Explaining Lenders Mortgage Insurance (LMI)

Most of you will have a mortgage, however, may still be slightly confused when discussing Lenders Mortgage Insurance with your family, children and friends. Here are some answers to some common questions.

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Who is insured?

The lender is insured. They are insured for the loss that may occur when a loan is defaulted and the property sale does not pay the lender back the full amount owing. Where a claim or loss is paid, the insurer may seek recovery from the borrower or any guarantor.

When is it required?

Lenders have different policies on when it is required. In general, lenders will pass the cost of insurance on to a borrower when the loan to value ratio (LVR) is over 80%.

How is it arranged?

The lender will prepare all the necessary documentation in order to arrange the insurance.

What does it cost?

The higher the LVR, the higher the % of loan amount that will be charged.

Example: an LVR of 85% may attract an LMI premium of 1.2% of the loan amount, whereas an LVR of 95% may attract 3%.

A payment of thousands of dollars may seem very tough when considering all the other costs involved with buying property, but it could result in strong wealth accumulation as it allows a buyer to purchase their desired property several years earlier than if they needed to save an extra 10% of the property price. That LMI premium could be made recouped over and over in capital growth. This is, of course, subject to the property market.

Do I have to pay the premium as a lump sum?

No. The cost of the LMI can be capitalised (or added to) your loan (which will increase your repayments slightly). It can be paid upfront if you have the money available.

When should I do it?

Whilst it is hard to provide advice on this, the advantage of getting into the property market sooner rather than later cannot be overlooked. Delaying a property purchase 2-3 years may mean missing 10-20% growth on the property. This could mean tens of thousands in equity for a cost of an LMI premium of a few thousand dollars.

What happens if I default?

If you default on a loan, the property may be at risk of being sold by the mortgagee. If the mortgagee sells your property and still does not recoup all their funds, the insurer pays the difference to the lender. The insurer can then chase you for the money (although this is rare).

Are GST and Stamp Duty payable?

GST is payable on all LMI premiums and is included in the quote provided by us or a lender. Different states will charge different rates of stamp duty on LMI premiums.