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Offset vs Redraw

How to **save thousands on your home loan** and pay your loan off sooner

Understand the differences and choose the right option for your financial goals.

Save money and pay off your home loan faster

Saving interest on your home loan can shave years off your repayments. But which option is best for you, an offset account or a redraw facility?

In this guide, we'll explore the key features, benefits, and differences between these two options, so you can make the right decision to suit your financial habits and goals.

Did you know? Every dollar saved through offset or redraw works as though you've made an extra repayment—lowering your interest and helping you own your home sooner.

What is an offset account?

An offset account is a separate bank account linked to your home loan. The balance in this account reduces the amount of your loan on which interest is charged.

Key features

- Works like a transaction account (depending on the lender)
- Allows you to deposit and withdraw funds as needed
- Salary deposits can go directly into this account, saving interest daily
- Comes with annual or monthly fees in most cases

EXAMPLE

$700,000	$10,000	$690,000
Loan Amount	*Offset account Balance*	*Interest Charged on*

Benefits

- Flexibility to access your money any time
- Immediate savings on interest with every deposit

How you can add funds to your offset account

An offset account is a transaction account linked to your home loan. You can make deposits or withdraw from it as you would with a regular transaction account.

What is a Redraw facility?

A redraw facility allows you to make extra repayments on your home loan while still giving you access to those funds if needed.

Key features

- Reduces the loan balance directly, saving on interest
- Funds are accessible via internet banking or transfers
- Often free of charge but less flexible than offset accounts

Benefits

- No fees for online redraws
- Helps disciplined savers reduce debt faster

EXAMPLE

$700,000	$10,000	$690,000
Loan Amount	*Extra repayments (Redraw balance):*	*Interest Charged on*

How can you make additional payments to a home loan

Nominated repayment: a nominated amount, above the minimum, paid at the chosen frequency. If at any point the minimum loan repayment amount exceeds the nominated repayment amount, the minimum will be payable.

Additional repayment: a set additional payment amount on top of the minimum repayment.

Direct salary crediting: direct crediting can be used to make additional payments on your home loan.

Once-off payments: a one-off payment to your loan account that can be applied against normal ongoing loan repayments due in the next month, if you have a variable-rate loan.

Offset vs redraw: side-by-side comparison

Feature	Offset account	Redraw facility
How it saves money	Reduces interest charged by offsetting loan balance	Directly reduces loan balance through extra repayments
Flexibility	High: works like a transaction account	Moderate: funds are accessible but require transfers
Fees	Usually annual or monthly fees	Usually fee-free for online redraws
Tax implications	Retains loan's tax-deductible status for investment loans	Redrawing funds may affect tax deductibility
Best for	Those with large, consistent savings	Disciplined savers happy to move funds manually

Avoiding a costly tax mistake when buying a home

If you're purchasing a home (your principal place of residence) that might later become an investment property, it's essential to plan carefully to avoid a common and expensive tax mistake. This mistake, once made, cannot be reversed and could cost you thousands in lost tax deductions.

Why loan interest deductibility matters

The tax deductibility of loan interest depends on whether the borrowed money is used to purchase an income-producing asset. Here's how it works:

- If you buy an investment property with a $600,000 loan, the interest on the loan is tax-deductible because the property generates income.
- If you save / make additional repayments of $50,000 into a redraw facility (which is legally considered a loan repayment) and later withdraw it for personal use (e.g. a holiday or a car), the interest on that portion is no longer tax-deductible. This is because the purpose of those funds redrawn have not been used for income-producing assets and therefore lose their tax deductibility.

The solution: use an offset account

Instead of a redraw facility, placing your savings into an offset account can preserve the future tax deductibility of your loan.

- An offset account operates like a savings account, reducing the interest charged on your home loan but without legally paying down the loan.
- If you later withdraw $50,000 from an offset account for personal use, the deductibility of the loan interest remains intact because the loan balance hasn't been reduced.

Why this is important when your principal place of residence becomes an investment

If you upgrade to a new home and turn your existing principal place of residence into an investment property, having used an offset account can save you thousands of dollars in tax deductions over the life of the loan.

- Offset account scenario: savings in your offset account can be used as a deposit for the new principal place of residence without impacting the tax-deductible portion of the loan on your investment property.
- Redraw facility scenario: funds redrawn are treated as new borrowings, if used for non-investment purposes (such as a deposit on a new principal place of residence), the tax deductibility on that portion of the loan is lost permanently.

Planning ahead for maximum tax benefits

If you're considering buying a principal place of residence that might later become an investment, plan strategically:

1. Minimise loan repayments: pay the minimum into the loan and store your additional funds in an offset account instead of a redraw.
2. Maximise savings: ensure that any additional amount above the minimum repayment that you can afford, is saved in the offset account to ensure you benefit from the reduced interest, while also building your savings.
    - This approach maximises your tax-deductible debt if the home later becomes an IP.

Caution: *This strategy requires discipline. If you spend your offset savings frivolously, it may be more detrimental to you than paying down the loan. The tax benefits are only worthwhile if the funds remain available for your next home purchase.*

The irreversible nature of loan repayments

Once you pay down a loan, the deductibility of that portion is lost forever if the funds are later used for non-income-producing purposes. Moving money from a redraw facility into an offset account doesn't reverse this.

Offset accounts: costs vs benefits

While offset accounts offer significant flexibility, they often come with higher costs:

- Higher interest rates: some lenders charge higher rates for loans with offset accounts
- Annual fees: many banks charge around
- $395 per year for offset accounts

Why choose a redraw facility

If you're confident your principal place of residence won't become an investment, a redraw facility may be more cost-effective:

- Lower costs: loans with redraw facilities often have lower interest rates and no annual offset account fees
- Less accessible: because funds in a redraw facility are less accessible (you need to move the funds from the loan into a savings account) you may be less likely to spend / draw on those funds for discretionary spending

Key tip: *compare the interest savings of a redraw only loan to the added costs of an offset account to determine which option works best for your circumstances.*

In summary

- In order to maximise long-term tax deductions, use an offset account if there's a chance your principal place of residence may become an investment property in the future.
- Opt for a redraw facility if you're sure your home won't be used as an investment, and you want to minimise the loan fees and attract the lowest interest rates.
- Always evaluate your discipline with savings and seek advice from a tax professional to optimise your strategy.

Which option is right for you?

Not sure which option to choose? Consider the following:

1. Your banking habits:
   - Visual savers or those who prefer convenience? Go with offset.
   - Happy to manage funds manually? Redraw may suit you.
2. Your financial goals:
   - Investment property? Offset helps retain tax deductions.
   - Owner-occupied loan? Redraw saves you fees.
3. Your savings habits:
   - Prefer to clearly see your exact savings regularly and a disciplined saver? Offset is more beneficial.
   - Happy to view your savings as available funds in the loan account, and/or prefer funds to be slightly less accessible? Redraw is a cost-effective choice

Speak to one of our expert mortgage brokers today to find the best option for your needs.