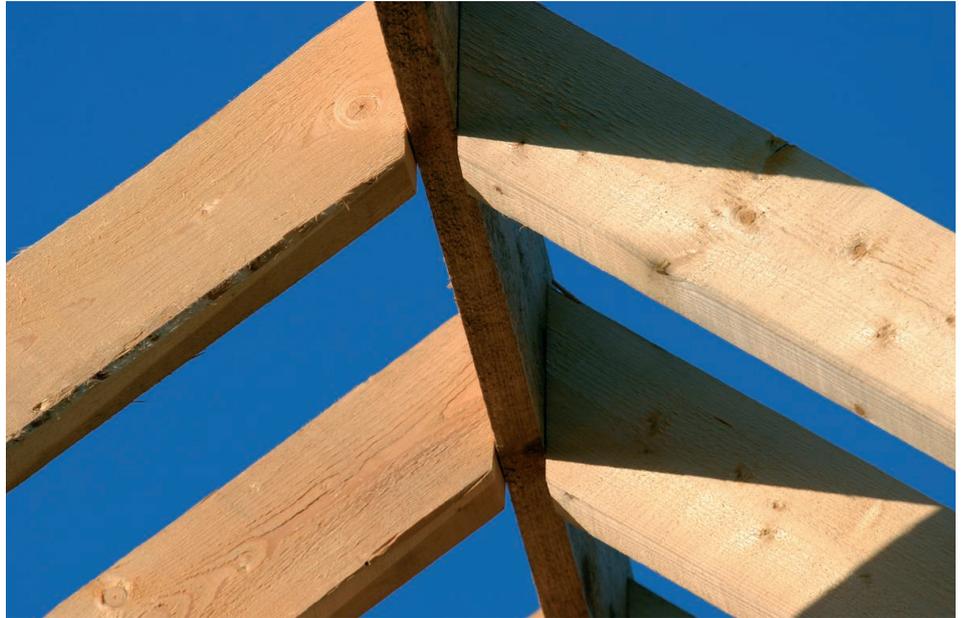
## 2. Land purchase

Selecting and purchasing suitable land is a critical step. A mistake here will cause major problems during the construction stage, so proper site investigations by properly-qualified professionals is a must.

Normally, lenders will allow up to two years from the initial purchase of the land to complete construction, and sometimes only 12 months.

## 3. Builder Selection

Allowed construction periods generally are not longer than two years. In order to grant a construction home loan a lender normally requires a fixed price contract from a licensed builder; council approved plans and specifications; written details of any work to be carried out by you, or your family, friend or sub-contractors; and proof of current builders' insurance.



## 4. Construction Starts

Funds are drawn down as the builder completes various stages of your home. Your building contract should nominate the number of progress payments for the construction, but there are typically four:

- When concrete or timber flooring is laid
- When the framework or walls are up
- When the house reaches lockup stage
- On completion

Lenders normally get involved in the management of the project. For example they will set up a schedule of progress payments for paying the builders.

They will also organise the progress payments to be made after each stage of building, once it has been independently inspected and verified by an independent expert (eg professional valuer) that the builder has reached certain objectives and met satisfactory standards. This protects the borrower by ensuring the builder isn't getting paid for work that has not yet been completed.

Note that each "Stage Inspection" will normally incur an additional valuation fee. Also each drawdown of the stage payment can also incur a drawdown fee from the lender.

## 5. Construction Complete

Once the property is built, the loan will normally revert to a standard principal and interest variable loan, although they can be set as a fixed interest loan as well. In fact lenders prefer to work this way, as it allows them to set up the entire approval process for you from the outset, and ensures that they "keep your business".

### Benefits of a Construction loan

Whilst the process can seem complex, it is worth remembering the benefits of a construction loan:

It usually operates as an interest only loan until construction is completed, and only gets drawn down (ie borrowed) in stages.

You provide invoices to the lender who controls payments to the builder.

The lender provides an expert to monitor construction and approve progress claims.

### Conclusion

If you are thinking of building your own home or an investment property, there are many products and lenders ready to help you. Get in touch with me and I'll help you find the best construction loan for your circumstances.



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