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going guarantor – be aware of the risks

Shakespeare may have said, “Neither a borrower nor a lender be” but at some stage most of us need to use debt for major purchases like a home. What we don’t need is someone else’s debt. Yet that’s just what older parents are agreeing to take on when they act as guarantor for their adult children’s home loans.

Earlier this year, a Commonwealth Bank survey found that around 87 percent of parents would like to help their children purchase a home. And lots are doing just that - and good on them. High property prices have seen a significant increase in loans involving support from family members, with many agreeing to act as guarantor.

There are a number of loans available that are specifically pitched at mum and dad acting as guarantor. St George for example offers a Family Pledge loan, where parents can nominate the amount of the loan they wish to act as guarantor for. The Commonwealth Bank offers a Family Support option.

Getting parents to guarantee a mortgage can let first homebuyers avoid extra costs like lenders’ mortgage

insurance. It provides big saving for the kids - but it may not be so good for older parents.

No matter how it is marketed, acting as guarantor is considerably more than a mere formality. It means you become responsible for the loan, if your adult child can’t make the repayments.

In today’s environment of generous grants and historically low rates, which encourage home ownership, older parents need to be especially careful about going guarantor. It may only take a modest rise in rates for some first homebuyers to face difficulty managing their mortgage.

By the time our grown-up offspring are looking at buying their first home, parents are typically at an age where they should be focusing on building their nest egg. Having to pay their children’s mortgage could seriously derail the best laid retirement plans. At worst, it could mean losing the roof over your own head.

That’s why it’s worth doing the sums with your kids to check that they can handle the loan, if – and when – rates start to climb.

Whatever you do, do not sign any document that makes you guarantor of your kids’ mortgage before getting legal advice. You need to know exactly where you stand and what your significant legal obligations are if you go guarantor.

There are other, less risky ways, parents can help out, like lending your kids part of the deposit, or offering your grown children rent-free living at home to really help them save. Having a bigger deposit would certainly take some of the sting out of rising loan repayments following from rising interest rates.

Saving for a first home is always a challenge, but it is achievable. For some tips on where you can cut spending to help build a deposit, tune into my TV show, Money For Jam, Wednesday nights on Nine.

Paul Clitheroe’s ‘Making Money’ for the week beginning 21 September 2009



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