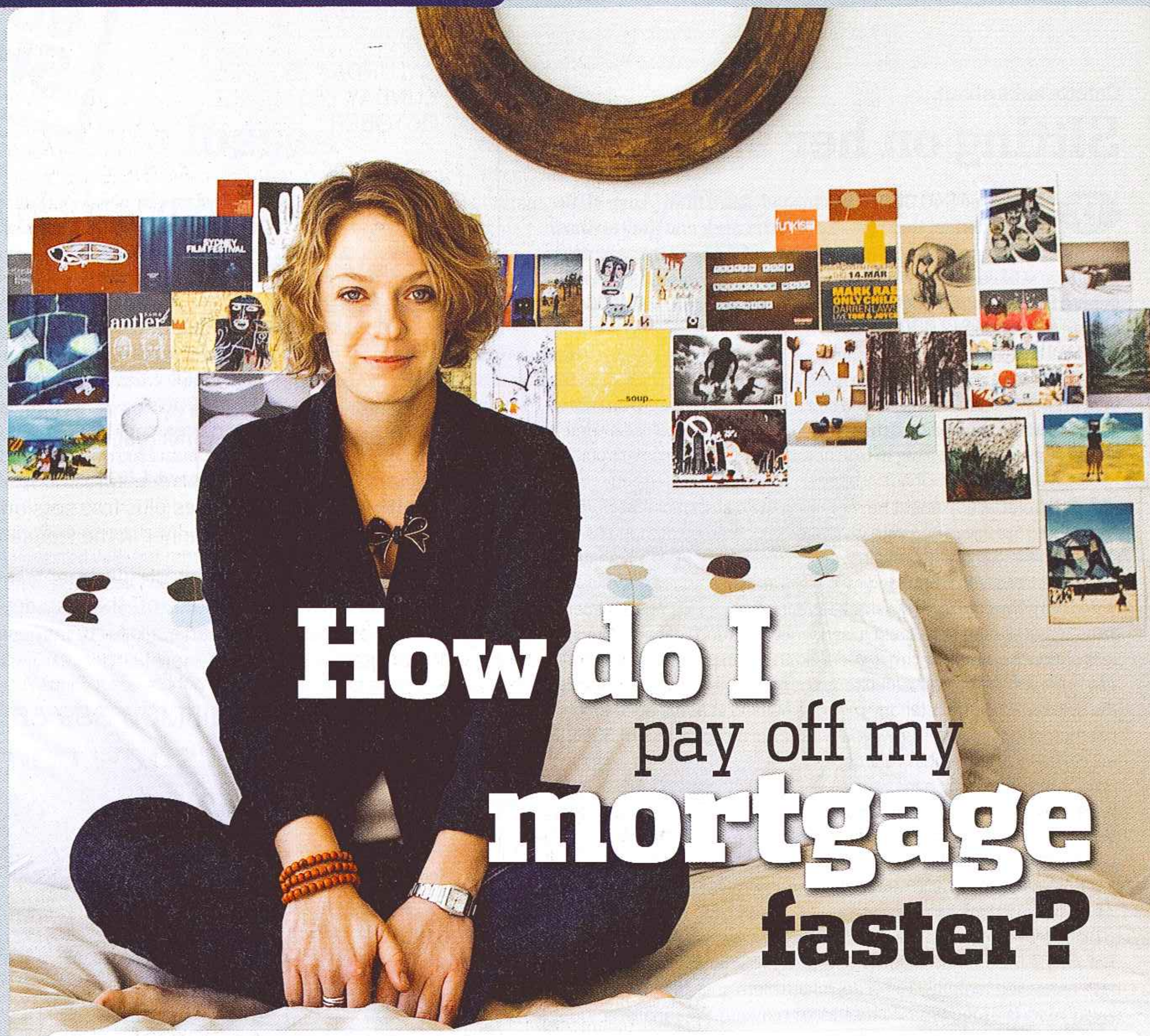
ask the experts



How do I pay off my mortgage faster?

ANDREW SHAW

Two experts in their individual fields advise one of our readers with a money dilemma

Mel Davis

AGE 33 **LIVES IN** Sydney
JOB Senior Designer

About a year ago Mel Davis bought a two-bedroom apartment, the first place she could call her own. Mel had been renting in the block for two years. She looked to buy in the area for six months before the owner approached her directly with the apartment. Mel has been a disciplined saver since she moved out of home at 20, and never spends more than she earns. She used a mortgage broker to secure the sharpest loan on offer from ANZ Bank. She opted for the whole loan at a variable rate, but when interest rates were rising she set two thirds at a fixed rate for 10 years and one third variable for 30 years.

Part of her loan is offset and she wants to know if this is the right strategy or is there a better one. Mel did take advantage of the First Home Owner Grant of $7000. She has a range of insurances such as income protection, death and TPD through ANZ, and super with the newly merged Media Super. She runs a Vespa scooter, cheaper than catching the bus after all expenses are calculated. She rents out her second bedroom and the garage.

While she believes it was a great opportunity, she acknowledges that buying a home is a big financial step. She sometimes wonders whether she will ever be able to afford to have a bit more fun, travel, further education and renovations. "How do I stay on top of things?"

Do you have any money queries for our experts? If so, email them to shely@acpmagazines.com.au

Review your insurance list

LISA FADDY

COMPANY Majella Wealth Advisers
TITLE Director

Lisa Faddy has a commerce law degree and a master of business administration. Majella Wealth Advisers offers clients tailored solutions to help them reach their financial goals.

Mel, you've taken a brave step in buying your own property. Sometimes you do need to take risks to get ahead. You also seem better than most at keeping to a budget.

Obviously your greatest need is to reduce the size of your mortgage, as your monthly repayments are almost 70% of employment income. Having an offset account is a great strategy in that the cash you use monthly is temporarily used to reduce your loan size.

We recommend you set up a regular fortnightly payment into your mortgage of an amount above the minimum repayment required, but not so much to not leave anything for "emergencies" or that holiday you're keen on! If your fortnightly repayments due are currently $1100, try setting the repayment amount at $1250, and keep the balance of your income/savings in your offset account. Paying off a little extra each time will help reduce the mortgage significantly.

Renting out a room and garage is both a positive and negative. While you will be taxed on the income received, you can also proportionally deduct expenses (including your mortgage interest, rates etc), which may provide an overall tax refund now (which can be repaid into your mortgage). But you may lose some of your capital gains tax exemption on the sale of your property. To confirm details, please speak to your accountant.

As you appear to be a conscientious saver, we recommend setting up a "treat" or "holiday" account with a goal of, say, $1000 for a holiday in six months time. Keep a record somewhere of the extra savings you make each fortnight – for example, an extra $40 saved each fortnight. Keep the money in your offset account to reduce your loan interest, but once you reach your goal, use it for a great holiday.

Other saving areas include a review of your insurance, as this is costing you over $1400 a year. While insurance is very important, without dependants you may not need life insurance. If you do wish to keep it, you may be able to move it into your superannuation fund at a lower cost. Income protection insurance is very important for you, as this will enable you to fund your lifestyle and continue paying your loan should you become sick or injured and are unable to work. Income protection can also be taken out in super, so this option may be worth considering. If it's a cost saving, it's more money for your loan repayments!

Use your offset account

DANTE DE GORI

COMPANY ClearView Retirement Solutions
TITLE Technical Manager

Dante De Gori specialises in supporting financial planners with ClearView Retirement Solutions, which specialises in advice, products and services to people nearing or in their retirement.

Mel is an opportunist with a good head on her shoulders. Not only has she broken into the property market, she has put her property to work by renting out the spare room and the garage, producing income to assist in repaying the property. There are also some positive taxation benefits with this strategy, as she will be able to claim a percentage of her interest as a tax deduction, thereby reducing her tax bill. Note that a portion of any profit made by the sale of the property will incur capital gains tax.

Mel is only one year into her mortgage, therefore the interest portion of her repayments are relatively high and reducing interest is important. One way is with an offset account. Mel mentioned that only part of her loan is offset and this is usually the variable portion of the loan. With standard variable interest rates around 9.5% this means she can offset $9.50 of interest for every $100 she contributes into the offset account.

Unless Mel can receive a greater net rate of return than her variable interest rate from other investments, I would recommend that she contribute her surplus income into her offset account. This offset account will achieve two goals – firstly reduce interest paid on the mortgage and secondly act as an emergency account.

To help with cash flow and reducing expenses, I think Mel would benefit from shopping around for both contents insurance and private health insurance. As for personal insurances, it is great she has them in place. However, with Life and TPD insurance she should look at transferring into her superannuation fund – Media Super. Mel should investigate what, if any, level of life and TPD insurance cover she already has in place through her super fund and the process of transferring/acquiring the level of cover she needs.

Having these insurances through her super fund can reduce total insurance premiums by almost half. Keep the income protection outside super, as premiums are tax deductible.

Mel need not think too much about super at this point of her life, especially with the mortgage. However, this should not stop her reviewing her super investment. She should research her investment options. At 33, I would look at a growth-style option, rather than leaving it in the default option, as this will help maximise her benefit in the long run.