Debt strategies

Transfer your debts using a financial windfall

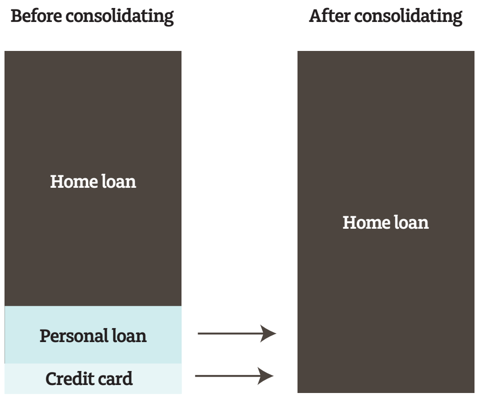
If you receive a financial windfall, you may want to use the money to reduce your home loan and borrow an equivalent amount for investment purposes.

How does the strategy work?

With this strategy, you need to:

- increase the mortgage on your family home, and
- use the extra funds to pay off other non-tax deductible debts (such as a personal loan or credit card) where the interest rates are generally higher than home loan rates.

By doing this you could potentially pay less interest, as the lower interest rate on your home loan will apply to all your debts, as the case study on the opposite page illustrates.



Maintain overall loan repayments

When consolidating debts, it's important you keep making at least the same overall loan repayments. Otherwise:

- it could take longer to pay off your combined debt, and
- you could end up paying more interest over the life of the loan, despite the lower interest rate.

Check loan features

It's important your home loan offers features that can enable you to pay off the combined debt quickly, such as a 100% offset account[1] or a redraw facility[2]. If it doesn't, you may want to consolidate your debts into a more flexible home loan.

Other key considerations

- You may need to pay refinancing costs, including loan application fees, stamp duty and early termination fees.
- You should ensure you have enough insurance to protect your income and cover loan repayments in the event of your death or disability.

Seek advice

A financial adviser can help you assess all the issues that need to be considered and determine whether debt consolidation suits your needs and circumstances.

[1] An offset account is a transaction account that is linked to a home (or investment) loan and the balance is directly offset against the loan balance before interest is calculated.

[2] If your home loan has a redraw facility, you can make extra payments directly into your loan and withdraw the money if necessary. You should confirm with your lender whether any fees apply.

Transfer your debts using a financial windfall

Case study

Daniel has a home loan of $200,000, the interest rate is 7.5% pa and he pays tax at a marginal rate of 39%[1]. He has just received an inheritance of $100,000 and would like to invest this money to build his long-term wealth.

If he uses the inheritance to purchase the investments directly, his home loan will remain at $200,000 and, because the interest payments are not tax deductible, the after-tax interest cost will be approximately $15,000 pa (see option 1 in the opposite table).

After assessing his goals and financial situation, Daniel's financial adviser explains that a potentially better approach would be to:

- use the $100,000 to reduce his home loan
- borrow an equivalent amount through an interest-only investment loan secured by his home, and
- purchase the investments with the borrowed money.

If Daniel follows this advice, he'll have a home and investment loan of $100,000 each and the after-tax interest cost of the home loan will be $7,500. However, because the investment loan interest (also $7,500) may be tax deductible, the after-tax cost of this loan could potentially be $4,575 pa (see option 2).

In other words, if Daniel uses this debt transformation strategy, while his total debts will remain at $200,000, his total after-tax interest bill could reduce from $15,000 pa to $12,075 pa and he'll still get to invest $100,000.

His financial adviser also suggests that:

- he use the income from the investments and the after-tax interest savings to pay off his home loan faster, and
- when his home loan is repaid, he use the investment income to purchase more investments and build even more wealth in the future.

	Option 1 Without debt transformation	**Option 2 With debt transformation**	
Loan type	Home loan only	Home loan	Investment loan
Loan amount	$200,000	$100,000	$100,000
Interest payable at 7.5% pa	$15,000	$7,500	$7,500
Less tax deduction at 39%[1]	N/A	N/A	($2,925)
After-tax interest cost	$15,000	$7,500	$4,575
Total after-tax interest cost	**$15,000**	**$12,075**	

[1] Includes Medicare levy.

A133941-0217

endeavor FINANCE

Endeavor Finance
61 Bull Street, Bendigo

03 5434 7690
endeavorbendigo.com.au

Venture Financial Services Pty Ltd trading as Endeavor Finance
Authorised Credit Representative 487813.
BLSSA Ltd ACN 117651760.
Australian Credit LIcence 391237

venture FINANCIAL ADVISERS

Venture Financial Advisers 61 Bull Street, Bendigo

03 5434 7600
venturebendigo.com.au

Venture Financial Planning Pty Ltd trading as Venture Financial Advisers
Authorised Representative Godfrey Pembroke Limited Australian Financial Services Licensee 230690 Registered office at 105 –153 Miller St North Sydney NSW 2060

GODFREYPEMBROKE