Lenders Mortgage Insurance (LMI)

LMI is insurance that a lender takes out to insure itself against the risk of not recovering the outstanding loan balance if you, the borrower, are unable to meet your loan payments and the property is sold for less than the outstanding loan balance. It is important to understand that LMI covers the lender, not you (or any guarantor), even though the lender will usually pass on the cost of LMI to you. This means you cannot make a claim under the LMI - only the lender can make a claim. LMI is not mortgage protection insurance, which a borrower might separately take out to insure themselves against the risk of not being able to meet their loan payments.

How does LMI help me?

LMI helps people buy homes. If you want to buy a home and otherwise meet lender requirements, but do not have a substantial deposit (usually 20%), it can be difficult to find a lender who will lend to you. If you are in this situation, LMI helps make it easier for you to obtain mortgage finance. LMI does this by reducing the risk of loss to the lender if you stop paying your loan repayments. Because LMI reduces the risk for the lender, it makes them more likely to lend to you even though you do not have a substantial deposit at the outset.

How is the LMI premium paid?

The lender will pay the LMI premium to the insurer at settlement of your home purchase. This once off up-front payment covers the lender for the life of the loan (which can be up to 30 years). The amount of the LMI premium depends on the lender, how much it lends to you and the size of your deposit.

The lender will normally pass on the cost of this LMI premium to you as a fee. This is because the cost of buying LMI is a part of the lender's costs of providing loan finance to you. You can pay this cost to the lender at settlement or you may be able to include the cost as a part of the loan (so the cost of LMI will be added to your loan repayments over the term of your loan). Your lender, broker or financial advisor will be able to provide details about the options available to you.

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What happens if I cannot repay my loan and my home is sold?

If you cannot meet your loan repayments and no other resolution is found, your property may need to be sold to cover the outstanding loan amount. In this situation, sometimes the house is sold for less than the amount of the loan balance, leaving an amount still owing (this may be referred to as the 'shortfall'). If this happens, you as the borrower are obliged to repay that outstanding amount of the loan or shortfall. The LMI insurer will cover the loss for the lender in accordance with the LMI policy. Where there is a shortfall, the LMI insurer may then ask you, the borrower, to repay this directly to them, rather than to the lender.

Financial hardship

If you defaulted on your home loan, and your home is sold for an amount less than the loan balance outstanding and your lender made an LMI claim, you still owe the shortfall amount but you will need to repay that money to the insurer (rather than the lender).

All LMI insurers have hardship policies in place. It may be possible to arrange a deferral or payment plan to help you pay off the debt in instalments. LMI insurers recognise it may be difficult for you to pay off your debt if you are suffering financial hardship. For example, you have lost your job.

If you are in financial hardship, you should contact the insurer as soon as possible.

Where can I find more information about LMI?

You can contact your lender, or visit the financial information website of the Australian Securities and Investments Commission at **www.moneysmart.gov.au.**

Frequently Asked Questions (FAQs) about LMI can also be found at **www.understandinsurance.com.au/types-of-insurance/lenders-mortgage-insurance.**

Example

Andrew borrowed $400,000 to buy a home.

His deposit was less than the lender's requirement of 20%, so he paid the cost of the LMI.

Andrew later lost his job. Andrew experienced financial hardship and was unable to continue making the repayments.

The lender repossessed the home and sold it for $300,000 which was less than the value of the outstanding loan amount. The shortfall was $90,000.

Andrew remains obliged to pay this shortfall amount. The lender makes a claim on the LMI policy and the LMI insurer pays the lender $90,000.

The LMI insurer then has the right to seek repayment of the $90,000 from Andrew.

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