monetary solutions
INDEPENDENT FINANCIAL ADVICE

A Guide to Mortgages

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There are many options; fixed rates, discount rates, cash back options, variable rates, capped rates, tracker mortgages - the list goes on!

And then you need to choose your repayment option; repayment, interest only, ISA, Endowment, Pension or 'mix & match'!

With all these options available the good news is that you can find the correct mortgage for you. However this improved choice can seem bewildering and you may miss out on the best option for you through confusion, lack of time or simply having too many choices.

In today's market it has never been more important to get clear, concise and simple independent advice to help you make the right choice.

This guide is designed to help explain some of the options available to you and to let you know how Honister can make sure that one of the most important choices of your life is the correct one for you.

The Mortgage Process

What is a mortgage?
A mortgage is made up of two parts:

The Capital - This is the amount of money that is borrowed from the lender to purchase the property.

The Interest - This is the interest that the lender charges on the capital until it is repaid at the end of the mortgage term.

Types of Mortgage

1) Repayment mortgage
Each month your payment to the lender repays some capital and some of the interest. As long as you maintain your payments you can be certain that your mortgage will be repaid at the end of the term.

Advantages
- As long as the monthly payments are maintained the mortgage will be repaid at the end of the term - no need to worry about investment returns.
- Ideal if you wish to limit the risk linked to your mortgage
- Simple to understand with payments to one provider

Disadvantages
- No possibility of additional investment returns

- If you move house frequently it is difficult to build up equity in the property in the early years, as early payments are mainly interest
- Limited possibility of repaying the loan early without increasing monthly payments

2) Interest only mortgage

Each month the payment to the lender repays the interest on the loan. In this way the amount that is owed to the lender remains the same throughout the mortgage term. At the end of the mortgage term the lender will require the original amount of the loan to be repaid. A separate savings vehicle is used to build up enough money to repay the loan.

Commonly used savings vehicles are:

- Endowments (With profits)
- PEPs (Pre April 1999)
- ISAs (Post April 1999)
- Pensions

Advantages

- Offers the potential for additional investment return at the end of the term or the ability to repay the loan early, subject to investment return
- The savings vehicle is usually portable when you move house
- Choice of a wide range of investments that can be tailored to meet individual needs
- Easy to move the mortgage without disrupting the repayment plan

Disadvantages

- The ability to repay the loan is dependent upon the investment performance of the savings vehicle and there may be a shortfall if the investment does not perform as well as expected.
- You are responsible for the repayment of the loan at the end of the term
- Two separate payments to track. One to the lender and another to the investment company

3) 'Mix & Match'

Many people moving house may already have an endowment plan from their previous loan. Their circumstances may have changed, however, so an additional endowment would not be appropriate for them.

In these circumstances, it is usually possible to arrange for a lender to set up part of a loan on an interest only basis, and part on a repayment basis, thus ensuring that the benefits already accrued under the endowment are not lost. Not only that, but the life assurance already provided under the endowment is not lost.

This method is becoming increasingly popular for people moving on to their next house.

4) Endowment Mortgages (With Profit)

This type of investment combines a savings vehicle with the life protection needed to repay the loan on death during the term.

Bonuses are usually, but not guaranteed to be added to the plan on a yearly basis and once paid these cannot be taken away.

In this way the endowment aims to provide steady growth over the mortgage term and provide a lump sum, which should allow you to repay the loan although this cannot be guaranteed and is dependant on investment performance.

Advantages
- Guarantees to repay the loan in the event of death during the term
- Portable and can be moved from mortgage to mortgage
- Once bonuses are added they cannot be taken away
- Potential for additional returns
- Potential to repay the mortgage early
- Can combine savings plan with life and critical illness protection if required

Disadvantages
- If surrendered early the return may be less than the premiums paid
- No flexibility in premium payments
- Term should be for at least 15 years
- No guarantee that the mortgage will be repaid. The return is based wholly on the investment performance of the chosen provider
- Must have life cover built in whether required or not
- A Market Value Reduction (MVR) could apply to your endowment (if with profits) in adverse market conditions

A Market Value Reduction is a reduction applied to unitised with-profits funds where the value of the underlying assets is low. The Market Value Reduction, if any, is applied only when the plan is fully or partially surrendered (for example, on early retirement or transfer to another plan) or units switched into another fund.

5) ISA Mortgage
An ISA (Individual Saving Account) is a very flexible way of saving to repay your mortgage. They do not have a set investment term and contributions may be varied (usually subject to maximum and minimum limits). You can pay on a regular monthly basis as well as making lump sum payments into the plan as long as you remain within the maximum annual limit.

They offer a wide range of investment choices and also have several tax advantages.

Additional protection such as Life or Critical Illness cover is usually purchased separately.

Advantages
- Tax efficient savings
- No specific term
- Potential to repay the loan early
- Potential for additional investment return
- Flexible premium payments
- Portable - can be moved with your mortgage

Disadvantages
- Separate protection plan(s) required as ISAs do not include life cover
- Return is reliant on investment performance
- No guarantee of return
- Can only be taken in single name

6) Pension Mortgage
This aims to take advantage of the tax free cash that is available from a personal pension plan. As this involves pension planning as well as mortgage planning it can be a very complicated area to consider.

As with all the other options highlighted, there are advantages and disadvantages, however due to the complex nature of Pension Mortgages they should be dealt with on an individual basis and independent advice should be sought.

Interest Rate Options

Standard Variable Rate (SVR)
This is the interest rate each lender sets as their standard. It usually varies as the Bank of England changes the interest rate in response to changing economic conditions. The different lenders have control over the rate that they set, so rates are generally driven by market forces.

While better rates are often available, the SVR usually has no penalties and may be suitable if your immediate future is uncertain and you do not wish to commit to a product that may have a tie-in period.

Your monthly payments may vary, so you should be comfortable that you can cope with changes in your monthly commitments.

Tracker Rates
These are similar to standard variable rates. The lender will set an interest rate that tracks the Bank of England Base Rate. For example, it may be set at the base rate + 2.00%. The lender has no control over when the rate changes. It will change when the Bank of England moves the base rate.

These offer the benefit of independence from the lenders discretion with regard to rate changes. The rate is subject to Bank of England changes only. These rarely have a tie-in and are the same as SVR mortgages in most other aspects.

Discount Rate
This rate is usually set at a discount against either a tracker rate or standard variable rate.

Should the tracker or SVR change, the discount rate also changes but always remains at a lower rate by the discounted amount.

These often offer the lowest monthly payments. There is often a tie-in period during which there may be redemption penalties should you redeem the mortgage.

If the general trend is for interest rates to fall or remain stable then a discount rate offers good value.

Be aware, should interest rates rise then your monthly payments will also increase.

Fixed Rate
The lender sets a fixed interest rate for a specific term. The rate will not change whatever happens to the surrounding economic climate within the arranged term.

If you need to know how much you will pay each month, then this option offers the stability that you need. They often carry redemption penalties should you repay the loan early and if interest rates fall you may be paying a higher rate than is available to other borrowers.

You should be prepared for an increase in payments at the end of the fixed period.

Capped Rate
The lender sets a maximum interest rate (cap) above which the interest rate cannot rise. Should interest rates fall below this rate you get the benefit of the lower rate.

These offer the benefits of the fixed rate with the additional benefit of allowing you to gain from any fall in interest rates.

The capped rate is usually slightly higher than any fixed rate and on some occasions there may be a tie-in period.

What is 'Cashback'?
This is usually a SVR mortgage where the lender offers a cash lump sum to you at or after completion of the mortgage set up.

The cashback can be very useful to help cover the initial costs of setting up the mortgage. Beyond this it carries all the same benefits of a SVR. However you may also incur penalties should you repay the loan during a given time period.

The Costs

Lenders Fees
- Arrangement Fees - The lender may charge a fee for arranging the mortgage
- Booking Fee - You may have to pay a fee to book (reserve) a deal

Both these fees are usually payable on application and are not refundable should the mortgage fall through.

Higher Lending Charge
This is an additional charge that lenders may make if the amount of your mortgage is high compared to the value of the property that you are buying (typically above 75%).

This is a one off insurance payment that insures the lender against any loss that they may make should you default on the loan and they cannot recover sufficient funds by selling your house. You may be able to add this to the loan if the lenders criteria allows this.

You should be aware that this is a payment that you must make to protect the lender and that this insurance premium offers you no protection against default on your mortgage.

Legal Costs
These will vary from solicitor to solicitor. The solicitor works to co–ordinate the mortgage lender, the seller of the property and yourselves. We would suggest that you get quotations for the cost of their services at an early stage.

Stamp Duty
- Don't forget to include Stamp Duty in your calculations – a Government tax on property purchases above a specified amount. The amount of tax is based on a percentage of the total purchase price and increases in price bands, as shown in the table below.

- If the transaction involves the purchase of a new lease with a substantial rent there may be an additional Stamp Duty Land Tax charge to that shown below, based on the rent.

Residential land or property Stamp Duty Land Tax (SDLT) rates and thresholds

Purchase price/lease premium or transfer	Stamp Duty Land Tax Rate
Up to £125,000	Zero
Over £125,000 to £250,000*	1%
Over £250,000 to £1m	3%
Over £1m**	5%

* In the Budget March 2010 temporary relief from SDLT is introduced for first time buyers of residential property of a value up to £250,000. The new relief will be available for residential purchases with a completion date occurring on or after 25 March 2010 and before 25 March 2012.

** A new higher SDLT rate of 5% was introduced with effect from 6 April 2011 and will apply to residential purchases where the price exceeds £1 million.

If the value is above the payment threshold, Stamp Duty Land Tax is charged at the appropriate rate on the whole of the amount paid. For example, a house bought by a second time purchaser for £130,000 is charged at 1%, so £1,300 must be paid in Stamp Duty Land Tax. A house bought for £350,000 is charged at 3%, so Stamp Duty Land Tax of £10,500 is payable. Further information can be found at:
http://www.hmrc.gov.uk/so/rates/index.htm

Valuations
The lender will require a valuation of the property that you wish to mortgage to ensure that it offers adequate security for the loan. There are three main types of survey.

- **Basic Valuation -** This is carried out on behalf of the lender to ascertain the value of the property and its suitability as security for the loan.
- **Home-buyers Report -** This report offers additional information about the condition of the property. It highlights areas that may need additional attention, such as damp or structural problems.
- **Structural Survey -** This is a far more detailed report with a more in depth analysis of all aspects of the property.
- **Specialist Reports -** These are supplementary reports that may focus on specific areas such as damp or timber surveys.

The cost of a survey will vary from lender to lender and may be between £150 - £1,000 depending on the type of survey and the value of the property.

How we can help
Honister is a national firm of Independent Financial Advisers. Our independence means that we are not tied to any one company. We can talk to most mortgage providers and insurance and investment companies on your behalf to make sure that you get the very best solution to your mortgage and financial planning needs.

Most Building Societies, for example, are only able to offer you their own products; typically 25 or so deals. As an independent, we can offer you many more; typically in the range of 3,000 to 4,000 different products from different lenders.

Rather than representing a single provider we represent you in the market place. This means that we focus on finding out what you need and offering the solution.

How it works
We will carry out a thorough review of your current financial situation, taking into account your current policies, your income, expenditure, employment etc.

Most importantly, we will discuss with you at length what you require from your finances. We will discuss the advantages and disadvantages of the various options available to you and make sure that we know exactly what you are looking for.

Following the first meeting we will carry out extensive research, checking with the lenders and possibly talking to providers to provide a tailor-made solution to your needs.

Because we can offer anything that is available in the market place we are confident that the solution will not only meet your needs but will also be the most competitive deal available.

As a national company we also have access to providers that you won't find on the high street and who can often offer deals that are only available through Independent Brokers.

As we are Independent Financial Advisers we will make sure that you are not paying too much for any insurance plans that you may have with your mortgage.

Again we will speak to the providers on your behalf. We will then come back and talk to you in plain English about the solutions to your needs. We'll make sure that you are happy with the options available and that you understand the choices that you have.

Then it is up to you!

If you are happy with the solution that we have found for you, we will process your applications and make sure that your mortgage is arranged as smoothly as possible**.**

For further information or to book an initial consultation, please call us on 020 8760 9940.

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