CONSUMER CREDIT LEGAL SERVICE INC.

MORTGAGE REDUCTION - MISLEADING MARKETING

A REPORT TO ASIC BY CONSUMER CREDIT LEGAL SERVICE

The Consumer Advisory Panel of the Australian Securities and Investments Commission (ASIC) funded Consumer Credit Legal Service to produce a "case study" report for ASIC on "debt reduction" plans. This report was provided to ASIC in March 2004. We also provided ASIC with a list of websites that appeared to promote the concept of "saving thousands" or cutting "years off your mortgage" by using a line of credit.

We have not included this information, which identified particular businesses, here. However, an indication of the extent of this form of marketing can be gained by searching key words such as "cut years off your mortgage" "without extra repayments" and similar phrases.

Since this report was originally provided to ASIC, there have been numerous articles warning consumers of the traps of this form of marketing, including a warning by ASIC. See: http://www.asic.gov.au/fido/fido.nsf/byheadline/Line+of+credit+mortgages?openDocument

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1 INTRODUCTION

Terms such as “mortgage reduction” or “mortgage minimisation” are commonly used by some in the finance sector. While there is no clear definition of these terms, our casework suggests that they refer to a financial plan that involves:

1. Refinancing of a mortgage (usually with a line-of-credit);
2. Paying salary(ies) into the line-of-credit;
3. Increasing payments on the mortgage (whether this is drawn to the borrower’s attention or not); and
4. In some cases, consolidation of other debts.

See APPENDIX 2 for a Credit Helpline FactSheet that explains why borrowers should be cautious about all mortgage reduction marketing. This paper focuses on the first three features of mortgage reduction.

2 The Line of Credit Hoax

True or False?

You can cut years off your mortgage – and save thousands of dollars if you:

- Refinance your traditional mortgage loan to a line-of-credit;
- have your salary paid directly into that account;
- use a credit card for expenses, with that account paid monthly from the line-of-credit.

In fact, most borrowers - even those on high incomes - would pay more by using this system!

This urban legend, fanned by misleading marketing - and to some extent by unthinking support from generally reputable sources - is really a hoax.

The idea derives from a degree of logic. Standard mortgage loans have regular monthly payments of interest and principal, struck to repay the loan over a longer term of, say, 25 years.

Interest on most mortgage loans is calculated each day on the outstanding balance. Therefore, the more money that is paid into the mortgage (even if it is left in for a short time) the lower the interest charged. It follows, according to promoters, that if your income is paid into your mortgage and left there as long as possible (by using an interest free credit card for expenses) you can reduce the term of your mortgage.

The truth is, the amount saved by this method is very small, and in most cases is far less than the additional costs[1] of the type of mortgage re•uired (offset account or line of credit mortgage).

As an example, Choice Magazine[2] found that a couple with an average of $14,000 savings and a $268,000 home loan were $830 worse off over a twelve month period with an off-set account, and would have been better off with a “no frills” mortgage. The difference between the fee and interest expense on the “no frills” mortgage, compared to the mortgage with off-set, were more than any interest savings made by keeping an average of $14,000 in the off-set account. This example did not assume that the couple had refinanced – as many borrowers do. Refinancing costs would have seen the couple even worse off.

Mortgage offset accounts are deposit accounts linked to a mortgage loan. Rather than earning credit interest on funds held in the offset account, the interest due on the loan is reduced as if the offset funds

had been paid to the mortgage[3]. There are additional advantages in that:

- as there is no interest earned, there is no liability for income tax; and
- deposits remain readily available for withdrawal.

A line-of-credit (or “all-in-one”) mortgage has similar features to an offset account, except the savings account and mortgage account are combined in one account.

Mortgage offset accounts and line-of-credit mortgages do have advantages for some classes of borrowers. There could be a reduction in interest expense for borrowers with significant savings if their mortgage isn’t too large, but the Choice example shows this benefit may not be there for the average borrower.

The line-of-credit mortgage in particular is very flexible and could suit investors looking to regularly draw funds for, say, deposits on new property purchases. With a line-of-credit, funds are always accessible with no need at all to contact the lending institution, although they are subject to annual review. However, these mortgages are often being marketed to consumers inappropriately.

3 Misleading Marketing

The promotion of line-of-credit mortgages (or off-set accounts) ranges from slightly confusing messages to downright misleading and deceptive conduct.

It is common for marketers to compare a standard 25-year home loan with a line-of-credit mortgage – both in advertising and when presenting a “scheme” or “plan” to individual borrowers. Comparitive examples provided during the marketing process assume that no additional payments are being made on the 25-year loan, but do assume that the amount being paid towards the line-of-credit mortgage is much higher.

This is not always immediately clear to consumers, however close examination of the examples, shows that even after drawing out living expenses each month, the amount remaining in the line-of-credit each month is much higher than the monthly payments on the standard home loan. It can be a complex exercise to examine these examples to identify the savings that result from increased payments and the savings (if any) resulting from use of the line-of-credit.

In most cases the borrower would be better off simply sticking to their current loan and increasing payments. There are many websites using this misleading marketing.

Looking at the calculators on these websites, it shouldn’t take most consumers very long to realise that more is being paid towards the line-of-credit mortgage than the standard loan. However, is all the “savings” due to making increased payments, or does the use of the line-of-credit itself contribute something?

It’s a bit more challenging for the consumer to establish this. It is the increased payments, rather than the product, that leads to the savings. However, it is not always easy to find this out by using the industry’s internet “tools”.

For example one calculator produced by Infochoice, has a default setting that shows over $90,000 in savings by using the line of credit (over a traditional loan). Close examination would show that the savings arise from increased payments – but the calculator doesn’t allow the user to, for example, increase the payment on the standard loan and compare the two loans. However, if monthly expenses are changed to e•ualize monthly payments on both loans:

* Standard loan with a 5 year term – payments $1,991.94 per month
* Monthly expenses $2,008 – (payments of $1,992 per month)

It results in a saving of just 78c!!

While some marketers mention the need for "disciplined budgeting", few mention that you actually need to increase mortgage payments.

In fact, some claim that you can cut years off your mortgage "without making extra repayments"[4].

4 Marketing of Debt Reduction Schemes

At the "extreme end" consumers are "cold-called" by telephone, and offered a "no obligation demonstration" to show how they can save thousands on their mortgage. If they agree, a representative visits them from a debt reduction firm. These firms charge (usually around $5,000) for a "debt reduction scheme". The savings from the "scheme" are, of course, based on making larger payments to the mortgage (and sometimes other debts). However, the emphasis is on the benefits of using a line-of-credit, and the scheme documentation avoids bringing any attention to the increased payments.

Using high-pressure sales tactics combined with graphs that indicate that huge interest savings can be achieved by the simple means of rearranging your loan, borrowers are enticed to refinance their traditional mortgages using the promoted products.

When closely investigated, the cash flow forecasts prepared by the debt reduction "consultants", usually re•uire a significant reduction in the borrowers' living expenses, in order to leave a substantial proportion of their income in the line-of-credit account. This is effectively increasing the borrower's mortgage payments, but the sales representative glosses over this.

A common marketing ploy is the "bank bashing" approach. Verbal representations and some written material suggest that "you are being told what the banks won't tell you".

In cases examined by CCLS, the borrowers could have achieved the same effect by simply increasing their existing regular mortgage payments with none of the additional expenses of:

* Fees to the debt reduction scheme promoter;
* Loan establishment fees to the new lender;
* Statutory and administrative expenses associated with the new loan; and
* Break costs with their existing borrower.

Similar plans are marketed by some other companies and brokers – and given the number of brokers promoting the savings resulting from a line-of-credit mortgage, it might be assumed that many brokers are using similar sales techni•ues, or supporting debt reduction firms in their marketing.

5 Sources of Case Studies

CCLS has collected 23 cases of consumer experiences with these companies and their agents. These cases are gathered in APPENDIX 1.

The cases have come

* Credit Helpline Victoria (CHL) 11
* Consumer Credit Legal Service (CCLS) 3
* Consumer Credit Legal Centre 2
* Camcare 1
* ACT Consumer Legal Centre 2
* •ueensland Legal Aid 1 – but advised they are aware of more
* Unknown 2

The cases have largely been sourced from the records of the Credit Help Line but there are more detailed examples from cases undertaken by CCLS and also some cases from colleagues in other Victorian and interstate community advocacy groups.

Anecdotally, the product sold is occasionally a mortgage offset account rather than a line-of-credit. The exact product could not always be identified from the case material – sometimes the client did not proceed.

Common sales practices have been identified from the transcripts but it should be noted that some practices probably occur even more fre•uently than shown, as only explicitly stated incidences were counted. For example, all cases are likely to have involved promises of substantial savings of time and money on existing loans but this was not always specifically highlighted in the client's recall of their experiences.

The inherent fallacy in the promotion of the debt reduction package of:

* line-of-credit mortgage and credit card; combined with
- direct crediting of salaries,

of itself producing dramatic interest savings, is also only occasionally especially addressed in the cases. Rather, it is manifested by clients' concern that they did not understand how the "system" worked.

It should be noted also that most cases have come to light from complaints about costs, etc. and the clients' focus is on their specific concern and not the overall misleading nature of the sales process. Similarly, few cases have been provided from interstate sources. We believe this is because Credit Helpline and CCLS identified the practices of debt reduction scheme promoters some years ago and staff have routinely identified the role of such schemes in callers' problems.[5]

The activity of the promoters throughout Australia is undoubted as many are domiciled interstate and have additional contact details in a range of towns and cities. A NSW Building Society has also contacted CCLS directly drawing specific attention to many such debt reduction firms operating in their market.

Attention is especially drawn to Case 17, as the writer of this report was able to interview the client specifically for the report. Although the client did not proceed with the product beyond telephone calls, her detailed recall of the sales claims made to her, are considered to be an important representation of general industry practice.

5 Sales Practices

Sales Practices	No
Unsolicited telephone calls to arrange home meetings	12
Soliciting in supermarkets	1
Home visits lasting many hours, usually late in the evening	6
Guarantees that "mortgage will be paid off in 7 years", "save thousands of dollars", etc.	8
When client offered that they were already planning to pay off their mortgage in 7 years, the telephone representative countered with " Are you doing that by making extra repayments? With our offer you will pay off your mortgage in 7 years without making any additional repayments. You just need to use our line-of-credit mortgage and free credit card."	1

When information was directly sought from the telephone consultant as to how the savings was made, this could not be provided. The only form of "explanation" offered was for a representative to call at their home.	1
Misleading comparative graphs used to demonstrate "savings"	2
"Training" given on how to "use a credit card to pay off your mortgage"	1
Attractive dream sold: ❖ "soon be debt free", ❖ "able to go on a holiday"	1
Names and telephone numbers of friends sought as referrals at an early stage in the sales process	2
Intimidatory tactics used if clients state they do not wish to proceed	3
Initial sales representative obtains signatures to a first stage agreement and collects a deposit fee. Financial information is obtained to complete debt reduction program. A couple of days later, another representative calls to complete sign up including very substantial fees and costs, often capitalised.	7
When clients •uestioned fees in initial agreement, they were told that the fees did not apply yet and to just sign "so my boss knows that I've been here". Fees were later claimed to apply.	1
Agent ❖ states loan facility would have no fees; and ❖ would not answer •uestions regarding interest rates, etc.	2
Clients realise the new loan compares unfavourably with existing loan on interest rates, etc	3
When the terms of the loan contract differed from the terms of the broker's offer, clients unable to get either the bank or the broker to clarify	1
'Agreements' signed without the clients fully understanding the offer and its implications	3
Very substantial fees charged for debt reduction program component of the offer	2
Poor assessment of clients' suitability for product e.g. selling credit cards and line-of-credit mortgages to financially naïve low-income earners.	3
'Staged signing-up' over several occasions in an apparent attempt to avoid "cooling-off period" provisions	1
Representative refusing to leave documents to allow legal advice to be sought before execution	1
"Independent advice" on the product offer given by a solicitor introduced by the representative	1
Representative insisting that the documents be signed "right now as he was running late for an appointment"	1
Substantial fees and costs invoiced even when the clients withdraw before the offer is fully accepted	6

6 What is the Impact on Consumers?

The most common complaints by consumers relate to debt reduction plans sold by debt reduction businesses. This is mainly due to high-pressure sales and a fee of around $5,000 that often takes the consumer by surprise. For these consumers, the problem is often an immediate one of how to cancel the agreement with the debt reduction firm and avoid being sued for the fee.

Other complaints come from consumers who have signed up for the plan and refinanced as advised – but have found that the line-of-credit is difficult to manage. In some cases consumers get into financial difficulty due to the problems of managing the line-of-credit and related credit card. Anecdotally, some brokers report an increase in re•uests from consumers to refinance from a line-of-credit back to a basic home loan.

However, without the high initial fees, the impact on many consumers will simply be the costs of refinancing, and possibly higher fees and charges on their new mortgage. Many will be worse off than if they had stayed with their original loan – but this will not necessarily be obvious. Some may actually believe that they are saving money due to the "magic" of a line-of-credit.

7 Does Anyone Do This Right?

There are techni•ues consumers can use to reduce their mortgage, and it is possible that some brokers or financial advisors may present helpful, independent advice in relation to mortgages. We are also pleased to see a few brokers telling the truth about the potential benefits (and otherwise) of line-of-credit and offset accounts.[6] However, given the volume of misleading information around, it is just not possible for a consumer to determine who is telling the truth.

8 Who's Marketing These Schemes?

Many lenders and brokers clearly benefit from the misleading marketing of line-of-credit mortgages, as borrowers are convinced to refinance on the basis of promised savings. However, lenders are rarely directly involved in misleading marketing.

Most case studies in this report relate to the selling of plans by debt reduction firms. It appears that some of these firms refer consumers directly to the lender for the line-of-credit. However, some debt reduction firms refer consumers to finance brokers that then arrange the finance with the lender. In most of those cases, the consumer does not have contact with the finance broker and may not be aware that a finance broker is involved.

Many finance brokers have information on their websites on line-of-credit or debt reduction that is potentially misleading. Some finance brokers appear to have referral relationships with debt reduction firms, and some may support the work of debt reduction firms by providing, for example, computer software and paperwork.

It doesn't appear that lenders are directly involved in misleading marketing, however the extent to which they are aware of the methods of marketing their products by brokers and others, is unclear.

There is an indication that some financial planners may, increasingly, play a role in providing advice in relation to mortgages.

The extent to which this involves the plans referred to here is unclear, but there is some evidence that mortgage advice (or "mortgage elimination" as it is termed on some planners' websites) and referral to lenders, or brokers, is already a key part of the service provided by some financial planners.

9 Regulation

There has been much said recently about problems arising due to the lack of regulation of finance brokers[7]. There have been some moves to address this problem by developing national, uniform legislation. Such legislation, when it is in place, will offer some protection to consumers who suffer loss as a result of bad advice by a finance broker. However, it already appears that the debt reduction marketing often involves three players – debt reduction firm, broker and lender. In some cases the debt reduction firm argues that it is not a broker – it is only providing advice and referring the consumer to a broker. However, as mortgage advice is not a financial service regulated by the Financial Services Act, these services are virtually unregulated.

It is crucial, therefore, that in developing legislation to regulate brokers, all entities in the chain providing information or advice about the loan product, be covered.

APPENDICIES

APPENDIX 1 • CASE STUDIES

Case studies have been sourced from consumer complaints to a number of services including Credit Helpline (Victoria), EACH Financial Counselling (Victoria), Consumer Credit Legal Service (Victoria), Consumer Credit Legal Centre (NSW), Legal Aid •ueensland, Credit and Consumer Legal Centre (ACT).
Some complaints have been investigated by advice services or regulators, but the information provided in most of these case studies is based on the problem as reported by the consumer.

Case 1

Mr. & Mrs. A had already arranged finance for the purchase of their home with the Bank of Melbourne when they received an unsolicited call from a mortgage broking company, offering to renegotiate their mortgage at a competitive rate, free of charges. The representative asked to call upon Mr. & Mrs. A in their home to discuss the offer with them. A couple of days later the representative arrived and spent 5 hours with them, at the end of which time they had paid $295 as a deposit for entry into the company's "debt reduction program" and signed an agreement, the nature of which was not fully clear to them.

Four days later, Mr. & Mrs. A contacted the mortgage broking company by telephone and stated that they did not wish to proceed any further, but they were influenced to stay with the broker. Shortly after, Mr. & Mrs. A received an unsolicited visit from a representative who tried to convince them to sign some documents.

Mr. & Mrs. A asked the representative to leave the relevant documents with them to allow them to seek legal advice on the proposed agreement, but the representative refused, stating that the documents were the property of the broking company. The representative further indicated that Mr. & Mrs. A were liable for $3,700 for the company's expenses and another $2,000 in associated property transfer fees. Mr. & Mrs. A again informed the representative that they did not wish to proceed with the arrangement.

At 7:00 pm that evening, Mr. & Mrs. A were telephoned by another company representative who informed them that:

- they would have to write to the company stating that they did not wish to proceed; and
- in any event, they had already incurred costs of $2,000 owed to the broking company.

Case 2

6/8/2001 Mortgage Broker E Lender C

Mr. & Mrs. B met a mortgage broker's agent at the local supermarket. The agent then came to their home, offering to 'train' them how to use a credit card to pay their mortgage. The 'training' took half an hour. Mr. & Mrs. B do not recall signing a contract but they paid $4,500 for the program

Mr. & Mrs. B have been on the program for one year. Their wages go into a mortgage account – they pay for living expenses with the credit card – and the credit card balance is 'swept' into the mortgage account monthly. The agent guaranteed them that they would pay off their mortgage in 7 years.

Mr. & Mrs. B rang the broker back to get more 'training' because they didn't know how the programme worked. Someone did come out – but Mr. & Mrs. B still don't understand.

From their viewpoint, the program has not made any difference. In fact it is harder for them to keep up. They had never had a credit card before. Mr. & Mrs. B now have financial problems as they can barely meet the credit card bills.

Before they entered into this program, they were able to keep up with their mortgage payments.

Case 3

17/9/2001   Mortgage Broker   E

Mr. & Mrs. C appointed a mortgage broker and paid a fee of nearly $8,000 for loan comparison, loan application and debt reduction program services.

The broker went to their home on three separate occasions, completing the signing in stages, all within the 5-day cooling off period. This staggered signing process appears to be an attempt to rob the clients of their right to cool off (Fair Trading Act S63 (1) provided for a 5 day cooling off period 'from the day on which the agreement is made.').

Case 4

28/5/2002   Mortgage Broker E

The mortgage broker's agent originally contacted Mr. & Mrs. D by telephone. The agent then came to their house. He was selling a "debt reduction program" and convinced Mr. & Mrs. D that they could soon be debt free. He arrived at 8:30 pm and stayed for 2 or 3 hours. He sold them a "dream" - they would be able to go on holiday with the money they saved. The agent also asked them to supply the names and telephone numbers of friends as referrals, but Mr. & Mrs. D refused to do that.

The scheme included a line of credit facility and was said to have no fees. The agent did not answer •uestions about details such as interest rates, etc. but Mr. & Mrs. D signed up and paid a deposit fee of $240.

Two days later, a second agent came and told them about the fees and charges. Under the program, all their income is deposited into the mortgage account and they use the credit card for expenses.

When they signed up they were charged the following fees:

$150	settlement fee
$176	stamp duty
$118	registration fee
$295	solicitors' fees
$590	valuation fee
$4,950	Mortgage Broker E's fee

Mr. & Mrs. D refinanced the following debts with the new loan:

S home loan $59,000
R personal loan $5,000,
Credit card $2,000

Before they refinanced they were managing all the loans. Now they are struggling.

They borrowed $73,000 on 21 December 2002 and it has now increased to $86,000. Mr. D has been unemployed for 3 years. Mr. & Mrs. D would like to get out of this loan and refinance to a P& I reducing loan but are deterred in part by the $800 exit fee and $400 registration of discharge of mortgage fee.

Case 5

3/6/2002 Mortgage Broker F

Mr. E is considering signing up for a home loan through a mortgage broking company. The representative called on him at home. The initial documents were two pages – a pre-approval information form and a letter from the broking company basically stating that once they are provided with Mr. E's financial details, they will present him with plans that will make him debt free within 3-7 years. The documents did not provide any further information about the offer.

Case 6

15/7/2002 Mortgage Broker A Lender H

A mortgage broking company contacted Mr. & Mrs. F by phone. A representative then came to their house and discussed the offer with them.

After this first visit, Mrs. F rang and said they were not interested but the representative persuaded her to let them come back a second time. The representatives did a savings projection summary for the F's at this second visit, which cost them $295.

Mr. & Mrs. F then signed a contract with the broking company to refinance their home loan, proceeding on the basis that the broking company would negotiate them a loan with a better interest rate. The broking company was to approach various banks until they got the best deal. There was a cooling off notice included in the documentation, which also stated that the broking company would prepare and provide a debt reduction program which included a savings projection summary, performance tracker, client training session and operations manual.

Now that the F's have seen the actual bank contracts, they have found that they would be worse off and do not wish to proceed any further. Their present loan with their current bank is a better deal. The broker's representatives are urging Mr. & Mrs. F to sign up, claiming that they have already incurred a fee of $5,000, irrespective of whether they proceed or not.

Mr. & Mrs. F received another call from a representative. Mrs. F advised them that they weren't going ahead. This happened a second time. Mr. & Mrs. F are concerned that the broking company will start making deductions from their credit card account. Mr. & Mrs. F have given a representative their credit card details but they have not yet signed a direct debt authority.

A representative again rang, this time offering Mr. & Mrs. F them the package without them having to swap banks. Mrs. F countered with, 'Why would we do that - pay for what we already have?" Mrs. F reconfirmed that they wouldn't be proceeding with loan. The representative said that Mr. & Mrs. F would have to pay for the broking company's services and the fees to the bank.

Mrs. F was contacted by telephone by a representative who advised that the broking company would be sending a bill. This bill was received, followed by a letter of demand.

Case 7

12/11/2002 Mortgage Broker E

Mrs. G of Mildura has just gone through a divorce settlement and is struggling to pay her mortgage. Some friends recommended she talk to a firm of mortgage brokers. A broker came around the other night, which cost her $195, and she signed an agreement for their debt reduction program.

As it is still within the cooling off period[8] Mrs. E is having second thoughts. She is concerned about the amount of fees - $6,000 all up.

Case 8

15/5/2003 Mortgage Broker A

Mrs. H has signed up with a mortgage broker. At least, she thinks they are, although the representative does not say so. Also, there is nothing in the documentation to say that the company is a broker and there was no document of appointment.

The documents re•uire:
$375 up front;
$1,395 for savings projection; and
other fees and costs totaling approximately $10,000.

Mrs. H has cancelled, but the representative is saying that she is outside the cooling off period and owes $2,750.

Case 9

2/7/2003 Mortgage Broker A Lender H

'In early May, we were contacted by a telemarketer on behalf of (the broking company) in relation to a product that would help reduce the interest and length of our loan. We agreed to have a representative come out and explain their product, etc.

On the 5th of May, a consultant by the name of Mr. R came to our home to see us and explain how the "Debt Reduction Program" works. At this appointment we were asked to pay a deposit of $395 towards completing the relevant •uestionnaire and continue, at which time another $1,395 would be re•uired for a Savings Projection to be prepared. (Mr. R stayed for 2 ½ hours and advised that we could save 1 ½ years on our home loan – up to $3,000 – although he couldn't say exactly how much we would save. Our present home loan is at 5.9% or 4.9%. It was represented to us that although the new loan would be at 6.75%, there was going to be a credit card attached and this was how the savings was to be made).

We explained to Mr. R that as we still did not understand how the product worked, we were not prepared to pay any more than the $395. Mr. R then made a telephone call to an associate in the office who then asked to speak with my wife and advised her that they would waive this next payment if we continued. We explained that we were interested, however as we still did not understand the product, we were advised by Mr. R that a "Senior Consultant" would be happy to come out and give a full explanation of their product and how it works with the completed "Savings Projection Summary".

Mr. B was the Senior Consultant who came and saw us. He did explain how the product worked, however advised that a decision was needed right then and there as he was already running late for another client. We wanted to discuss this by ourselves, as it was a major financial decision, however we were again advised that a decision had to be made that night, and we signed the relevant application documentation. (Mr. B had stayed for 1 ½ hours).

We decided not to proceed and we faxed them a letter explaining that we no longer wished to proceed, as we will be retaining our existing mortgage with Members' E•uity. We received a Tax Invoice for $2,950.00 re•uesting payment within 14 days. As we are not implementing their recommended product, we believe that such fees are not warranted.

In summary, we believe that the service (or lack of it) provided by the mortgage broker was not professional and that extreme pressure was applied for both my wife and I to sign then and there. As stated in my letter to them, how can a couple make a financial decision with a representative sitting at the same table opposite them, advising them to hurry and made a decision as he is "running late for another appointment"?

Since the mortgage broker has become aware that we were reluctant to proceed and sign the relevant loan documentation, I was advised that if we did not go through with it, fees of approximately $5,950.00 would be implemented

My wife and I believe that we have not been dealt with in a professional manner.We have forwarded a copy of this email to the mortgage broker as advised by the ASIC Infoline.

Case 10

8/8/2003 Mortgage Broker I Lender B

Mr. & Mrs. J were concerned with conflicting information in the forms they received from the mortgage broker and the bank.

After an initial marketing telephone call, the broker's agents came to their house on two occasions, selling a debt reduction program and also offering to find a loan for them. A program was offered where the broker's agents came to their house on a monthly basis and reviewed their expenditure, etc. The cost for this was $5,000 but Mr. & Mrs. J say they did not sign up for this.

Mr. & Mrs. J had already been considering refinancing their mortgage but now find that the fees in the new bank's loan contract differ from those in the broker's offer. The terms of the loan are also contrary to what they were seeking. They are planning to sell their home in a couple of years and payout their loan but the new offer includes line of credit and pay their living expenses by using a credit card.

Mr. & Mrs. J do not want to enter into a contract until everything is clarified. The broker's agent has told them that if they do not proceed it will still cost $350 for work already completed.

Case 11

21/8/2003 Mortgage Broker I Lender T

Mr. & Mrs. K were attracted to a broker refinanced home loan which they understood to involve them putting all their income into a line-of-credit and living off a credit card, thereby paying off their loan •uicker. Mr. & Mrs. K believed the system would work for them.

Initially, the broker rang them and then came to their house where documents were signed. A month after the refinance settlement occurred, Mr. & Mrs. K had received nothing from the lender and had not made any payments. They rang the lender to see what was happening. The lender said they would send out the information but it was not until Mr. & Mrs. F rang the broker that they received a call from the lender. The lender advised that the new loan they had did not include a line-of-credit or a credit card.

This effectively meant that Mr. & Mrs. K had ended up with the same loan as they already had but with a different lender and had paid $6,000 for it. The $6,000 fee has been capitalised into their new loan.

The broker is now saying that he did not understand that they wanted the loan program with the line-of-credit system, even though the budget he prepared was based on that assumption. Now instead of a line-of-credit and credit card account with 55 days interest free, they are told that they have to have two accounts, a business account and a savings account.

Case 12

29/8/2003 Broker B Lender A

Mr. & Mrs. L received unsolicited phone calls from a representative of a mortgage broker. That representative advised them that the broker could show them how to save thousands of dollars on their home loan. Following a number of phone calls Mr. L agreed to allow the broker to visit him and his wife at their home for a discussion.

'M' attended Mr. & Mrs. L's home where they advised him that they had recently refinanced their home loan and were reluctant to do so again. Their home loan at that time consisted of two facilities: the majority of funds were repaid by principal and interest repayments, and the minority, being $40,000, through a line-of-credit which was used for their business. Our clients advised M that they liked to do all their banking on the internet, as this was convenient for their small business. Mrs. L worked in the business part-time and Mr. L full-time.

M drew graphs, which illustrated how they could save '$100,000 on their mortgage'. His advice essentially was based on one line-of-credit facility into which all income was paid and expenses drawn upon. On the basis of the following representations, Mr. & Mrs. L signed the finance brokerage agreement and loan application forms:

- If they paid all of their income into the line-of-credit they will save money as their interest payments will be reduced;
- All other bank accounts could be closed as they could do all of their banking online using the line-of-credit account, thereby saving on account keeping and transfer fees;
- Further, all business che•ues could be deposited at the Post Office;
- Our clients would have enough money to pay off their current ANZ credit card;
- Our clients did not need to get a financial advisor as the broker not only negotiates credit for their high fee but also provides ongoing financial advice - M will personally be on call whenever they need him;
- M would attend their property following settlement of the loan to set up a facility whereby their new bank credit card debt would be paid off automatically by the line-of-credit each month, thereby not incurring interest at a higher rate;
- Following settlement of the loan, he, or another employee, would attend their home and provide software, and instructions on its use, to create a budget plan; and
- If Mr. & Mrs. L made repayments according to that plan, in approximately two year's time they would have enough money to be able to purchase an investment property.

At that meeting Mr. & Mrs. L advised M of the debts they wished to be paid by the purported refinance. There was no mention at that time of the payment of break fees, and Mr. & Mrs. L assumed they would be charged approximately $600 to $1,000 in break costs to pay out their recently refinanced loan.

Mr. & Mrs. L received confirmation from the broker that their loan had been approved. It was arranged for Mr. & Mrs. L's solicitors to attend at their home one day at 12 noon. At approximately 10am Mr. L called Mrs. L, who was out, to advise her that the solicitors were on their way and were in a hurry. Mrs. L rushed home and Mr. L had already signed the documentation. Mrs. L felt pressured by the time restrictions placed on her by the solicitors and •uickly signed the documentation.

Following the signing of the documentation, Mr. & Mrs. L were advised by their previous lender, that the total break and other fees were $2,743.49, fees which were substantially higher than anticipated. They contacted M to en•uire why they hadn't been advised that the fee would be that high. He advised them that he assumed it would be the normal amount and he should have asked them to investigate the fees. He stated that if he'd known it was going to cost that much he would not have advised them to refinance.

M further stated that the only consolation he could offer them was that they were going to be making more than ade•uate savings on the mortgage, savings that would cover the additional fees.

Mr. & Mrs. L conse•uently re•uested that the brokerage fees be paid by installments as the loan amount, taking into account the break fees and additional fees, was not sufficient to cover all their debts. M attended their home and provided them with a direct debit form, agreeing to enter into a direct debit arrangement whereby Mr. & Mrs. L would pay $200 per month from their credit card. They signed that form and provided it to him at that meeting.

Following settlement our clients discovered that not only had their former bank credit card debt not been paid off, but also that the direct debit form was not processed and the full amount of brokerage fees were disbursed from the proceeds at settlement.

After settlement, Mr. & Mrs. L completed a deposit form provided by the new bank and attempted to deposit a che•ue at the Post Office. They were advised that they were unable to do so as the che•ue was made out to their business and the account was in their personal names. They were advised to amend their account name to add 'trading as ( )'.

Following incorrect advice from a number of persons, Mr. & Mrs. L were advised that they would be unable to deposit those che•ues into the line-of-credit account as the new account couldn't have a business name.

Our clients are conse•uently unable to close their old bank account and must attend a branch to deposit their business che•ues into that account. They must then transfer those funds by internet into the new line-of-credit account. Further, they are paying all of their expenses with the credit card, which they then have to pay by an internet transfer from the line-of-credit account.

When our clients discussed the problem with M, he advised them to save the che•ues and deposit them all at the end of the month, contrary to his original advice that in order to reduce the interest paid and therefore save money they must deposit all che•ues and income as soon as it is received. Clearly, the purported savings will not be made through such a practice. Mr. & Mrs. l had by now lost confidence in M as a financial advisor as they felt he was not working in their best interests and had not even delivered all the agreed services – the budget plan and software had not been delivered.

Mr. & Mrs. L are currently in no better a financial position, and in fact may be in a worse position, than they were with their previous facilities. The line-of-credit account has been at its limit since settlement – expenses being e•ual to their income. Mr. & Mrs. L feel that they will have significant difficulty in reducing the principal given they still have a $5,000 credit card debt. They feel they were in a more advantageous position with their previous facility where they were able to make payments of principal and interest on one facility and, if necessary, maintain the $40,000 line of credit at its limit. Mr. & Mrs. L will only be able to save money, compared with their previous facility, if they make greater repayments, a solution which is clearly not possible.

Case 13

Broker A Lender H

After receiving a telephone call offering to cut years off their home loan, Mr. and Mrs. M agreed to a visit by a mortgage broker.

A budget has been drawn up which shows that after all living expenses and paying the above debts, the M's have $295 left over per month.

The broker is proposing that the M's refinance with a line-of-credit – the interest rate would be 6.72% - slightly higher than their current line of credit @ 6.57%.

The amount to be borrowed would be $87,462. This would pay:
the current mortgage $81,000;
the broking company's fees about $5,000; and
bank fees, etc. about $1,400.

The mortgage analysis comparison provided by the broker shows a $79,230 saving over 12 years using their Mortgage Reduction Program (MRP).

The M's do not see any benefit in what has been offered and want to cancel the deal. No refinance has been arranged, but the M's are currently in dispute with the broking company who want their fees - around $4,000.

Case 14

Broker G Lender C

In early 2001, Ms O was introduced to a local agent of an interstate mortgage broker.

At that time her situation was as follows:

- she was in her early sixties
- working part-time with a gross income of less than $30,000 pa
- partner was paying $125 per week towards household expenses
- hopeful of earning a limited amount - $2,000 to $5,000 pa – from a part-time business she ran from home, but this did not eventuate
- credit union home loan of $52,000 secured against a house in her sole name
- payments of $170 per week scheduled to repay loan by 2013 – 12 years

The agent visited her at home and did a presentation on how she could pay off her home loan in 6 years by restructuring her finance through the company he represented.

Ms O proceeded with the offer and at settlement:

- paid out credit union $52,014
- paid out 3 credit cards $10,038
- legal fees, stamp duty, etc. $1,425
- fees to the broker $3,190
- total loan was $87,000

It seems that the facility was an interest only line-of-credit. Ms O received 'independent advice' on the product from a solicitor introduced by the broker's agent.

Some months later, the new bank offered Ms O another facility, which she understood to be a line-of-credit but was actually a credit card. She accepted this and soon owed another $3,000.

The broker made a couple of visits to Ms O but she did not find him helpful in explaining how the new loan arrangement was meant to be working, or why it wasn't achieving the principal reductions she had been led to believe it would. He took copies of her loan and credit card statements but did not get back to her and she was unable to contact him when she tried to follow him up herself.

Due to some personal grief, Ms O developed a gambling problem and was falling further into debt. Her income had reduced due to less working hours and she had been unable to activate her home business due to her depression. She was concerned about her financial situation.

In August 2002 she contacted the broking company directly, having been unable to contact the broker she originally saw and arranged for another agent to call. She advised this broker of her gambling problem.
broker arranged an increase in her line-of-credit facility of $22,000. The application stated the purpose of increase was to refinance two credit card debts totaling $9,000. The application included a copy of Ms O's PAYG certificate showing gross income of $27,061 for 2001/02.

By February 2003:

- the $13,000 net increase in the line-of-credit was used up
- only the minimum interest payment was being made
- there was no capacity in the line-of-credit to meet that month's sweep from the connected credit card of $1,800
- Ms O had no funds to meet other bills such as rates.

The new agent had not made the agreed follow-up visits. He could not even be contacted and it transpired he had moved interstate.

After several calls by Ms O to the broking company, the Director of Sales and Customer Services visited when he was in her city. He was unable to offer much of a solution to her financial situation, other than to advise her to:

- stay with her current facility;
- accept her partner's offer to contribute to repayments. Ms O's partner is not an owner of the property;

and to offer

- some money management forms;
- telephone access to advice from the interstate office; and
- perhaps some home visits from himself when in was in town.

Case 15

Broker B Lender I

Mr & Mrs. • received an unsolicited phone call from B offering to take thousands of dollars and years off their mortgage and agreed to a home visit from a representative.

The representative came in the evening and stayed for several hours. He claimed he could cut years off their home loan. This family had a two year old and a one year old at the time so the long evening visit was not all that convenient. Mrs. • in particular said that the explanation was far too convoluted for her to understand and when asked for explanations, the rep. just repeated himself about the money they could save, etc. The deal was that they were to pay almost $3,000 for the plan to be put into effect.

A family member with some financial skills heard about this and arranged to be present for the next visit of the representative. When he was asked to explain what was being proposed, they received the familiar outline of promises of a complicated 'line-of-credit' arrangement involving more than one loan account and a credit card but when asked for actual details of what was proposed, he refused to provide this until Mr. & Mrs. • had signed up for the $3,000 plan. Spreadsheet projections of savings of money and time off their home loan were provided but it was not clear this were based on an underestimate of expenditure. There was also an underestimate of the early termination fee they would have to pay to their current mortgagee.

The outcome was that Mr. & Mrs. • did not proceed with B despite several follow up phone calls. In fact, when they no longer had to pay an early termination fee to refinance, they saw another mortgage broker who assisted them to refinance into a better deal with ANZ. This mortgage broker was very good and operated as brokers should with the borrowers' interests paramount - a full assessment of their situation including their current mortgage, no pressure about a particular product and a disclosure that he would receive a commission from ANZ for his work.

Case 16

Mr. and Mrs. J had a normal variable rate loan with a mortgage originator. The balance of the loan was $94,000. Mr. and Mrs. J were "cold called" by someone wanting to talk about their "special mortgage deal". As Mr. and Mrs. J wanted to increase their loan to buy a car they agreed to the visit. At all times Mr. and Mrs. J thought the person who called was a mobile lender and not a finance broker.

Mr. and Mrs. J were given papers to sign some papers to apply for a loan for $100,000. As they believed the papers were just an application form they signed. Mr. and Mrs. J had applied for a line-of-credit loan with a major bank. This type of loan was completely inappropriate in their circumstances and more expensive. When the loan settled, they were shocked to find there was no money available to buy a car. They discovered that the "mobile lender" was in fact a finance broker and a fee of $2,950 had been taken at settlement to pay that finance broker. In total Mr. and Mrs. J had paid a total of around $4,000 in fees (including the bank's application fees and solicitor's costs) to move to a loan that was more expensive.

Case 17

Lender C

Mrs. N answered an unsolicited phone call right on dinnertime. The caller claimed to be from a bank. The caller then re•uested that Mrs. N provide a few personal and financial details to enable their consultants to prepare an offer that would enable Nr & Mrs. N to "pay off their mortgage in seven years". Mrs. N was very busy with the family dinner and other evening tasks – she has four children – but she gave the details.

The details sought were:

- how much was presently owed on their mortgage
- the value of their home
- their household income
- number of children

Another woman rang back about an hour later, reaffirming the offer that "their mortgage could be paid off in 7 years". Mrs. N stated that she and her husband were already planning to pay off their existing mortgage in 7 years. The representative asked "Are you doing that by making extra repayments?" When Mrs. N affirmed that, the representative stated" Well, with our offer, you'll pay off your mortgage in 7 years without making any additional repayments. You just need to use our line-of-credit mortgage and interest free credit card."

Mrs. N was sceptical that a home loan could be reduced to such a short term without making extra repayments and asked the representative for an explanation of how the system worked. The representative explained that she was just a call centre officer but she could arrange for a representative who understood the product in detail to make a personal visit to explain it more fully.

Mrs. N was reluctant to arrange such an appointment without understanding the offer and asked if some information could be sent out. The representative could not provide such information and only reiterated the offer to have a representative call to explain the product. Mrs. N did not proceed with the offer.

Case 18

Broker H

A broking company contacted Mrs. • and an arrangement was made for a salesperson to attend her home. A salesperson arrived about 7:00 pm on a Friday night – and didn't leave until 12 midnight, after the client and her partner had signed an agreement. Mrs. • said that the salesman actually refused to leave until they had signed.

The cost was over $4,000 and Mrs. • was reluctant to proceed. By mid-week she had decided to cancel. She contacted an advice service to ask what rights she had. She rang back the next day and said that the company had agreed to allow them to rescind the agreement, and so no assistance was re•uired.

There was apparently no attempt to comply with the ACT door-to-door sales legislation, which would have given a clear right to cool off.

Case 19

Mr. & Mrs. R received a phone call at home one night and were asked if they wanted someone to show them a financial plan, which would make them better off. They were told that they would be able to pay their home loan off years earlier.

Mr. & Mrs. R accepted an offer for someone to visit them at their home who provided them with a host of documents including a contract with a finance broker. Upon reading the documents after the broker left, they were concerned about the budget prepared and realised that it was not sustainable. They also noticed that the estimated costs of refinancing their $144,500.00 home loan were very high. The costs, if they had gone ahead, would have been close to $10,000.

When the loan contracts arrived they found out that the interest rate was 6.23% when their current home loan rate with their existing financier was only 5.8%.

Case 20

Mr & Mrs S were visited by a Broker E representative, after being cold-called. After the broker had been in their home for about three hours, Julie needed to collect her child from school. She says the broker rushed her into signing an agreement and paying a $195 fee. Mr & Mrs S were told a senior broker would call around next.

The second meeting lasted several more hours, resulting in a 'Mortgage Efficiency Freedom Program'. The plan suggests budgeting and refinancing would save them $97,092 in interest and reduce their mortgage term from 22 to 9 years. "We felt really pressured into signing," says Mr S.

Mrs S says they didn't even get a choice of banks. "There was no list of lenders to compare." Mr S believes the savings plan, which included paying their salaries into an offset account, under budgeted for living expenses.

They heard nothing from the broker for around six weeks, during which time they made several phone calls to the company but nobody could help them. "Once they had our signature there was a complete lack of information," says Mr S. They next phoned the lender who thought the broker's fee ($5,950 when the loan settles) was too much to pay and advised against going through with the refinance. But the broker's cancellation fee was still $2,000 – they were well outside the 5-day cooling-off period. "We feel cheated and don't think we should have to pay this fee," says Julie. "We'd need another bank loan to pay it. We shouldn't be charged $2,000 for a graph generated by a computer."

Case 21

Ms J had a standard variable interest rate home loan with an outstanding balance of $114,000. Ms J was cold called by a telemarketer offering to talk to her about how she could save money on her mortgage. Ms J was interested in increasing her loan to buy a computer (to work from home) and agreed to a visit. The person who visited Ms J only discussed finance with one particular lender, and did not disclose that he was a broker. He led Ms J to believe he acted for that lender, and that she would only have to pay the lender's application and loan fees. The broker gave Ms J a series of documents to sign. These included a broker agreement (which was not explained to her) and an application for a loan of $120,000.

In fact, the loan was to be provided through a line-of-credit. This type of finance was completely inappropriate and unnecessary for Ms J, while the interest rate was more expensive than on her existing loan. When the loan settled, Ms J paid around $4,000 in fees, including nearly $3,000 to the broker, as

well as the lender's application fees and solicitor's costs. This meant there were insufficient additional funds available for her to buy a computer.

Case 22

Mr. and Mrs. F were contacted by a representative of a broker firm, who said that he could arrange a budget plan for them, designed to cut thousands of dollars and many years off their mortgage. Mr. and Mrs. F agreed for the broker to visit them at home. They stipulated to the representative, however, that they wanted a "no obligation" discussion. The representative spent three hours at their home, providing them with calculations showing how they could save several years in repayments. He then announced that he could go no further unless Mr. and Mrs. F agreed to pay a deposit.

Mr. and Mrs. F then signed an agreement committing them to paying $4,000 for a plan specifying the amount they could save in repayments, and how this could be achieved. They were then provided with a cancellation notice under the door-to-door sales provisions of the Fair Trading Act (Victoria); the notice was not completed correctly. After considering the matter, Mr. and Mrs. F attempted to cancel the agreement within the five-day period allowed by the Fair Trading Act for contracts signed at home. The broker firm told them that the five-day period had in fact expired, as it included the weekend. Mr. and Mrs. F argued the point with the broker firm, and the representative eventually conceded that five days meant five business days and so the weekend should not be counted. However, the representative then told Mr. and Mrs. F that they would still be liable for reasonable expenses so far, and that these were over $2000. Mr. and Mrs. F contacted CCLS for advice, and a solicitor wrote to the brokers.
Initially, the broker firm refused to acknowledge any failure to comply with the Fair Trading Act and insisted on being paid $1000. However, CCLS was subse•uently able to get the firm to agree to release Mr. and Mrs. F from any further obligation to pay money.

Case 23

Ms Y received an unsolicited call from a finance broker, who said that he could "save her money" on her home loan. Ms Y and her husband were interested, and arranged for the broker to visit their home on a weekday evening. The broker arrived at 8 pm, and explained that he would need to get an idea of their financial position and goals, and then discuss the specific home loan product he endorsed and how it would help them, given their financial position. Ms Y and her husband were genuinely interested in hearing about the product. By 11 pm, the broker had not finished his presentation. Ms Y and her husband explained that they were too tired to concentrate and that they would not sign any contracts that night, although they would be happy if the broker came back another time to continue their discussion. Ms Y asked the broker to leave, but he refused,saying, "You promised me a cup of coffee". The broker continued to pressure Ms Y and her husband to sign a contract that evening, and said that it would be unlikely he could visit again, as he was too busy.

After many pointed re•uests to leave, the broker eventually left Ms Y's home at 12.15 am. He refused to leave any documentation or contracts for Ms Y and her husband to review. At no time during the meeting did he describe the interest rate, or the terms and conditions of the loan. He was even reluctant to leave a business card. The next day, Ms Y made an official complaint about the broker's conduct to the broker's head office. However, the office was unsympathetic, and said only that their staff were very enthusiastic about making sure their clients received "a good deal".

Case 24

Mr & Mrs D had a regular home loan at a major bank. Mr D worked as a labourer and Mrs D receives social security. Mr & Mrs D's annual income combined was around $35,000 per annum. Mr and Mrs D have one dependant disabled child.

Mr & Mrs D were barely able to manage their current repayments on their current loan. Mr & Mrs D were cold called by a man (Mr. N) one afternoon claiming they could save thousands on their home loan. Mr. D invited him in to their home, as he knew he needed to borrow some extra money to complete some renovations on their home. Mr. N told Mr & Mrs D that he could save them 11 years off their home loan and thousands dollars of interest. He explained that all they would have to do was to live off their credit card and pay both of their incomes into the loan account. At no time did Mr. N explain that to achieve the projected savings Mr & Mrs D would have to make greater repayments. At the time of the 1st interview both Mr & Mrs D explained they could not read very well.

Mr. N returned to see Mr & Mrs D a few weeks later with a financial plan and a budget they must stick to. Mr & Mrs D were told they needed to refinance to another bank and get a line of credit loan with a credit card attached. Mr & Mrs D were also told to close their savings account and all expenses they had must now be put on the credit card. Mr. N did not read the plan to Mr & Mrs D or explain that they had to pay him a $5500 fee for the plan.

Mr & Mrs D are now considerably worse off financially as a result of the visit from Mr. N. They owe around $7000 on Mr. D's credit card that is attached to the loan. The loan is almost fully drawn and has not been reducing. Mr & Mrs D have incurred substantial fees because they fre•uently need to withdraw cash from their loan account for everyday living as many retailers in their area do not accept credit cards for payment. The line of credit loan has proved to be a very inappropriate loan for Mr & Mrs D in their circumstances. Worse, Mr & Mrs D have added to the term of their loan NOT reduced the term by 11 years.

Debt Reduction (Mortgage Minimisation)

This information is based on a number of individual cases seen by Credit Helpline and Consumer Credit Legal Service. The information may not apply to your particular situation – if in doubt obtain advice.

These “Cut 10 years off your home loan” proposals usually involve a budget plan and refinancing of the mortgage and other debts

Savings •uoted in most cases arise from:

- A budget that allocates a higher monthly amount to your home loan than you are currently paying; and/or
- Where other debts are also refinanced; a budget that allocates a higher monthly amount to all your debts throughout the term of the plan

In most cases it is not necessary to obtain a new mortgage product to reduce the term of your loan, as you can usually achieve this by simply increasing the repayment amount on your current home loan and other debts.

The Budget And Mortgage Refinancing

Mortgage minimisation businesses achieve most (if not all) claimed savings on home loans by setting up a budget that reduces the amount available for living expenses. The funds freed up (on paper) by this reduction in spending are then applied to the home loan. The problem with this is that although spending on living expenses can be achieved on paper, consumers might not actually be able to manage with this reduced spending.

These programs usually claim they can further reduce the home loan by setting up a system where the consumer deposits all their income into the mortgage account and then withdraws from this each month to pay for all their expenses from a credit card linked to the account.

In order to set up this system, a line-of-credit mortgage or offset account is re•uired. The “debt reduction” programs usually propose that you do this by refinancing your current mortgage with a line-of-credit mortgage.

In the experience of CCLS and Credit Helpline it can be difficult for people to manage a line of credit.

In most cases it is unnecessary to refinance your home loan to set up the system proposed by the debt reduction programs. The reasons for this are:

- Many consumers already have a mortgage off-set account or line-of-credit on their current loan
- If consumers do not have an existing off-set account or line of credit, in most cases they could set this up with their current lender

Furthermore even if consumers don’t have this type of product or cannot set it up with their current lender, the actual savings achieved through paying income into the mortgage are minimal, and are often less than the fees and charges relating to the new mortgage product.

Most consumers are no better off refinancing. In most cases the only savings that can be made are by sticking to the budget proposed by the mortgage minimisation business. These budgets are often unrealistic and impossible for the consumer to stick to and even if they are possible you can do this without refinancing.

Any representation therefore, that implies that refinancing of the mortgage is necessary to achieve the savings is in most cases misleading and deceptive.

Debt Consolidation

Sometimes the consolidation of other debts is included in a "debt reduction" plan.

It is not uncommon for statements to be made in relation to debt consolidation along the lines of "reduce your monthly payments and be debt free in less time".

It is possible to reduce your monthly payments and to pay out your total debt in less time with debt consolidation – but there is a catch.

The catch is that although monthly payments on the new loan may be less than current monthly payments on all debts, this will be so only for a short time. Also the monthly payments on the new loan remain constant, whereas a consumer with a number of debts finds that monthly debt payments reduce as each debt is finalised. Consumers who do not consolidate can shorten the period of the loan and save on interest payments by ensuring that the same amount is allocated towards debts, even as some debts are finalised.

If you are not in financial trouble (and need to reduce monthly payments), in most cases you will be better off not consolidating. If you want to shorten the period of your loans and save on interest you can allocate a set amount to all debt payments, as each debt is finalised do not reduce the amount of your debt payments, but apply the surplus amount to the other debts.

If you already have a mortgage facility that allows you to redraw, you may also wish to consider redrawing to pay out higher interest accounts such as credit cards. However this option should probably only be used as a last resort as most people will be tempted to incur further credit card debt once the balance is back to zero.

Analysing the Plan

This is simpler if your home loan is the only debt refinanced:

- Identify the monthly amount allocated to the home loan in the plan (Most of these plans do not specify what this amount is, you need to work it out by deducting the estimated monthly expenses from the stated monthly income);

  - Using this amount as the home loan payment, and a mortgage calculator such as http://www.commbank.com.au/personal/other/useful_tools.asp; or http://www.yourmortgage.com.au/calculators/ calculate the time in which your current home loan will be repaid and any interest savings.
- Compare this to the "savings" offered in the plan.

If the plan includes refinancing (consolidation) of other debts as well as the mortgage:

- Identify the monthly amount allocated to mortgage and debt payments in the plan (deduct the estimated monthly expenses estimate from the monthly income);
- Using spreadsheet software such as Excel, allocate that monthly amount across all debts, calculating when each debt will be finalised and then allocating the "spare" funds to another debt such as the mortgage. If you can't use excel, you may be able to draw this up on a chart using approximations.
- Compare how long it will take to finalise debts against the proposed debt reduction program.

In both cases, you will usually be better off without refinancing due to the costs in obtaining the new loan, paying out your current mortgage and payment of fees to the debt reduction firm.

(Footnotes)

[1] Line of credit loans (or loans with offset accounts) may not be more expensive than all standard loans – but generally the more features (or flexibility) a mortgage has, the higher the fees and/or interest rate.

[2] http://www.choice.com.au/viewArticle.aspx?id=103112&catId=100296&tid=100008&p=1

[3] This is how a 100% offset account works. Some offset accounts may offset at a rate less than the mortgage interest rate.

[4] See the front cover of "How to be Mortgage Free in 4 Easy Steps" available from Mortgage Free Australia Pty Ltd, 2003, which states "Own your home years sooner and save thousands of dollars in interest without, making extra repayments" . Also see Harj Gill & S. Therry,1996, "How to Own Your Home Years Sooner without making extra payments." The term "without making extra repayments" is repeated throughout this book, although analysis of the examples given shows that the dramatic reduction in mortgage terms are primarily achieved by increasing mortgage payments. Later editions of this book insert the word "interest" into the title – ie "without making extra interest payments". While technically more accurate, this new title is curious. It appears to admit that extra payments are required, because extra mortgage payments are almost always principal – not interest payments!

[5] Consumers may not initially identify "debt reduction" itself as a problem, but may refer to problems with a loan or a finance broker.

[6] http://www.peachhomeloans.com.au/newsletters/newsletter1.htm
http://www.loan.echoice.com.au/pages/h_tipsheet.html
http://www.prosolution.com.au/downloads/offset.pdf

[7] Report into mortgage brokers, prepared by the Consumer Credit Legal Centre NSW (Inc) and released by ASIC, 26 March 2003 http://www.asic.gov.au/asic/asic_pub.nsf/byheadline/Reports?opendocument

[8] Under Victoria's Fair Trading Act