

# Helping children/grandchildren onto the property ladder

## Outline

Buying a first home may seem like a distant dream for many younger people, in light of high mortgage rates and hefty property prices, and the cost of living squeeze. Younger people are increasingly struggling to save enough for a deposit, or

meet mortgage lenders' affordability criteria. This factsheet explores ways in which parents or grandparents can help younger family members onto the property ladder.

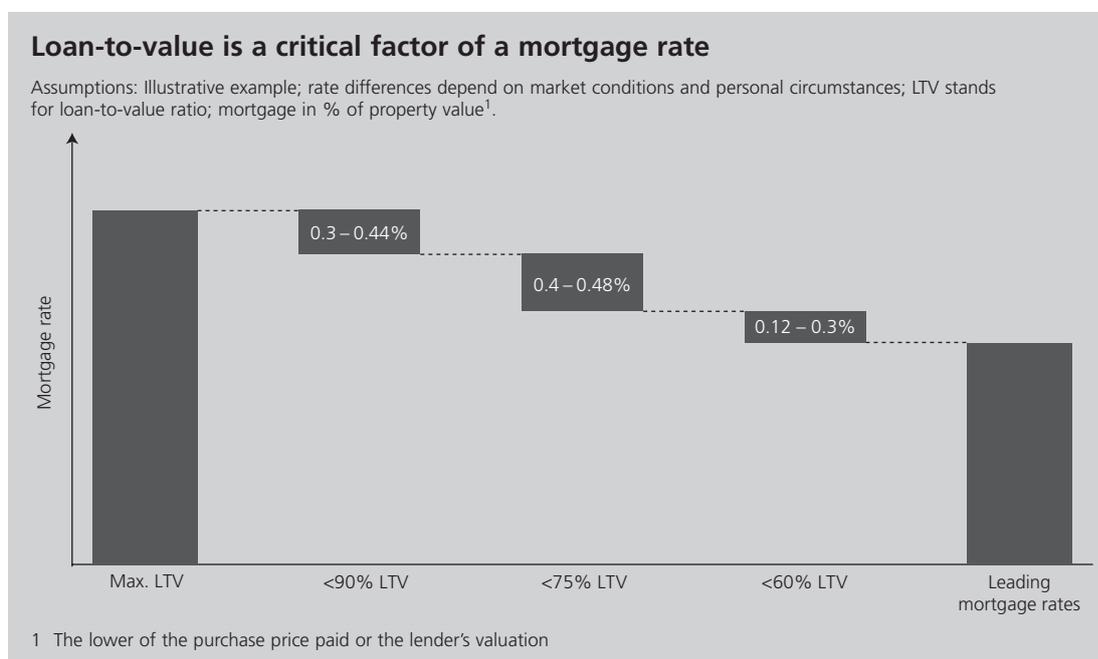
## Hurdles for first-time buyers

First-time buyers usually have to contribute at least a 5% or 10% deposit to fund the purchase of a property. Another key barrier is affordability. Mortgage lenders typically only lend up to 4.5x an applicant's income, and may not take all earnings – such as bonuses – into account. Some buyers reduce their monthly payments by taking a longer mortgage term than the standard 25 to 30 years, but this increases total interest costs until the loan is paid off.

Sometimes a mortgage lender's valuation may be lower than the purchase price, which increases

the deposit requirements as a result. For example, if the purchase price was £525,000, but the lender's survey only values the property at £500,000, then an additional £25,000 deposit would potentially need to be found if the price couldn't be re-negotiated in line with the valuation.

Typically, the larger the deposit, the better the mortgage rate (up to a point), which in turn means lower monthly repayments and better affordability. Market-leading mortgage rates are normally available for loan-to-value ratios (LTVs) of 60% or below – see illustration below.



## What a bigger deposit means for mortgage costs

The financial benefits of being in a more favourable LTV bracket can be huge, as the table overleaf illustrates. In the following sections we cover ways in which you might be able to help your children or grandchildren purchase their first home.

Options can include gifting (which can also mitigate inheritance tax liabilities on an estate), parental loans, joint borrower/sole proprietor mortgages, and early investing via junior ISAs to benefit from the snowball effect of compounding.

## Deposit vs mortgage costs

Assumptions: £500,000 purchase price; five-year fixed rate, over 25 years.

Deposit	5%	10%	15%	20%	25%	40%
Loan-to-value	95%	90%	85%	80%	75%	60%
Mortgage	£475,000	£450,000	£425,000	£400,000	£375,000	£300,000
Mortgage rate (assumed)	5.14%	4.69%	4.41%	4.41%	4.21%	4.09%
Monthly repayment cost	£2,816	£2,550	£2,341	£2,203	£2,023	£1,598
Total cost over 5 years (rounded)	£169,000	£153,000	£140,500	£132,000	£121,500	£96,000

### Gifting

You may be able to afford gifts on the back of a solid financial plan, providing funds for a deposit and also mitigating inheritance tax (IHT) liabilities on your estate at the same time. This option can be especially attractive if you have a large estate, given that a 40% IHT charge applies to assets above your allowances (up to £1,000,000 for married couples/civil partners with a family home) and exemptions. Gifts don't face any immediate

tax and are no longer part of the estate for IHT purposes if you survive for seven years.

**Tip:** Draw up a declaration of trust to retain ownership of the gift and protect it if your child splits from a partner. Consider how to financially compensate other children/beneficiaries to avoid any potential family friction.

### Parental loan

If you can't or don't want to gift, you can consider lending the money. Any debt obligations, including a parental loan, need to be declared to the mortgage lender and repayments form part of their affordability assessment. Family loans are often made interest-free. Consider potential tax implications on loan interest.

**Tip:** A written loan agreement provides clarity and avoids surprises by covering potential events such as bankruptcy or divorce. See checklist, right. Some lenders will not lend if there will be a legal

charge registered behind their own mortgage. This can limit the number of potential lenders.

Checklist for parental loan:

- Agreement signed in writing
- Interest rate and term stated
- Secured/charge on property
- Repayments
- Life cover/other insurance
- Provisions in case of bankruptcy/divorce
- Provisions in the event of death (parents or borrower)

### Joint borrower/sole proprietor mortgage

A parent or family member can apply for their income to be considered through a joint borrower sole proprietor mortgage. Second (parent) income can increase the maximum mortgage amount or lower the mortgage interest rate.

A joint borrower – for example, a parent with a daughter – is jointly liable for the mortgage debt if the owner (proprietor) fails to meet repayment

obligations. Sole proprietor means that the parent is not on the deeds and therefore won't be impacted by a 3% stamp duty surcharge or capital gains tax on second homes.

**Tip:** The parental age may affect the mortgage term that's available, which can impact on your monthly payment obligations.

### The 'snowball effect' of returns

Children and young adults can start saving towards a deposit from an early age. Friends and family can pay up to £9,000 annually into junior ISAs (for under-18s), which benefit from tax-free gains/interest. Adults can pay up to £20,000 into an ISA annually.

If you have a long-term time horizon and can tolerate the ups and downs of financial markets,

investment ISAs offer higher growth potential than cash ISAs or general savings accounts.

Some lenders will accept 'notional income' from UK-listed investments, whether or not any taxable income is actually being drawn from the investments yet. This means that you can avoid disturbing investments at a time when the markets/values might be depressed.

**Tip:** Start the saving plan as early as possible, as compounding – the ‘snowball effect’ – will increase the overall pot size substantially over time. Start

rolling your child’s snowball from the top of the hill, rather than half-way down.

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How Lumin can help

Many parents or grandparents are eager to help children or grandchildren with their first property purchase, but there are a number of routes you can go down. Some options, such as gifting,

have inheritance tax implications. Contact the experts at Lumin to learn more about how you can help family members onto the property ladder.

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