

Your questions answered

We put some of your trickiest questions to a panel of experts, who offer wise words on everything from cross-collateralisation to avoiding being gazumped – without putting down a deposit!



Q I'm about to purchase my first investment property, and I'm keen to do so by using the equity in my own home. Friends have advised me against cross-collateralisation, however, saying it's too risky and expensive. What do you think?

A I am well over hearing the stories of how at risk property investors are if they choose to cross-collateralise their properties. I am almost certain that the advice from brokers and the like not to cross-collateralise is for the purposes of maximising commissions

for them, more than it is to provide any real benefits to the investor.

Cross-collateralisation is the process of providing a mortgage to one bank across all of the securities (properties) you offer them. Rather than have one loan per property, independently 'securitised', you offer the bank all of your property as one security, and they offer you as much debt as you qualify for, based on this security and your borrowing capacity. Typically, you would then structure 'sub-accounts' under this loan umbrella, one for each property, representing the amount of the debt outstanding against each one.

The main benefit of cross-collateralisation is that once the equity begins to grow a little on each property, you can use that equity collectively, as well as the usable value of any new property you buy (usually 80% of its value), to set up an additional 'account', again presenting the total outstanding amount of the debt needed to buy that new property.

If you choose *not* to cross-collateralise, you would instead have one separate loan for each property. When each property grows a little in value and you want to buy another, you must get an increase on each loan *plus* another loan against the value of the new property, or refinance the lot. Consequently, you will have a lot of loans, with little bits of each existing loan attributable to the new property. The accounting alone would be a nightmare!

So why independently securitise, and why is there such a scare about cross-collateralising? It is said that when you keep your properties separate, you are safer. If you get into financial trouble over one, then the bank's ability to recover any debt you owe them is limited to this one property – the one they hold – and you can continue to prosper from the ones you have left.

This could not be further from the truth. When you borrow money, the bank takes out a mortgage. Among other things, a mortgage is also a guarantee that, if you experience difficulty and the value of the property is not enough to satisfy the mortgage, the lender can sue you for the balance. They will take you to court, and the courts will order you to sell any other assets you have until what you owe the lender is completely satisfied. This

can include selling other mortgaged property to release any equity you have in them to satisfy your defaulted debt.

Keeping them separate offers no protection, increases accounting and loan set-up costs and results in difficulty drawing back on increasing equity. Cross-collateralising does not increase your risk or costs in any way, and makes adding to your portfolio easy and efficient. As with any clever 'strategy' you may hear about, always ask yourself, 'Who gets the greatest benefit from this idea – me or the adviser?' This question will help you to only ever employ straightforward, honest and reliable property investing methods.



Margaret Lomas is the founder of Destiny Financial Solutions, a qualified financial adviser and the author of five best-selling property investment books. She is the 2006 Telstra NSW

Businesswoman of the Year. Visit: www.destiny.net.au

Q I want to up the rent on my investment property to take advantage of the current lack of availability in the rental market. I'm worried I may lose a good tenant in doing so – is it worth the risk?

A While your tenant would prefer to pay the lowest rent they can, as a property investor, you obviously want to get the best return possible on your investment.

But as a landlord you cannot just put up the rent as and when you feel like it. For example, you usually cannot increase the rent until the lease expires and there are legislative notice periods you must adhere to and these vary from state to state.

When considering how much you should increase the rent, it is worth considering the following:

- The current rent
- The rent of similar properties in the vicinity
- When you last increased the rent
- The vacancy rate in your area, which is, of course, affected by the local supply and demand of tenants and properties

- The time of year – there are some periods when there are plenty of tenants wanting to move and other times such as the dead of winter or around Christmas when there are fewer tenants around

Supply and demand of tenants and properties is the biggest factor in your ability to increase rents. If there are more rental properties available compared to tenants looking for them, increasing rents will be difficult. In our current market, however, there is a shortage of properties and rents are generally rising. Regardless, you cannot just ask any rent you want; tenants are still price-sensitive and if you ask too much they will use it as an excuse to move.

If this happens, you will have a vacancy period with no rent and you will then be faced with having to pay your managing agent a leasing fee and possibly advertising costs.

With an average rent of \$400 per week, you could be out of pocket over \$1,000, meaning you would have to get an extra \$20 a week over 12 months just to break even. The good news is that with the prevailing low vacancy rates, we are able to increase many rentals, something that has been difficult to do over the last few years.

When calculating the rental increase, you must balance the emotions and reaction of the tenant with maximising your income. In some situations it may not be worth losing a quality tenant for an extra \$20 per week.



Pamela Yardney is a director of Metropole Property Investment Strategists and is a member of the REIV. Visit: www.metropole.com.au

Q Is there a way that I can avoid being gazumped without spending money on deposits?

A Yes, there is. This is a common mistake made by investors. It doesn't take long for people to get sick and tired of missing out on deals. They eventually realise they need to get the property off the market in order to do their due diligence without coming under pressure from other buyers.

There is nothing worse than trying to buy property and being gazumped by another buyer each time. I was often gazumped in my early years of investing and I wasted many hours researching deals that I'd miss out on time and time again, especially in a hot market.

That is why I always insist that my investor clients take the property off the market first so they can undertake further due diligence without pressure from other buyers.

The key to taking a property off the market is to put in an offer and include contract clauses that make the contract conditional upon you undertaking certain searches and due diligence. Using 'Special Conditions' contract clauses allows you to take the property off the market so you can conduct your due diligence before unconditionally having to commit to purchasing the property. The clauses you use (which would preferably be written by a solicitor) will allow you to withdraw from the deal should your research uncover anything unfavourable.

When purchasing property, I always use a 'due diligence' clause which I set for a period of about 35 days. This allows me to conduct all my research in a timely manner and to avoid being put under pressure, especially if I am purchasing property in another state.

By using this clause I am able to secure the property and prevent others from bidding on it for those 35 days. It's an ideal way to purchase property. And the bonus is that I rarely provide a deposit.

Why would anyone want to purchase under pressure when you may not have all your facts, therefore increasing your risk of making a mistake? Taking the property off the market buys you the time you need to ensure your investment is a great one.

Here's my tip: ensure you seek legal advice for the content of your 'subject to' clauses before including them in a contract of sale.



Helen Collier-Kogtevs is an educator and author of 47 Biggest Mistakes Made by Property Investors and How to Avoid Them. Visit: www.realwealthaustralia.com.au