LEARN THE LINGO

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As you are going through the purchasing and home loan process for your investment property, you will come across many terms that you may not understand.

You should ask your agent, lender or broker (if you are using one) to explain these terms so you fully understand the type of loan or circumstance you are getting involved in. Here are some common terms you may encounter:

- **AARP:** Annualised average percentage rate sometimes referred to as the comparison rate. This figure takes into account all the costs associated with the loan and may be a more accurate reflection of the true overall cost. It can therefore be helpful when comparing loan products.

- **Amortisation period:** The length of time a loan is calculated over and re-paid, most commonly 30 years.

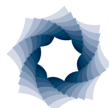
- **Appraisals/valuations:** A written report of the estimated value of a property, usually prepared by a valuer.

- **Appreciation:** an increase in value.

- **Basic variable:** A variable home loan that has fewer features and a lower rate than a standard variable loan.

- **Break costs:** The fees incurred when a loan is paid off ahead of time.

- **Body corporate:** An administrative body made up of all the owners within a group of units or apartments of a strata building. The owners elect a committee which handles administration and upkeep of the site. Owners are typically charged annual fees, used by the body corporate to pay for upkeep.



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- **Bridging finance:** A short-term loan used to bridge the gap, when someone buys a new property while selling an existing one (the loan is used until the property is sold).

- **Building approvals:** The approval to build a number or type of dwelling/s in a given time frame.

- **Capital gain:** The amount by which a property has increased in value, relative to what you paid for it. A property previously purchased for $200,000 that is now worth $350,000, has made a capital gain of $150,000 (before costs).

- **Cash rate/bank rate:** The cash rate is the money market interest rate, set by the Reserve Bank of Australia. The cash rate has a strong influence on bank rates, which are the interest rates charged by banks on their loans. Bank rates are always higher than the cash rate so banks can make a profit on their loans.

- **Cash flow positive:** A cash flow positive investment is one where incomings exceed outgoings, after tax has been calculated. For example, a positive cash flow property is one where the rent received is higher than the loan repayments and costs of owning the property (such as insurance, property management fees and maintenance).

- **CGT (capital gains tax):** CGT is charged on capital gains made from investments, including property. The amount of CGT payable may depend on factors such as how long a property has been owned and whether it is considered the owner's primary place of residence.

- **Conveyancing:** The process that legally transfers property ownership from one entity to another.

- **Cooling-off period:** A period of time given to the purchaser to legally withdraw from buying a property. The length of time varies in each of the states and territories. Some states such as Western Australia do not have a cooling-off period.

- **Credit report:** Before you apply for a home loan, you should obtain copies of your credit report so you can check for errors, see how much money you owe on credit cards and loans and to see what your credit score is. This is another way lenders will determine if you will receive a loan.

- **Cross-securitisation/cross-collateralisation:** When a financial institution uses your property (whether owner-occupied or investment) as security for another property you purchase.

- **Debt to income ratio:** This is one way that lenders will use to determine if you can afford your monthly mortgage payments on your current income. The lender will subtract all your reoccurring debt to determine how much is left for a mortgage payment. This is why not buying a car or spending money on your credit cards is so important when buying a home. The less debt you have will mean more available money for your mortgage payment.

- **Default:** Failure to pay a debt by the due date.

- **Density:** The level of occupancy in a given area, or the number of people permitted to reside in an area. For example, inner-city areas are usually higher density than outer-suburban areas.

- **Deposit:** Is the amount of money you are prepared to pay upfront to secure a property. A deposit is helpful in several ways. It will lower the amount of money you will need for a home loan, it will allow lenders to see that you are responsible for paying off a mortgage and it will move the home buying process faster.

- **Depreciation:** A decrease in value. In accounting terms, depreciation refers to the 'writing down' of the original cost of an asset, systematically over an extended period.

- **Equity:** The difference between the value of a property and its mortgage. A home worth $400,000 with an outstanding loan balance of $250,000, has equity of $150,000.

- **Fittings:** Installed items that may be removed from a property without causing irreparable damage. An example is a fridge.

- **Fixtures:** Those parts of a property affixed to structures or land, usually so they can't be removed without causing damage. An example is a built-in wardrobe.

- **Fixed rate loan:** A loan that has an interest rate fixed for a specified term, typically between one and five years.

- **Interest-only:** A loan where the purchaser only makes repayments on the interest charged and not the principal (i.e. the purchase amount). Investment loans are generally structured as interest-only.

- **Joint tenants:** Each owner has equal shares and rights in a property.

- **LMI (lenders mortgage insurance):** Usually required by lenders when someone is borrowing more than 80 per cent of a property's value. It provides insurance to the lender in case the borrower defaults on the loan and it is an additional cost to the borrower.

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- **LOC (line of credit):** A facility available from financial institutions that provides the borrower with a line of credit facility that can be drawn down at any time. It's similar to a credit card, although a LOC doesn't require set repayments of the principal.

- **Low doc loans:** These are loans that don't require as much documentation to set up as a traditional loan (such as proof of income, assets or liabilities). They are popular with self-employed people and those who have not yet established a credit rating for the purposes of borrowing.

- **Lower quartile:** The price point below which 25 per cent of sales were recorded. If there were 100 sales in a suburb, the 25th lowest price would be the lower quartile price.

- **LVR (loan to value ratio):** This is a measure used by banks and shows the amount you are borrowing, represented as a percentage of the value of the property. Banks use LVR in assessing the risk of a loan; the lower the LVR, the lower the risk from a bank's perspective. A property worth $500,000, with a mortgage of $400,000, has an LVR of 80 per cent (loan value divided by property value, multiplied by 100).

- **Median house price:** The median house price is the "middle" price of all sales recorded in a particular area. It is also known as the 50th percentile. This is not the same as the average price, which is determined by summing all sale prices, divided by the number of sales.

- **Mortgage:** Even though you have heard of a mortgage before, you probably thought of it as the home loan you will be paying once you own the home. Technically, a mortgage is a loan on your home created by your lender. If you cannot make payments on your home, the lender will have the right to sell the property in order to gain the money they have lost.

- **Mortgage broker:** A mortgage broker is a person who does not work for a bank, but rather works on commission to match homebuyers with many lenders that may or may not be in your area.

- **Negative gearing:** Negative gearing occurs when incomings are less than outgoings. For example, a negatively geared property is one where the rent received is less than the loan repayments and costs of owning the property (such as insurance, property management fees and maintenance). The difference in incomings and outgoings is often referred to as a shortfall, and is treated as a loss for tax purposes.

- **O & A (offer and acceptance) form:** A form used when making an offer to purchase a property.

- **Off the plan:** When you buy off the plan, you are buying a property before it's been built, having only seen the plans. New apartments are often sold this way.

- **Over-capitalising:** In property, over-capitalisation occurs where the cost of renovating or building a home is less than the gain apportioned to that work when the property is sold. For example, a property worth $300,000, which has $50,000 of renovations and is later sold for $325,000, has been over-capitalised.

- **Passed in:** When the highest bid at an auction doesn't meet the reserve price set on the property and the property therefore does not sell.

- **Portfolio (as in property portfolio):** The number and type of investment properties owned.

- **Positive gearing:** This is the opposite of negative gearing occurring when the rent received from a property is more than the loan repayments and costs of owning the property (such as insurance, property management fees and maintenance). The owner may be subject to income tax on the extra income derived from the investment.

- **Price on application (POA):** Price on application, a term used when a seller does not wish to reveal a price in an advertisement.

- **Principal and interest:** This is a type of loan that consists of a principal (the amount borrowed/still to be repaid) and interest (charged by the bank).

- **Principle place of residence (PPOR / PPR):** This is a property owned and used as a sole place of residence. This term is relevant for capital gains tax calculations as a PPR is exempt from capital gains tax.

- **Property cycle:** History shows that property prices have tended to move in a cycle of recurring events, although the timing of this cycle is typically unpredictable. Broadly this cycle follows the following pattern: boom, bust, recovery and growth.

- **Refinance:** This involves replacing an existing loan with another loan on different (usually better) terms. An investor may refinance a loan with another bank offering better interest rates, however there may be costs involved in refinancing.

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- **Reverse mortgage:** A loan designed for people who want to access the equity in their home, without selling it. Reverse mortgages are usually available for people over the age of 60 who are cash poor but who have significant equity. Usually the loan is not paid out until the borrower passes away or relocates.

- **Rental yield:** The rental return on a property investment, represented as a percentage of the amount invested. Gross rental yield can be calculated by dividing the annual rent by the value of the property, then multiplying this figure by 100.

- **Reserve price:** The minimum amount a seller will accept at an auction.

- **Repossessions or foreclosure:** This is a term that refers to homes whose owners could not make payments each month. Once a lender has decided to sell the home, it will be in foreclosure. You should find out ways to work with your lender in case you miss a mortgage payment at any time. Having this knowledge in advance will make financial emergencies easier to deal with.

- **Sold under the hammer:** A property that sells at auction.

- **Serviceability:** Whether you can manage your mortgage repayments, based on your regular income and expenses.

- **Shortfall:** A way of describing the discrepancy between the rent received from an investment property and the loan repayments (and other costs of ownership such as insurance and management fees).

- **Stamp duty:** A State Government tax on the transfer of property, calculated based on the value of the property.

- **Strata title:** Also known as unit title. This title grants ownership of a section or a 'unit' of a larger building. This unit can be sold or transferred by the owner.

- **Subdivision:** A parcel of land divided into individual lots.

- **Supply and demand:** The dynamics of supply and demand can impact property prices. Where there are a lot of properties for sale, an over-supply may result in decreased prices and is typically referred to as a buyer's market. The opposite, especially where properties sell quickly, is termed a seller's market.

- **Tenants in common:** Two or more buyers own a property, with each owner stipulating a percentage of ownership.

- **Upper quartile:** The price point below which 75 per cent of sales were recorded. If there were 100 sales in a suburb, the 25th highest price would be the upper quartile price.

- **Vacancy rates:** A measure of how many dwellings are available for rent over a specified time period. A low vacancy rate means there are not very many dwellings available for rent, while a high vacancy rate means there is ample supply of rental properties.

- **Vendor:** This term is often used as a substitute for "seller" in legal documentation.

- **Vendor's terms:** A method of buying and selling where the purchaser pays the purchase price to the vendor in instalments, rather than paying the full price by way of a mortgage. The vendor usually retains title to the property until the full amount is paid.

- **Wrap:** See 'Vendor's terms'

- **Yield:** The overall return of an investment, shown as a percentage of the amount invested.

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