

Almary Green

> Independent Financial Advisers

MORTGAGE GUIDE

A Borrowing Guide for Home Buyers



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Introduction

Buying a home is often one of the most important decisions that an individual may make during their life. Therefore, it is vitally important that as much information as possible is obtained beforehand.

Despite the contraction of the mortgage market that has occurred as a result of the recent recession, there is still a bewildering array of products and options available to the property buyer. This guide attempts to clarify what is available from mortgage lenders and to explain the various types of deal that are on offer. In addition, it highlights a number of critical documents and financial issues that form part of the home-buying process.



How Much Can You Borrow?

How much an individual or couple can borrow has changed quite a lot in the last couple of years as we witness the lenders returning to much more conservative and, arguably, more sensible practices as a result of the credit crunch.

The amount that you can borrow for a mortgage varies from one mortgage lender to another but, as a general rule of thumb, you can borrow up to 4 times your income if you are borrowing as a single applicant or if you are a couple up to 4.5 times your joint income.

Some lenders base their lending on your ability to pay the monthly mortgage payment (the affordability) in addition to other everyday expenditure such as utility bills, council tax, insurance and even the weekly trip to the supermarket. Other debts that you may have will also be taken into the equation, to ensure that you are not over-committing yourself financially. Therefore any credit card balances, personal loans and HP agreements have to be disclosed. However the most important factor to consider here is not the maximum you can borrow, but what you can afford to pay comfortably, not just at the start of the mortgage but over the coming years. Therefore, seeking mortgage advice is very important. Whilst interest rates are low, borrowing 4 times your salary may well seem affordable, but you need to take a longer term view and seriously consider what you would need to pay monthly if interest rates were to rise.

What Size Deposit Is Required?

This is probably the most asked question at the moment. The days of not requiring a deposit at all or very little deposit are over. The most straightforward answer to the question is **as much as possible** and for two very good reasons. The first is that you want the smallest possible mortgage as that way you will have less to pay back and less interest will be charged, and secondly, the larger the deposit you can provide, the more competitive interest rate you will be offered.

Ideally, you should have at least a 15-25% deposit, as most lenders will offer a better interest rate with a higher deposit and you are less likely to be charged a High Lending Fee (see below.) Post credit crunch there are only a handful of lenders offering mortgages with an initial deposit of 10% and some of those are only offered to existing customers.

Remember: you need to have extra money for the other costs associated with buying a house. These include solicitor fees, estate agency fees (if applicable), stamp duty and removal costs.

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Mortgage Types

There is a very wide range of mortgage types and new products are being designed all the time. When looking for a mortgage, it is important to seek advice, as the market is constantly changing. As a basic guide, the main types are:



Standard Variable Rate

This is when the lender simply charges you their standard rate of interest. The interest rate – and your repayments – will go up and down from time to time as market conditions change. Most lenders take the fluctuations in the Bank of England base rate as a guide, however they are not compelled to do so.

Some lenders still set the level of repayment annually and if there are interest rate changes during the year, your payments only change at the end of the year with an appropriate adjustment.

If possible, it is advisable to find a lender who charges interest on a daily or monthly basis. This is particularly important if you are making overpayments as it means that the amount you owe is reduced immediately.

Discounted

This is similar to a variable rate in that the amount you pay varies as interest rates vary. However, the interest rate is normally reduced by a set amount for a set period, typically for up to 3 years. At the end of this term you revert to the standard variable rate. The discount is applied to the lender's standard variable rate. There is normally a penalty if you redeem the mortgage before the end of the discount period.

Fixed

A fixed rate mortgage is when you pay a set interest rate for a set period of time. The interest rate will not vary during this period whatever happens to interest rates at large. This can be useful as it means you know exactly what your payments will be in the early years of your mortgage and you can budget accordingly. However you will not receive a reduction in the rate if the lender reduces its rates. Your payments are fixed for a set period of time.

Fixed rates are available over a wide range of terms but the most common are 2, 3 and 5 years. At the end of the term you revert to the standard variable rate.

There is normally a penalty if you redeem the mortgage before the end of the fixed rate period. This penalty sometimes applies beyond this period, and it is important to check the conditions carefully.

Capped

Capped rate mortgages are a cross between variable rate and fixed rate mortgages, and are relatively uncommon whilst interest rates are low. The terms of the mortgage will state that the interest rate will not increase above a set level for a set period, but it may reduce if the lender's variable rate goes down to a lower level.

As with discounted and fixed rate mortgages, there is normally a penalty if you redeem the mortgage early.

Flexible

There are different types of flexible mortgage available but the basic principle is that it allows you to pay more, or less, than you would do normally, depending on your circumstances. For example, you may want to 'overpay' for a year or two, whilst interest rates are low and this may allow you to skip some payments if you were taking a break from work or were suffering financial hardship. Usually with this type of mortgage there are no or very few penalties to redeem the mortgage early.

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Cashback

This is when the lender pays you a sum of money as an incentive to apply for a mortgage. This can be useful for meeting some of the costs such as the legal fees. There is usually a penalty if you redeem the mortgage within a set period and the cashback often has to be repaid. In the current climate cashback mortgages are very few and far between.

Mortgage Repayment

In addition to considering the type of mortgage rate, you will need to consider the method by which you repay the amount borrowed. There are two repayment methods to consider:

Repayment Mortgage

This is the traditional way of repaying a mortgage. It is where you pay capital and interest each month and therefore if all payments are met the full amount is paid back by the end of the term, typically 20 - 25 years. In the early years of the mortgage, a large proportion of the payment made to the lender is interest and little is capital, but in time, more and more capital is repaid. At the end of the term all the capital is repaid, providing every payment due is paid.

The advantage of the repayment mortgage is its simplicity. The outstanding loan will reduce month by month (albeit only slowly in the early years).

Interest Only Mortgage

Under this type of scheme, only interest is repaid to the lender each month, and so monthly payments to the lender are lower. At the end of the term of the mortgage the full amount of capital is still outstanding. Therefore a sum of money equal to the outstanding loan will need to be available at the end of the term to pay off the mortgage. Traditionally an investment vehicle would be set up to generate capital to repay the loan at the end of the mortgage term. The cost of the investment vehicle is in addition to the payment to the lender. There are only a few lenders in the current climate who offer interest only mortgages without a repayment vehicle, and normally only with a larger deposit.

An investment vehicle relies on the performance of funds it is invested in. The performance of the funds cannot be guaranteed and you may not have sufficient to repay your mortgage at the end of the mortgage term. You should always take advice before considering this type of repayment method.

Fees

There are a number of potential fees associated with a mortgage.

Application fee

This fee is charged by the lender to cover the administrative expense of processing an application and is often charged for a specific product such as a fixed rate. It can also be known as a booking fee or arrangement fee. Some of this fee is deemed non-refundable from the outset, and once the application process is well advanced, it is usually considered entirely spent. Fees have risen in recent months and are generally between £999 and £1,999. In certain cases, they can be added to the loan.

High Lending Fee

The lender may impose a charge when the amount borrowed exceeds a certain percentage of the property's value. The charge is usually added to the loan. Lenders use this money to indemnify themselves against any financial loss they experience should they have to repossess a property due to payment default. Although you pay this fee, the protection it buys will only benefit the lender. It does not stop the lender or any insurer involved from trying to recover from you all or part of any financial losses they experience.

Other Fees

Valuations

Before a lender will consider an application for a mortgage they will require a standard valuation to be undertaken in order to ascertain the true value of the property being purchased. This will normally be arranged by the lender, but paid for by you. It is often not possible to choose a surveyor as the lender will make the instruction. Although many lenders provide a courtesy copy of the survey report to the borrower, this is purely for information only and you have no right to redress from the surveyor if the property is later found to have defects not listed in the valuation report.

The cost of a basic valuation depends upon the value of the property, but is normally in the region of around £300 - £500.

There are two more extensive reports which you may wish to consider.

Homebuyer's Report

You may wish to obtain a Homebuyer's Report, which provides you with more detailed information about the general condition of the property you are purchasing and it should highlight any major defects. In addition, unlike the basic survey, you can seek redress from the surveyor. The cost of a homebuyer's report is in the region of £500 - £1,000 depending on the value of the property.

Full Structural Survey

If you are concerned about the condition of the property in any way (if, for example, it is of an unusual design or construction), or if you simply want more reassurance, then you should consider commissioning a full structural survey. This should be arranged with a qualified surveyor. The surveyor can only access the areas specific to the property to be purchased and may not be able to conduct a thorough appraisal of any associated property, such as within a block of flats. The approximate cost of a full structural survey is likely to be in excess of £1,000.



Please note that if you pull out of the property purchase as a result of any defects highlighted from a survey you will not get a refund of any costs incurred to date.

Stamp Duty

Stamp Duty is a fee that is paid to the government as a tax when purchasing a property and this can add a significant amount to the costs involved. Properties below £125,000 are exempt from Stamp Duty, but the amount payable increases with the value of the property being purchased. The current rates are 1% of the full property value between £125,000 and £250,000, 3% of the full property value between £250,000 and £500,000, and 4% over £500,000. From 6 April 2011 for any property valued at £1,000,000 or more, the stamp duty payable will be 5%.

First time buyers will not have to pay stamp duty for any property they purchase up to the value of £250,000 between now and 25 March 2012. According to HM Revenue & Customs, a first time buyer is 'a person who has not acquired a freehold or leasehold interest in residential property in the UK or an equivalent interest elsewhere in the world'. This means if you have owned a property at any point in the past even if you do not own a property anymore you will not be considered a first-time buyer.

Key Documents and Processes

Key Facts Documents

Prior to completing a mortgage application, you must receive a Key Facts Document which outlines all the features and costs of the particular mortgage product that has been selected/recommended. It is either the responsibility of the lender (if you have applied directly) or the financial adviser (if you have sought advice) to provide this document in advance of making a mortgage application.

Disclosure of Personal Details

At the start of the application process you will be required to disclose information to enable the lender to undertake credit enquiries about you. This is to check that you are a good person to lend money to. The information you supply is checked against the information held about you with a Credit Reference Agency regarding the way you have handled a previous mortgage account, loan or credit card. If you are concerned about your previous credit history, then you should contact a credit reference agency, such as Experian or Equifax, to get a copy of your latest report.

It is important to be honest with a lender and disclose accurately the information requested. The lender will provide you with an initial decision often called an agreement/decision in principle (AIP/DIP). This confirms to you that subject to the necessary documents being supplied, the lender of choice is likely to provide you with a mortgage. This part of the mortgage process is often misunderstood; an AIP/DIP is not a guarantee of a mortgage merely an indication that the lender of choice may lend. If an AIP is provided by one lender it does not automatically mean another lender will come to the same conclusion.

In the current climate purchasers that require a mortgage are often asked to provide evidence that they can borrow and some purchasers agree to have an AIP carried out. However, you should note that applying for an AIP/DIP normally means that a lender will carry out a credit score, which leaves a "footprint" on your credit history. Too many "footprints" can actually downgrade your credit rating as it may look as though you have been turned down by another lender, so it is vital to proceed with caution. Therefore if you use the services of a mortgage IFA then you will have the peace of mind of knowing that the process is conducted properly.

Documentation

Once the mortgage application process moves beyond the initial AIP stage you will be required to provide the lender with a number of documents. You will need to provide proof of your identity and address (e.g. passport or driving license and household bill), proof of income in the form of the last three months' payslips and the last P60 or for the self employed the last three years certified accounts. In addition, a previous or current mortgage statement (if applicable) and bank statements, usually covering the last three months, are required. With bank statements the lender is not only looking at day-to-day conduct but also at the affordability of the mortgage and comparing it with your regular outgoings.

This assessment has tightened considerably in last couple of years. Some applicants have found that although they have received a successful AIP, once the application moves on and they provide bank statements or payslips the mortgage is declined. The self employed have been very much affected by this and accounts are scrutinised much more than in the previous ten years.

Timeframe

Once the lender has received your application and relevant documents, the survey is instructed. Assuming there are no problems along the way with either the documents or the structure of the property then the lender should approve a mortgage within 3 weeks. The mortgage offer as it is known is sent to you and your solicitor.

The solicitor will advise you of the legal process but on average in the UK the purchase of a home will take from 8 to 12 weeks. The first mortgage payment is usually due in the same month as the house purchase. This does vary from lender to lender, but it is advisable to ensure that funds to meet the first payment are in the bank by the time the purchase goes through.

Using an IFA

It is beneficial to employ the services of an Independent Financial Adviser who specialises in advising on mortgages. An IFA will advise and guide you through the options available and assist you in establishing which type of mortgage is best for you. In addition, an IFA has access to the whole mortgage market and can find you a suitable and competitive mortgage. Often applicants ask for the cheapest rate, however that does not always mean it is suitable for that particular applicant. Headline rate chasing is not the be all and end all of the mortgage process. There is very little point in applying for the cheapest mortgage if the lender is unlikely to lend to you.



The role of the IFA is wide-ranging. It is to provide you with mortgage advice, to research the whole market place and shop around on your behalf, to work with your solicitor to ensure that the money is there when your purchase goes through, to make the mortgage application with you, and to present you to the lender ensuring the information provided accurately reflects your situation and more importantly fighting your corner!

In the post credit crunch mortgage world we hear clients complain that they have been declined a mortgage for what feels like quite tenuous reasons when they have applied directly to a Bank or Building Society. On closer inspection they should not have been declined but lack of mortgage knowledge and details of what the lender required had resulted in a negative outcome. This can often cause many weeks of delay, possibly losing the purchase altogether and a whole lot of stress. Remember your adviser works for you and therefore will work very hard to ensure a successful outcome.

Mortgage information can be obtained directly from a lender but they are not obliged to provide you with advice—only information on their own product range. In addition, some estate agency offices have in-house mortgage advisers. But remember, if you are negotiating on the purchase of a house, do you want the estate agent to know your top price?

As the title Independent suggests the IFA is Independent and is employed by you, but you will often have to pay a fee for the service. It does vary from IFA to IFA but a fee of around £250 - £500 is likely.

Mortgage Related Products

You will need to consider a number of other products at the same time as arranging your mortgage. Life assurance, payment protection insurance in the event of sickness or redundancy and buildings and contents insurance are the most common.

Some lenders insist you buy their own buildings and contents insurance in order to take advantage of their best products. If you are not obliged to buy the lender's buildings and contents policy, some lenders will charge a modest "administration fee" should you arrange your own cover. Many insurers currently agree to pay this fee as an incentive.

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The Almary Green Mortgage Service

Our mortgage division will advise on any type of mortgage you may need, whether it's a first mortgage, if you're moving home, purchasing a property abroad or just looking to change your mortgage arrangements.

Our mortgage advice team do all the work—they will:

- Research the market for you
- Advise on the best options available
- Organise the necessary paperwork
- Liaise with the mortgage provider
- Work with your solicitor to ensure that the money is there when your purchase goes through.

What we can bring is peace of mind—you can be confident that you will have the right product at the right rate, available at the right time.

For advice and support in selecting and arranging the right mortgage for you, contact us by calling 01603 706740 or email one of our mortgage experts below.

Almary Green's Mortgage Experts



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Get the specialist advice you need from our Mortgage experts

Almary Green Independent Financial Advisers

Based in Norwich's newest premier professional district, Meridian Business Park, Almary Green Investments Ltd provides independent financial advice and support to businesses and individuals throughout East Anglia and beyond. Their advisers have a collective depth of experience extending over many years and they are specialists in advising both individuals and businesses on how to prepare for a prosperous future.



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