

LOANS APPROVED

The Property Investor's Mortgage Broker

Special Report For Property Investors: **“How to Structure Your Property Loans for Maximum Stability and Control”**

Introduction

Welcome to the first part of this Special Report for property investors. It explains how to structure your new or existing loans so you retain **maximum control over your assets**.

To make this Report easier to understand and digest, I've broken it up into 4 parts. Here's an outline of how the Report is structured:

Part 1

“Crossing” of loan securities: the “fine print” on your loan documents that gives too much power to your bank and can leave you unnecessarily tied up.

Part 2

“How to structure new loans to avoid ‘crossing’”

Part 3

“Substituting security: how you may be able to get back the title to your property with one quick fax to your bank”

Part 4

“Deposits Under Lien : A powerful loan structuring strategy for freeing up security and keeping more in your hands”

Although the topics and examples in this Report give you a good overview of some important issues to consider when structuring your loans, you should also bear in mind that every situation is different. We recommend that you always seek qualified and professional advice before making any loan or investment decisions.

Successful investing,



Ed Nixon
Director
Loans Approved Pty Ltd

About the Author – Ed Nixon

Ed Nixon is the founder of Loans Approved Pty Ltd, a boutique mortgage broking firm that specialises in helping property investors arrange and structure the right loans for long term stability and flexibility.

He has been involved in the finance industry since 1991, with 12 years experience in commercial finance. In early 2003, he changed his focus to specialist mortgage broking.

Ed's area of expertise is "structuring multiple loans for continued investing". He runs occasional seminars on this subject for property investor and industry groups.

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Part 1:

“Crossing” of loan securities: the “fine print” on your loan documents that gives too much power to your bank and can leave you unnecessarily tied up.

So you have some bank loans, but have you ever considered **how** your loans are secured?

Sure, you know that the loan is secured by a residential house, but *is it secured by all the other houses in your portfolio as well?*

In other words, are your loans “stand-alone” or are they “cross-collateralised”?

Many property investors believe that their loans are stand-alone when in fact they are “crossed” with other properties.

“Crossing” is very widespread (my estimate is that up to 95% of residential property investors are affected).

So what is “cross-collateralisation”?

It used to be the way that loans were structured years ago: borrow 106% of a property's purchase price to cover all acquisition costs and secure it against another property that had enough equity.

This is called “cross-collateralisation”, and as an investor you should know that it **is not always a suitable way to borrow**. There are certain situations when

crossing is a useful vehicle, but in the vast majority of cases it offers no benefit to you.

“Cross-collateralisation” explained:

Collateral is defined as “Security used for the payment of a loan” and to cross collateralise is to use **multiple securities for the payment of a loan or loans.**

A simple example:

1. John owns Property A outright
2. John wishes to buy Property B but has no funds for deposit.
3. John buys Property B using a 106% loan and the Bank holds **both Properties A and B** as security against the loan for the purchase of Property B.

Property A & B are said to be **cross-collateralised**, or “crossed”

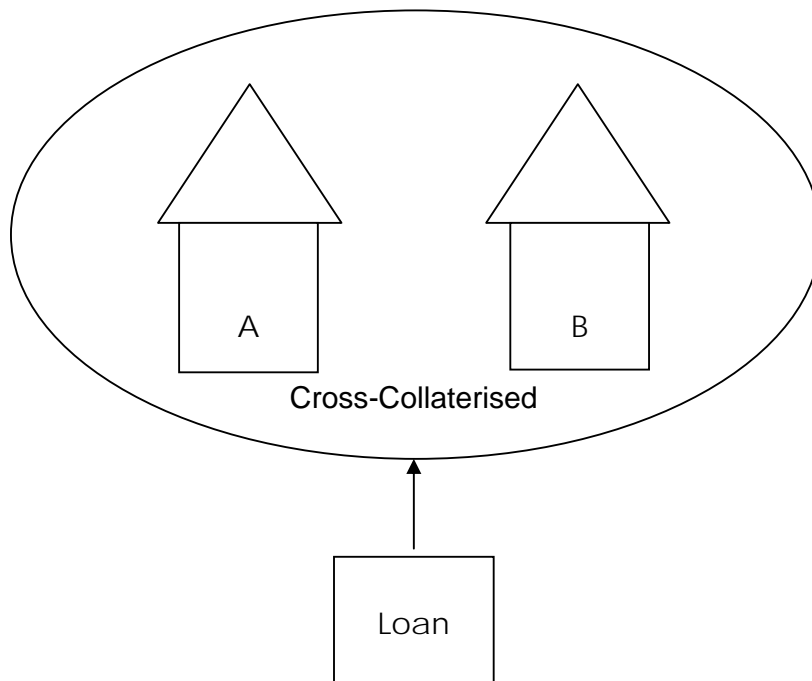


Diagram #1: Cross-collateralised structure

It all sounds fairly straightforward.

However, most investors buy subsequent properties, offering previous properties as security for the next transaction. Eventually you can end up with a “chain” of properties that are securing each of your loans. (In a moment we’ll look at the negative implications of this)

Even if you only have 1 investment property, crossing is **often unnecessary and ties you up with no benefit to you.**

So if there’s no benefit to you, why are so many loans crossed?

Because in many cases lenders **automatically** cross your loan securities, whether you realise it or not, so they can add extra strength to their position.

“How do I know if my portfolio is cross collateralised?”

The only true way to find out whether or not your portfolio is crossed is to look at your loan contract (that’s the one put in a safe place that you can never find! ☺). Have a look to see which properties have been used to secure the loan, listed under the heading, “Security”.

If there is more than one property listed, your loans are crossed.

Sidebar: The two parts of your loan documents

Remember when you signed your documents, there were two parts:

There is the **loan contract**: This is a legally binding agreement that sets out the terms, fees and charges of the loan. It’s also sometimes referred to as a “credit contract” or “loan offer”.

Then there is the **mortgage document**: This places a “dealing” or “encumbrance” over your property and allows the lender to take possession of the property and sell it if you default on your loan contract. This is registered in the registry for land titles in each relevant state.

“So what? Why should I care if my portfolio is crossed?”

Because in most cases, crossing of loans is not beneficial to you, the borrower. It favours the bank.

Cross collateralisation isn't a problem until it becomes a problem. Then untangling it can be a long, expensive and traumatising experience. You can lose time, money and opportunities as a result of cross collateralised structures.

If your portfolio is crossed, you're at the mercy of "bank policy". We have had clients come to us to help get them a loan because their bank insisted that their next loan be Principal and Interest as opposed to Interest Only, or they have been told "no more money because you're too rent-reliant". Other clients have simply been told, "we are comfortable at your current level of debt".

In many instances these problems could have been avoided if the loans had been structured correctly in an uncrossed, "stand alone" structure.

7 reasons why you shouldn't cross your property portfolio

Reason #1: You may not be able to access your funds when you sell a property

When you sell a property in a cross-collateralised structure, you may not be able to access the funds that you expected. The bank may request **some or all** of your funds to go back against the existing loans you have with them to strengthen their position. They don't need your permission at that time as they already sought this when you first accepted the loan terms.

Picture this: you're selling one of your properties for an opportunity or worse still, because you are having cash flow problems, and the bank deducts some or all of the surplus funds to strengthen their position. Where would that leave you? I've seen this happen to some very asset-strong and successful property investors. **Answer given: "Bank Credit Policy"!**

Reason #2: Unnecessary paperwork and fees when you buy or sell

When you sell a property, the bank will often require your whole portfolio to be revalued (at your cost) to determine whether the bank is exposed and/or how much, if any, of the surplus funds you can have. After the revaluation you also have to complete paperwork known as "Variation of Security".

The same occurs when you want to realise increased equity in a property that has grown in value. You may be required to get your whole portfolio revalued (possible multiple valuations instead of one – an additional and unnecessary cost).

Reason #3: Extra stamp duties when buying property interstate

If you buy a property interstate and secure it against a property in a state that has no mortgage document stamp duty, then **both** properties may be charged duty.

ACT, VIC & NT have no mortgage stamp duty.

QLD, NSW, SA & WA charge \$4 / \$1000 on the mortgage document.

Example: You have a property in Victoria with a \$200,000 loan balance and you buy an investment property in Queensland requiring a \$400,000 loan. If these two properties are crossed, you may be charged mortgage document stamp duty on the total \$600,000 loan balance, resulting in \$2400 in stamp duty as opposed to \$1600.

By not crossing you can eliminate this additional tax.

Reason # 4: You may lose product selection and control if you're with only one bank

When you take out multiple loans with one bank, the bank may insist on a crossed structure to strengthen their position. This may cause problems when you want to borrow again.

For example, the bank may say, "No more Interest Only loans for you. We want you to take Principal and Interest loans from now on to reduce your debt with us". This is quite common when the dollar value of your debt is high with one funder, regardless of your overall asset position.

Having at least two lenders lets you play one off against the other, or pick and choose other lenders, which gives you more product choice and control.

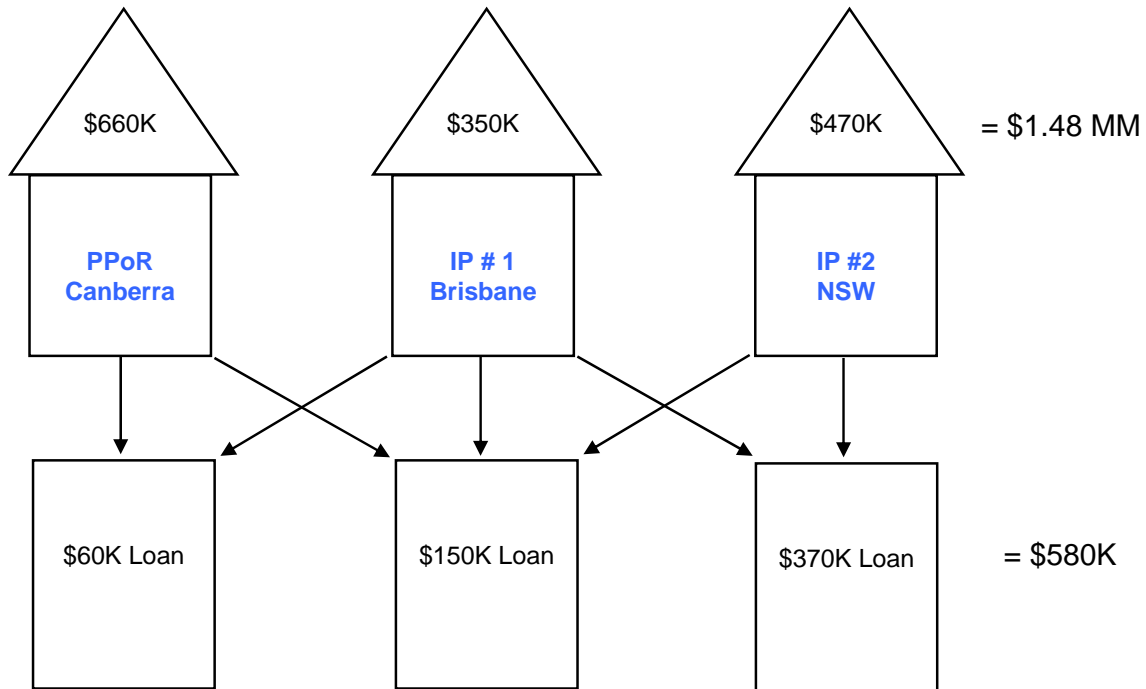
Reason # 5: The bank holds far more security than necessary

For example:

Your Principal Place of Residence is in the ACT. It's worth \$660,000 with a loan balance of \$60,000.

Investment Property #1 is in QLD, worth \$350,000 with a loan balance of \$150,000 (secured against your PPR).

Investment Property #2 is in NSW, worth \$470,000 with a loan balance of \$370,000 (secured against IP #1 and PPR).



In the example above, you can see how the bank holds \$1,480,000 of assets against only \$580,000 in loans – a **39.19% Loan to Value Ratio!** The bank holds all your cards.

Reason #6: Difficulty and inconvenience changing banks

It becomes harder to change banks if you no longer like or agree with their service - or lack of it.

If you choose to move banks, you may be subject to exit fees. These exit fees may be substantial, especially if you have fixed some of your loans. This can make it a very difficult decision to swallow.

Reason #7: Inability to revalue properties individually to obtain equity

In some cases, one of your properties drops in value and it is linked to another that has grown. In this instance, your net gains may be zero as the property values may offset each other. In an uncrossed structure, you could increase the loan balance on the property that has increased in value without the lender considering the other properties.

This happened to one of our clients:

They owned an investment property and the local fruit bats decided to roost in their back yard. Our clients were in the middle of revaluing their properties to obtain equity and this investment property was linked to another with significant growth.

However, because of the bat problem, the property's value was reduced because the valuer considered the property difficult to sell. This in turn reduced the net equity available to our clients by the bank.

Conclusion

Now you have an understanding of what "crossing" is and why it's sometimes unsustainable. In the next instalment of this Report, you'll learn **how to structure a new loan so you aren't crossed**. Expect it in your email inbox **tomorrow**.

Then in later parts, we'll discuss some strategies for uncrossing existing loans so you can avoid running into any of these problems in the future.

In the meantime, for a professional take on your situation, including how to structure your portfolio for greater stability, flexibility and control, why not take advantage of our complimentary [property finance consultation](#) for subscribers to this newsletter?

With one 10 minute chat we can usually tell you whether or not we can help. The consultation is free of cost and obligation, so [register now](#) or call **1300 657 132 to schedule a time.**

Do you know any other property investors who might be interested in this Report? Tell them about it using [this quick form](#).

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