Your Guide to Financing your Home Purchase

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Your guide to financing your home purchase

When thinking about buying your first home you may be tempted to raise the money you need using what you believe to be the quickest and cheapest method. You may also be tempted by offers of shared ownership and the various schemes available which promise to make things more affordable for you.

What you may not realise is that how you choose to finance your home purchase can have an impact on how much say you have over what you can and cannot do with your property and, in some cases, could even mean that you do not actually own the home you buy.

Conventional mortgages with a bank or building society:

Money lent through a mortgage will be secured against your home. It may be in your name or in the joint names of you and your partner, or any other co-owners. All these possibilities have legal implications.

Because the mortgage is secured against your home, the lender will have certain rights over the property, meaning that you will not be able to do everything an outright owner could. For example, depending on the type of mortgage, you may not be able to rent your home out without prior written consent. You may also have to notify them if you intend to carry out structural building work and arrange to have home insurance in place for a sum which may exceed the level you believe is needed.

If the mortgage is in your sole name, you have ultimate responsibility for paying the debt, irrespective of any agreement you have made with anyone sharing the house with you.

If the mortgage is in joint names then you are all liable to make repayments, but be aware, if that other person fails to pay their share the mortgage lender is usually entitled to ask you to settle the debt instead. You should talk to your solicitor about what steps you can take to protect yourself.

You also need to be aware that:

- Your home will be at risk of repossession if you do not keep up your mortgage repayments;
- Mortgage arrears could affect your credit rating and may also result in debt recovery action being taken against you at court;
- Additional costs associated with a mortgage, such as early repayment fees, can be significant;
- You have to satisfy certain conditions to qualify for a mortgage, which vary from lender to lender and can be complex;
- All banks and building societies have a duty to lend responsibly and to assess affordability, which may limit the amount you can borrow;
- Most lenders will expect a deposit of at least 10%; and
- You may find it harder to get a mortgage if your circumstances are unusual, for example if you are self-employed or close to retirement age.

Mortgage agreements can be complex, but your solicitor should be familiar with your lender's detailed requirements and therefore advise you on all the possible implications. They can also help if you fall into arrears with your mortgage repayments and are being threatened with court proceedings.

Personal loans:

If you mortgage falls just short of what you need to make the purchase, you may consider taking out a small personal loan. If this is the case, you need to make sure that you can afford to repay this, along with making your mortgage repayments and settling any other costs associated with your purchase. Be aware also that not all lenders will accept a mortgage deposit financed by a personal loan.

An increasing number of personal loan providers are asking for loans to be guaranteed. If this happens, for example, family members agree to act as a guarantor, you and they need to be aware that if you fail to repay the loan when due, they could be asked to settle it for you.

If the money owed is not repaid, you or they could be taken to court and if this happens and a judgment is obtained, it could seriously affect both yours and their credit rating and may even result in the loss of your homes.

Bridging loans:

A bridging loan can be useful where you already own a property which you need to sell in order to buy a new one, but where you need to complete on the purchase of your new property before the sale of your old property is finalised. The problem with bridging loans is that they usually need to be repaid within six to 12 months so you need to make sure that you can still make the repayment if the sale of your old property has not been finalised or, even worse, if the sale falls through.

You need to be aware that if you have not sold your old home by the time you buy your new one, you may also have to pay a higher rate of Stamp Duty Land Tax. Your solicitor can advise on this and explore other ways the gap in funding could be plugged.

Government backed schemes:

There are currently three government backed schemes to help home buyers:

- The Help to Buy ISA, allowing first-time buyers to save towards a new home, with the government topping up their savings by 25%, up to a maximum of £3,000;

- The Help to Buy equity loan, which allows buyers to benefit from a government-backed loan of up to 20% of the purchase price (or 40% in London); and

- Lifetime ISAs which allow you to deposit £4,000 in each tax year. You can either deposit a lump sum or make multiple payments across the year. The government pay a 25% bonus on what is deposited each year. These can be opened between the ages of 18 and 39, and can be paid into until you reach the age of 50. If you already own a home, you can access your Lifetime ISA once you turn 60 to help fund retirement costs.

It is important to consider the details and how restrictions could affect you. For example, a Help to Buy equity loan is limited to new build properties, which tend to be more expensive than comparable older properties.

Some recent new build homes are sold as leasehold properties, meaning that, unlike freehold property, you will not own your new home outright and there may be restrictions on what you can do with it, along with additional ongoing costs, such as a service charge to keep the property and its garden in good order and possibly also a ground rent charge to the person who owns the land. These charges can, in some cases, be significant and it is important that you appreciate this before you commit to the purchase.

Ground rent charges, in particular, need to be considered carefully because some new build properties sold as leasehold may start off with a ground rent charge of £100 a year, but there will be a provision in the lease that allows this to be increased and may be prohibitive.

Your solicitor will be able to spot this type of provision and advise you on your total possible liability for future costs. They will be familiar with the various government funding schemes available and can advise the best option for you. It may be, for example, that you would be better off buying an older property, in which case the Help to Buy ISA would possibly work better for you because there is no new build condition attached; however, you need to ensure the property you are buying costs less than £250,000, or £450,000 in London.

Shared ownership schemes:

A shared ownership scheme allows you to buy a share of a home using whatever money you can raise. Typically, you can buy a 25 to 75% share in a property, with the remainder being owned by the housing association, which runs the scheme. You will need to repay any money borrowed to buy your share, for example, by making repayments to a mortgage provider, and you will need to pay rent (at a discounted rate) to the housing association.

Most shared ownership properties will be leasehold, which means there will be restrictions on what you can do with the property. For example, you may not be able to sublet your home. There will also likely be additional costs in the form of a service charge to cover the maintenance of shared areas.

When you sell, you will generally have to offer the housing association a right of first refusal, which could mean that selling your home takes longer than usual. Where the housing association decides that it does not want to buy your share of the property back, it may insist that anyone else wanting to buy it has to meet certain criteria, which could affect your ability to sell freely.

Purchasing with a friend or relative:

Most people cannot afford to buy a home outright using their own funds, and may consider buying with something else. While this can be a great way to get a foot on the property ladder, you must bear in mind that you will share ownership with that person and decisions will need to be made together.

Think about whether you will own the property jointly or in defined shares: in simple terms, if you own the property as ‘joint tenants’, your share will automatically pass to the other co-owner on your death. If you own the property as ‘tenants in common’, you will own a share of the property (usually dependant on how much you have paid) and your share will pass to those named in your Will, or, if there is no Will, according to set legal rules.

Your solicitor can explain the implications of owning property jointly in more detail, and prepare a declaration of trust which confirms your percentage share in the property.

The Bank of Mum and Dad:

Asking parents or grandparents for help might be an option if they can afford it, but this type of arrangement needs careful consideration. You need to agree whether any help will be as a gift or a loan, and if as a loan, whether any interest will be payable or share in the property expected. There are also potential tax implications to consider. Arrangements need to be documented to ensure there are no misunderstandings. It may also be necessary for your parents or grandparents to update their Wills and to prepare a letter of wishes explaining the arrangement, particularly if your inheritance may be reduced as a result.

Conclusion:

It is essential to have sufficient finance in place before committing yourself to a purchase and, where money needs to be borrowed, to understand the options available and the legal implications of the arrangement you decide to enter. These are just some of the options you may consider, but there are other types of arrangement which have their own, additional legal implications, such as equity release where you are an existing home owner.

Whichever option you choose to go with, you need to budget carefully and always discuss plans with your solicitor who will be familiar with the whole process and the consequences of any decisions you make.

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For more detailed advice about **financing your home purchase** and how it can affect you and your personal circumstances, **please contact your nearest Humphries Kirk office.**

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