young enterprise TRUST

[Personal Financial Management Unit Standard]

Each Package contains:
Student Workbook (this sample)
Assessor Guidelines
Teaching Powerpoint
Assessment

28103

Analyse and select personal house financing and purchase options

Level	3
Credits	3
Version	1

STUDENT WORKBOOK

NAME:

TEACHER:

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Outcomes and evidence requirements

Outcome 1

Analyse and select personal house financing and purchase options

Evidence requirements

1.1 Options for personal house financing and purchasing are analysed and compared in terms of costs and benefits.

Range:

- **financing options** include – mortgage types, mortgage providers, deposit, calculation of interest;
- **purchasing options** include – mortgage establishment fees, lawyer fees, Land Information Memorandum report, builder's report, predicted ongoing costs;
- **predicted ongoing costs** include – rates, repairs and maintenance, insurance, property management fees.

1.2 Preferred personal house financing and purchasing options are researched and selected in relation to a purchase and personal financial circumstances.

Award of Grades:

Achieved, Merit, or Excellence

This unit standard can be awarded with *Achieved, Merit*, or *Excellence*.

Criteria for Achieved

For the *Achieved* grade to be awarded, the outcome must be achieved as specified in the outcome statement. Leaner must analyse, compare and select personal house financing and purchasing options.

For *Merit* or *Excellence* to be awarded, the candidate must meet the *Merit* or *Excellence* criteria specified below.

Criteria for Merit

Analysis includes a detailed comparison of the calculated costs and benefits of the options for personal house financing and purchasing options. Preferred options for a personal house financing and purchase are supported by reasons for their selection by making links between purchase options and personal financial circumstances.

Criteria for Excellence

Analysis includes a comprehensive comparison of the calculated costs and benefits of the options for personal house financing and purchasing options and a justification for selection of personal house financing and purchasing options for a purchase, and includes explanation of their suitability to personal financial circumstances over other options.

Financing Options

Mortgage Types	Mortgage Providers	Deposit	Calculation of Interest
Table	Family/Whānau	Savings	Compound
Reducing	Iwi	Kiwisaver	Simple
Interest only	Banks	Family/Whānau	Interest rates
Revolving	Finance Companies		• fixed
First mortgage	Building Societies		• floating
Second mortgage			
Bridging finance			

Mortgage Type:

What is a mortgage?

- A mortgage is a specific type of loan for the purchase of **property or land** and is usually taken out over a longer period of time, for example 30 years.
- The rate of interest on mortgages is either **fixed or floating**, or can be a combination of both.
- A **home loan**, also referred to as a **mortgage**, is used by purchasers of real property to raise money to buy the property to be purchased or by existing property owners to raise funds for any purpose.
- The loan is "**secured**" on the borrower's property.

- This means that a legal mechanism is put in place which allows the lender to take possession and sell the secured property ("foreclosure" or "repossession") to pay off the loan, in the event that the borrower defaults on the loan or otherwise fails to abide by its terms.

The features of mortgage loan can vary considerably between financial institutions, such as:

- the size of the loan
- maturity of the loan
- interest rate

Type of Loan

- When you're choosing a mortgage, apart from the mortgage **interest rate**, you'll also need to think about the **type of loan** you want.
- Each type is designed to suit different situations and goals.
- Also, with tailored repayments, you have the option to gradually increase your repayments so you could save thousands in interest.
- You can also split the amount you borrow between more than one type of mortgage.
- For example, some people choose an offsetting **floating** mortgage (so they can use cheque and savings accounts to help reduce the interest on their mortgage) and a **table loan** with a fixed interest rate for the certainty of fixed mortgage repayment).

Task:

Describe in your own words what a mortgage is.

Mortgage Type:

Table mortgage

- This is the most common type of home loan.
- You can choose a term up to 30 years with most lenders.
- Most of your early repayments pay off the interest, while most of the later payments pay off the principal (the lump sum you borrowed).
- You can take a table loan with a fixed rate of interest or a floating rate.
- Application fees for table loans range from nothing to over $1,000. Most lenders charge around $200 to $400. This is often negotiable.

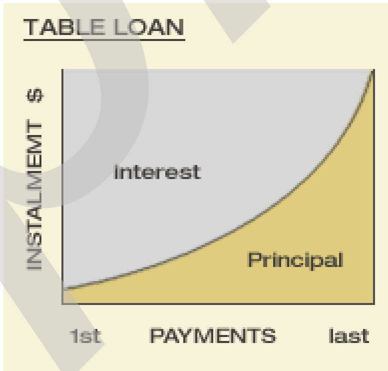
Advantages:

Table loans provide the discipline of regular payments and a set date when they will be paid off.

They provide the certainty of knowing what payments will be, unless you have a floating rate, in which case repayment amounts can change.

Disadvantages:

Fixed regular payments might be difficult for people with irregular income.



Task:

Describe in your own words why a **Table Mortgage** would be a good option for someone taking out a 25 year mortgage.

Mortgage Type:

Reducing mortgage

- Reducing or straight line mortgages repay the same amount of principal with each repayment, but a reducing amount of interest each time.
- These are quite rare in New Zealand.
- Payments start high, but reduce (in a straight line) over time.
- Fees are similar to table loans

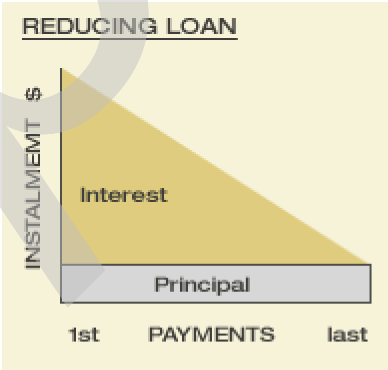
Advantages:

You pay less interest overall than with a table loan because early payments include a higher repayment of principal.

These may suit borrowers who expect their income to drop, for example, if one partner plans to give up work in a few years' time.

Disadvantages:

- If you can afford higher payments you would be better to take a table loan with payments high for the whole term, so you'll pay less interest.



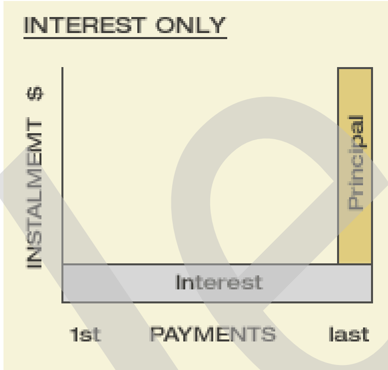
Task:

Explain the benefits of a **Reducing Mortgage** compared to a **Table Mortgage**.

Mortgage Type:

Interest only mortgage

- You only pay the interest part of your loan, not the principal, so the payments are lower.
- Some borrowers take an interest-only loan for a year or two and then switch to a table loan.
- The normal table loan application fees apply.



Advantages:

You have more cash for other things, such as renovations.

Disadvantages:

You will still owe the full amount that you borrowed until the interest-only period ends and you start paying back the loan.

Task:

Explain a situation where it would it useful to be able to get an **Interest Only Mortgage**.

Mortgage Type:

Revolving mortgage

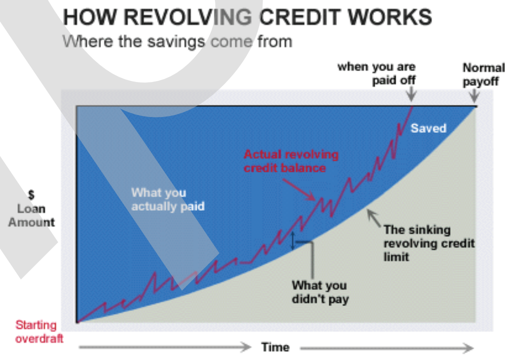
- Revolving credit loans work like a large overdraft.
- Your pay goes straight into the account and bills are paid out of the account when they're due.
- By keeping the loan as low as you can at any time, you pay less interest because lenders calculate interest daily.
- You can make lump sum repayments and re-draw money up to your limit.
- Some revolving credit mortgages gradually reduce the credit limit to help you pay off the mortgage.
- Application fees on revolving credit home loans can be up to $500.
- There can be a fee for the day-to-day banking transactions you do through the account.

Advantages:

- If you're well organised, you can pay off your mortgage faster.
- This suits people with uneven income as there are no fixed repayments.
- Putting surplus funds into this account rather than a separate savings account will give bigger interest savings and also avoids the tax on the savings account interest.

Disadvantages:

- You need discipline. It can be tempting to always spend up to your credit limit and stay in debt longer.



Tasks:

1. Describe in your own words how a **Revolving Mortgage** works.

Outline the possible issues a person with a Revolving Mortgage needs to be careful about.

Mortgage Type:

First mortgage

- A first mortgage is a loan secured by the property. This mortgage is the first to be paid if the property is sold in the event of default. If a person has a second mortgage, the first mortgage will take precident
- The mortgage company holds the deeds to the property.

Task:

Describe what **deeds** to a property are.

Mortgage Type:

Second mortgage

- Is simply another mortgage on your home – a loan secured against the property.
- The term "second" indicates that the loan does not have priority on your home in case you default.
- Instead, your first mortgage (typically the loan used to purchase your home) has priority and that loan would be paid off before any funds go towards the second mortgage.

Why would somebody risk their home with a second mortgage?

- These types of loans are appropriate for times when you need a lot of money.
- You may not have unlimited credit on your credit cards, and finding the cash just lying around is difficult.
- Where is there a lot of equity or value in your home, assuming you've paid off part of your home loan or the price your home has risen.
- Second mortgages may allow for bigger loans because the lender considers a loan against the home to be safer; the home serves as collateral.

Disadvantages of Second Mortgages

- The main disadvantage with second mortgages is that you are **risking your home** by using one.
- This is a serious risk; if you can't pay the loan back, your lender can potentially foreclose and force you out of your property.
- Make sure that your intended use of funds is worth the risk you're taking by using a second mortgage.
- Another drawback is that second mortgages have **slightly higher rates** than senior mortgage rates.
- This is because the second mortgage won't be paid until the first one is (in the event of a default).
- Because the loan is riskier than the first mortgage, it costs more. However, the rate might still be lower than alternative sources like credit cards and unsecured personal loans.

Task:

Explain in your own words why someone may want to take out a second mortgage.