

(dollarDEX, www.dollardex.com)

Editor's choice: A guide to home loans

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A home loan is usually the biggest financial transaction you'll ever make. But loans are sometimes taken without too much thought. And since HDB stopped providing market rate loans to HDB flat buyers, it means an additional 20,000 novices could be introduced to the arcane world of private-sector loans this year. That's a lot of new clients for the banks to gobble up. To ensure you don't get chewed up by slick marketing, scan this beginner's guide to home loans (useful for HDB or private properties).

What is an HDB market rate loan?

Regular concessionary HDB loans are subsidized and restricted to certain borrowers – for example, a first-time buyer of an HDB flat. Other buyers, such as those whose income exceed \$8,000 per month, or have already benefited from a concessionary rate loan, will have to get a "market-rate loan". The market-rate is tied to one set by POSB. But since January 1, HDB (via POSB) will no longer offer market-rate loans and borrowers will have to get loans from private-sector lenders, including the three big local banks and six foreign full banks. In a nutshell: financial institutions will provide housing loans to HDB flat buyers, just as they do to private property buyers.

What are the benefits for HDB flat buyers?

Loans from banks should in theory be more attractive because they are subject to more competitive pressure, rather than being tied to POSB's rate. This implies borrowers will be exposed to prevailing rates – low now but possibly much higher in future. Competition should also result in greater flexibility in loan packages and more customization. Indeed even borrowers eligible for concessionary rate loans may opt for an HDB loan from a bank, if it proves more aggressive. Even those already on a concessionary rate loan can refinance their HDB loan with a bank.

What are the catches?

In bad economic times (a low interest rate environment) bank loans might seem better, but as rates rise banks may be quicker to pass on the pain to borrowers. Rates for HDB properties may be higher than for private property loans too, for a number of reasons. These include the smaller sizes of the loans (and proportionately larger administrative cost), and the uncertainty around how a bank would repossess an HDB flat even though that is legally enforceable.

And if you have a personal loan or credit card with the bank to which you're now mortgaging your HDB flat, the flat may serve as collateral not just for your home loan but also for your other loans with the same bank.

If you are using CPF savings to pay for part of your property, then the property must be built on freehold or leasehold land with a remaining lease of at least 60 years. Older leasehold properties may be much harder to sell in as little as 10-15 years time.

How much can you borrow?

New home buyers will find that the maximum loan that a financial institution will provide is 80% of the purchase price, or market valuation of the property, whichever is lower. This amount is after deducting CPF monies used to buy the house. 10% of the down payment can come from CPF savings for private property, and 20% for HDB (by Jan 1 2008, this will also be 10%).

Example 1 - new home buyers: using CPF to pay for stamp and legal fees

Market valuation s\$1,000,000

- less 20% cash downpayment (assuming quantum at 80% of valuation) s\$200,000
- less CPF lump-sum withdrawn to pay for property s\$200,000
- less CPF monies used for payment of stamp and legal fees s\$35,000
- equals maximum loan quantum that can be obtained, s\$565,000

Example 2 - new home buyers: using cash to pay for stamp and legal fees

Market valuation s\$1,000,000

- less 20% cash downpayment (assuming quantum at 80% of valuation) s\$200,000
- less CPF lump-sum withdrawn to pay for property s\$200,000
- equals maximum loan quantum that can be obtained, s\$600,000
- cash used for payment of stamp and legal fees s\$35,000

How much should you borrow?

Conventional lenders allow you to dedicate up to around one third of your gross monthly income on your debt. But that's not to say you borrow to the hilt. Just because you can have access to 80% of a property's value doesn't mean you should. Think about the implications of loan repayments to your lifestyle before you borrow too much. Even if you use CPF to pay much of the installments, you don't want your cash flow curtailing other important spending

Your loan size should not depend too much on where interest rates are at any given time. Although rates are at low of 2-3 percent now, calculate what your monthly repayments would be if rates went up to 5% in a few years time. Plan for a worse case, so you didn't get into difficulties in future.

Refinancing

Refinancing refers to getting a housing loan from a bank or finance company to replace the one offered by the HDB at market interest rates. It makes sense when the rates of the new loan offset the costs of changing. With new bank loans starting at two per cent level, and HDB's market-rate loans still at 3.75 per cent, for a \$200,000 loan over 15 years a saving of \$1,200 a year would not be surprising.

For home owners with an existing mortgage, the maximum loan that a financier may provide is up to the full value of the outstanding loan or 100% of the market valuation of the property, whichever is lower, less all CPF funds withdrawn on the property undergoing refinancing.

However, many financial institutions will refinance your property at 100% market valuation only if it is a good case. Financiers are naturally concerned about the history of your current loan, so you need to be prepared to furnish your loan statements for the last one to two years.

What you pay for loans

Most financial institutions charge the following, although there are exceptions and waivers:

- Processing fee for processing a loan application.
- Pre-payment fee for paying back in part ("partial redemption") or in full ("full redemption") ahead of the loan repayment schedule. Some also require a notice period, for example, 3 months ahead, in writing. You may be able to give shorter notice and instead pay interest in-lieu-of notice.
- Third-party charges include valuation fee, legal fee (including the fee for the lawyer acting on behalf of the financial institution), stamp duty payable to the government, and insurance premium.
- Some institutions also charge for making an amendment to your original loan application or for cancelling a loan offer after accepting it.

Stamp duty

Stamp duty is payable by a buyer and every person who acquires a private residential property in Singapore. For a private property purchased directly from a developer, the stamp duty is payable upon the TOP (temporary occupation permit) of the property, or when you sell the property, whichever is earlier. If you have taken a mortgage loan from a financial institution, the bank's lawyer requires you to place the full amount of the stamp duty with them before the loan may be disbursed. Alternatively, you may place the stamp duty amount in the form of a fixed deposit with the financial institution. There are instances where the financial institutions waive this requirement until TOP.

For a property that is purchased in the resale market, the stamp duty is payable 14 days after signing the sale and purchase agreement if it is signed in Singapore. Where the document is signed outside Singapore, the stamp duty has to be paid within 30 days after the sale and purchase agreement is received in Singapore.

The stamp duty payable is calculated on a scale: 1% on the first \$180,000, 2% on the next \$180,000 and 3% thereafter.

Property insurance

Financial institutions require fire insurance policy to be taken on the property mortgaged. The insurance policy for property under construction is taken up upon the TOP of the property. The insurance policy for completed property must be taken up on or before the purchase completion date. Financial institutions generally offer free fire insurance for the first year from a selected insurance company. Mortgage reducing term assurance (MRTA) is required by some financial institutions, but not all.

Legal fees

Legal cost may range between 1% to 1.5% of property purchase price for completed properties

and 1% for properties under construction. However, there are instances where lawyers grant waivers for certain costs.

The exact details for HDB loans are not yet known, but it's likely they won't be so different from private home loans. With the latter, legal fees are paid to lawyers for acting in property transactions. Legal fees are calculated based on a scale cost set by the legal profession act. Lawyers are not allowed to charge more or less than the scale cost though he is allowed to waive the entire set of cost. The different sets of legal fees incurred in a property transaction are as follows: 1. Costs for acting in the purchase. 2. Costs for acting in the mortgage. 3. Costs for acting in the CPF withdrawal. These fees do not include disbursement expenses or out-of-pocket expenses incurred by the lawyer eg. Title search fees, cost book search fees, registration fees, legal requisitions.

The above costs are dependent on the property purchase price, loan amount and total CPF amount used respectively. You will also be required to pay for the cost charged by your bank's lawyers (if you are taking a loan) and CPF board's lawyer (if CPF funds are used for the purchase).

There are usually cost savings if a lawyer acts for more than one party in a property transaction, in these situations: same lawyer acting for both borrower and bank, same lawyer acting for buyer, seller, borrower and bank.

Documents required

Buying a house requires more paperwork than having a baby. You'll need all of the following: latest income tax notice of assessment. (for self-employed, please produce last two years notice of tax assessment), latest CPF statement of account, option to purchase (if any), and tenancy agreement (if any). And for those refinancing you'll need the latest CPF statement for CPF withdrawn under the residential property scheme and latest one to two years housing loan statements from current financier.

Bridging loan

Most financial institution would be glad to help you pay the 20% cash down payment for the purchase of your dream home, in the form of a bridging loan, if you have a current property to sell. The financial institution would require that the cash sales proceed from the sale of your current property be more than the bridging loan amount. The amount by which the cash proceeds must exceed the bridging loan amount varies among financiers.

Loan advice

Finally, if this simple user guide still seems complex you may want to seek advice. The best advisors can help you choose the right loan for your situation, and can even get certain fees waived for you. Try our home loans section.