

Use this factsheet if you:

- want to find out about schemes that offer to cut years off your home loan

What is “mortgage minimisation” or “debt reduction”?

Some mortgage brokers and other businesses use the terms ‘debt reduction’ and ‘mortgage minimisation’. These businesses commonly make claims that you can cut years, or thousands of dollars, off your home loan. However some mortgage minimization plans are expensive (over \$5,000), and are also based on confusing and misleading information.

Mortgage minimisation plans usually involve a budget plan *and* refinancing of your home loan (and sometimes refinancing of other debts.) Most borrowers would be better off keeping their current home loan and increasing their repayments if they want to pay their loan off sooner and save interest.

How do mortgage minimisation plans work?

Usually a plan is based on creating a budget for you to follow and using a line-of-credit home loan (or sometimes an off-set account).

A line-of-credit mortgage allows you to pay any spare funds into your home loan (so reducing the amount you pay interest on). You then withdraw those funds when you want them. An off-set account works in a similar way.

A mortgage minimization business will probably tell you about the benefits of paying your salary into the line-of-credit home loan, and leaving it there as long as possible by using an interest free credit card for your expenses. The

mortgage minimization business might show you figures that illustrate how much you will save with this new plan.

Warning: It can be difficult for some people to manage a line of credit.

Don’t just accept the claims made by the mortgage minimization business!

The experience of Consumer Credit Legal Service and Credit Helpline shows that:

- The savings that come from leaving your salary in the line-of-credit account are unlikely to be very much; and
- . The additional fees and interest that are often charged on a line-of-credit home loan might exceed any savings, and
- Most, if not all, of the savings in the mortgage minimization plans come from:
 - A budget that pays a higher monthly amount to your home loan than you are currently paying; and/or
 - Where other debts are also refinanced; a budget that pays a higher monthly amount to *all* your debts over the term of the plan

You can do your own budget, you don’t need to pay thousands of dollars to someone else to do a budget!

Do I need a mortgage minimisation scheme to cut years off my home loan?

No. In most cases you do *not* need to obtain a new home loan product to reduce the term of your loan. If you have spare cash or can find spare cash by reducing your expenses, you can achieve this result by simply increasing

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Mortgage Minimization

the repayment amount on your current home loan and other debts.

Budgets set up by mortgage minimization plans

These plans free up money (on paper) by setting up a budget that reduces the amount that you spend on living expenses. The funds freed up (on paper) are then applied to the home loan.

The problem with this is that although a reduction in spending on living expenses can be achieved on paper, *in reality* these budgets are often unrealistic and sometimes impossible to stick to.

What sort of savings do I get from a line of credit home loan (or an off-set account)?

The actual savings achieved through paying income into the home loan (or off-set account) are minimal unless you earn a very high income or generally save a significant amount from your income..

Furthermore any savings achieved are often less than the fees and charges you will have to pay for your new home loan.

Generally, line-of-credit home loans and loans with off-set accounts are more expensive than basic home loans. In the April 2002 edition of Choice Magazine, an example was given of a couple with a home loan of \$250,000 and average savings of \$14,000. Even with these savings in the offset account, the couple was \$240 worse off per year than they would have been if they had obtained the cheapest basic home loan and put the \$14,000 in an electronic savings account.

Is refinancing necessary to get a 'better' loan product?

Refinancing ensures that a mortgage minimization business can take its fee (from the proceeds of the loan) and will also earn the firm, or a broker, a commission.

However, refinancing might not benefit *you*.

You should be wary of any broker or business that tells you (or somehow suggests) that it is necessary for you to refinance your home loan to achieve significant savings – furthermore the broker/business might be engaging in misleading and deceptive conduct and so be breaching the Trade Practices Act.

Debt Consolidation

Sometimes the consolidation of other debts is included in a “debt reduction” plan. See Fact Sheet #9 for discussion of debt consolidation.

Analyzing the mortgage minimization plan

These plans can be very confusing (sometimes this confusion is deliberate!). If you have been given a plan try to analyse where the “savings” are coming from.

If your home loan is the only debt refinanced:

- Identify the monthly amount allocated in the plan to pay the home loan. (Most of these plans do not specify what this amount is, you might need to work it out by deducting the estimated monthly expenses from the stated monthly income);
- Using this amount as the home loan payment, calculate the time in which your current home loan will be repaid if you paid this amount to your current loan. (You can do this with a home loan calculator such as http://www.commbank.com.au/personal/other/useful_tools.asp; or <http://www.yourmortgage.com.au/calculators/>.)
- Compare these results to the “savings” offered in the plan and check to see if there is any difference.

If the plan includes refinancing (consolidation) of other debts as well as the home loan:

- Identify the monthly amount allocated to home loan and debt payments in

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Mortgage Minimization

the plan (deduct the estimated monthly expenses estimate from the monthly income);

- Using spreadsheet software such as Excel, allocate that monthly amount across all debts, calculating when each debt will be finalised and then allocating the “spare” funds to another debt such as the home loan. (If you can't use excel, you might be able to draw this up on a chart using approximations.)
- Compare how long it will take to finalise debts against the proposed debt reduction program.

In both cases, you will usually be better off without refinancing due to the costs in obtaining the new loan, paying out your current home loan and payment of fees to the debt reduction firm.

How Can I Reduce the Term of My Home loan?

- If you don't already have a home loan, get the cheapest home loan possible; making sure that you can make additional payments without any penalty.
The “comparison rate” will give you a better idea of the true cost than the interest rate.
The cheapest loans usually don't have many features. Unless you know you will need to redraw funds, or you are sure that you will benefit from extra loan features, the cheapest loan might be your best option.
- Increase your payments.
- Pay off higher interest debts first, and when they are finalized, allocate this payment to your home loan.
- Use one of the web calculators mentioned above and find out how quickly you can pay off your home loan by making extra payments.

Free Advice & Assistance

Credit Helpline

Ph: (03) 9602 3800, or
1800 803 800 for country callers.
Mon – Fri 10am – 4pm

Free telephone advice about credit and debt matters and referral to Consumer Credit Legal Service where necessary.

<http://www.communitylaw.org.au/credithelpline>

Financial and Consumer Rights Council

Ph: (03) 9663 2000, or
1800 134 139 for country callers

To find your local financial counsellor who can give free advice and assistance with credit and debt problems, negotiating with creditors and budgeting.

www.vicnet.net.au/~fcrc

Consumer Affairs Victoria

Ph: (03) 9627 6454 Mon – Fri

Consumer Affairs can help you resolve a dispute with a trader by informing you of your rights or by conciliating with the trader.

www.consumer.vic.gov.au

Victoria Legal Aid:

Ph: (03) 9269 0120, or
1800 677 402 for country callers.
Mon – Fri 9am – 5pm.

VLA publishes a useful series of pamphlets on credit & debt issues that it will send to consumers free of charge.

www.legalaid.vic.gov.au

Federation of Community Legal Centres:

Ph: 9654 2204

To find your local community legal centre.

www.communitylaw.org.au

Insolvency and Trustee Service of Australia

Ph: (03) 9272 4800

ITSA is not an advice service but it can send information about bankruptcy and forms.

www.itsa.gov.au

Dispute Resolution

Victorian Civil & Administrative Tribunal (VCAT)

General ph: 9628 9700, country callers: 1800 133 055

Credit List ph: 9628 9790

Civil List ph: 9628 9830

www.vcat.vic.gov.au

Federal Privacy Commissioner

Ph: 1300 363 992 (Privacy Hotline)

To complain about credit reporting or other breaches of privacy.

www.privacy.gov.au/

Industry Dispute Resolution Schemes

**Banking, Insurance and Investment Assistance
1300 78 08 08.**

A central telephone number to the appropriate scheme, for disputes with:

- banks
- insurance companies (claims disputes)
- credit unions
- finance brokers
- investment advisors

Water, gas and electricity disputes

Energy & Water Ombudsman (Victoria) EWOV

Tel: 1800 500 509

www.ewov.com.au

**Telecommunication disputes
Telecommunications Industry Ombudsman (TIO)**

Ph: 1800 062 058

www.tio.com.au

Regulators

They investigate industry conduct & are unlikely to assist with individual complaints.

Australian Securities & Investment Commission (ASIC)

Complaints about conduct of financial services, including debt collection of consumer credit.

Ph: 1300 300 630

www.asic.gov.au

Australian Competition & Consumer Commission (ACCC)

Complaints about conduct of businesses including debt collection complaints. (Not complaints about credit or financial services).

Ph: 1300 302 502

www.accc.gov.au



Useful Contacts

Telephone interpreter service:

Free to callers. Available 24 hours, Ph: 13 14 50.

Hearing & Speech Impaired Access:

National Relay Service
All free calls (within Australia)
1800 555 677

Speech to Speech Relay

All local and chargeable calls (within Australia): 1300 555 727
All free calls (within Australia): 1800 555 727

You can obtain more information about the National Relay Service on their website at

www.aceinfo.net.au/Services/NRS/

Acknowledgments

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