Guarantor Loans

What is a Guarantor?

Many lenders will allow a related third party to provide additional security to help a family member buy their own home. The person providing this assistance is known as a Guarantor.

The Guarantor is not included on the loan, instead they are linked to the loan by a guarantee. This guarantee can be released and the Guarantor's responsibility ceased without the loan being repaid in full.

Borrowers must be able to service the entire loan on their income alone.

How does it work?

A Guarantor allows the equity in their own property to be used as additional security for the loan. The primary security will be the property being purchased by the borrower. The lender will also take a mortgage over the Guarantor's property in lieu of a cash deposit.

Who can be a Guarantor?

Guarantor's are typically limited to immediate family members. Most commonly this is a parent, however siblings and grandparents are also able to act as Guarantor.

How will having a Guarantor help?

Having a guarantor may allow homebuyers who have insufficient deposit, but have the ability to make the required repayments, to secure additional funds to purchase a home.

Saving a deposit can be a long road for many, especially if you are also paying rent. By having a Guarantor, the borrower may be able to borrow the full purchase price, as well as the costs associated with purchasing property. This varies across lenders and some may still require you to contribute what savings you do have.

The main benefit is that the borrower may save thousands of dollars by avoiding Lenders Mortgage Insurance (LMI). LMI is payable when the Loan to Value Ratio (LVR) is higher than 80% and is taken by the lender to cover the additional risk of high LVR lending.

Although LMI protects the lender against the borrower defaulting on the loan, the borrower pays the premium.

The amount of the guarantee will depend on the policy of the lender. Typically, the guarantee is for 20% of the loan amount when the borrower is borrowing 100% of the purchase price.

After the borrower has built up equity in their property the guarantor can request to be released from the loan. Timeframes will vary depending on the original deposit saved, the number of extra repayments made and whether the property has appreciated in value over the time period.

Example of avoiding LMI with Guarantor

A borrower wished to purchase a $400,000 property and will need to borrow $380,000. The loan has an LVR of 95%, resulting in LMI.

If a family member is willing to be a Guarantor by using the equity in their own property, the LVR would reduce and avoid the need for LMI, saving the borrower approximately $12,000.

Depending on the lender, the borrower may need to pay some additional fees at the time of the request to release the Guarantor. This can include a fee to revalue the primary security as well as lender discharge fees.

What if the borrower defaults on their loan?

If the borrower is not able to pay back the loan as per the terms of the contract, the lender can take legal action against the borrower, and in some circumstances, the guarantor. The guarantor will be liable for the amount specified in the guarantee.

Anyone who is considering being a Guarantor is advised to seek independent legal and financial advice before accepting the role of Guarantor. Most lenders will insist on this.

It is important to note that a Guarantor's ability to borrow could be reduced after they have agreed to act as a Guarantor.

PO Box 49, Maitland, NSW 2320
1300 438 547 | admin@wilsonfs.com.au | www.wilsonfs.com.au
Wilson Finance Solutions ABN 21 611 779 554
Credit Representative 489286 authorised under Australian Credit Licence 389328