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Mortgage Fact Sheet

CLAIRVILLE YORK FINANCIAL ADVISERS

Introduction

Arranging a mortgage is one of the biggest financial decisions we ever make. There are thousands of different schemes with hundreds of options which means that advice is essential when:

- Buying a new home.
- Remortgaging to a better interest rate.
- Raising money for home improvements.
- Buying to let.
- Buying a second or holiday home, in the UK or abroad.
- Funding another project.

Choosing the right type of mortgage is every bit as important as finding the right property and there are a number of different options available to borrowers. This Fact Sheet together with our Mortgage Advice Process Document is designed help you to understand the options available in greater detail.

Back to Basics

A mortgage is a loan you take out to assist you in the purchase of a property and a 'remortgage' is where you change the existing loan but don't move home. When you borrow money from your mortgage lender, you commit to paying back the capital (the amount they lend you) and the interest (the charges for borrowing the money) over an agreed term, typically 25 years.

Mortgages are available from most banks, building societies and specialist mortgage lending companies. Their loan is 'secured' on the property, which means the lender can take possession of the property if you fail to keep up the mortgage repayments. The monthly cost of the loan will depend on a combination of factors including the amount borrowed, the length of term of the loan, the interest rate deal and the type of repayment method chosen.

Types of Mortgage

In terms of how your loan is repaid there are basically two types of mortgage.

- **Capital & Interest Repayment mortgage**
  Every month, your payments to the lender go towards reducing the amount you owe as well as paying the interest they charge. So each month you are paying off a small part of your mortgage. In the early years the bulk of each monthly payment consists of interest, so there will be very little reduction in the outstanding amount of loan. In the later years the amount of capital repaid by each payment increases, so the amount of outstanding loan reduces more quickly towards the end of the term. Provided you keep up to date with your payments each month you will be assured that the loan will be repaid.

- **Interest Only mortgage**
  As the name suggests, your monthly payment only pays the interest charges on your loan. The whole amount of the loan remains outstanding until the end of the term when it needs to be repaid to the lender. This is why it is very important you consider at outset how you will repay the capital. This could be by using an investment or savings plan, the sale of the property (if appropriate and/or practical) or from inherited wealth. The benefit of an interest only mortgage is that the monthly payments are lower, as no capital repayment is included in the cost, but this should only be considered as a short term solution.

  If you are relying on savings and investments to repay the capital balance, you will need to check on a regular basis that they are growing sufficiently so that at the end of the term you will have enough money to pay off the loan; otherwise you may have a shortfall and will need to think about alternative ways of making this up. If you are unable to repay the loan at the end of the term you could lose your home.

  Most people who buy investment properties (buy to let) select an interest only mortgage. Interest payments can be offset against rental income for tax purposes and it is easier to account to HM Revenue & Customs for the interest payments using this method compared to a repayment mortgage.

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Mortgage Interest Rate Types

Whether you choose a repayment or an interest only mortgage, you will be paying interest on the money that you borrow. Lenders offer many different interest rate schemes.

- **Standard Variable Rate (SVR)**
  Your payments may increase or decrease according to decisions made by the lender. This may or may not be in line with changes to the Bank of England base rate. If rates rise rapidly, you could struggle to keep up with your mortgage repayments. Usually you can leave your lender or pay back extra amounts at any time without penalty.

- **Tracker Rate**
  This is a variable rate at a set differential above or below the Bank of England or some other bank base rate. It tracks (increases or decreases in line with) that rate and at the end of the initial Tracker Rate term your payments normally revert to the lender's Standard Variable Rate. As with a Standard Variable Rate, your Tracker Rate mortgage payments could increase rapidly leaving you struggling to keep up your mortgage repayments.

- **Discounted Rate***
  This gives you a gentler start to your mortgage at a time when money may well be tight. The lender gives you the opportunity to pay less than their Standard Variable Rate for an agreed period, typically 2, 3 or 5 years. But you must be confident you can afford the payments when the discount ends, as after this period the mortgage will usually revert to the lender's Standard Variable Rate. If you want to repay your mortgage during the discount period, you will normally have to pay an early repayment charge (or redemption penalty). Some of these schemes also require you to stay with your lender on their standard terms for a fixed period after the discount finishes.

- **Fixed Rate***
  The interest rate you pay will be fixed for a given period, usually between 1 and 5 years, although some lenders offer a lifetime fixed rate. Your monthly payments will stay the same in that fixed period, even if variable interest rates change. This gives you the security of knowing that you can afford your payments should rates rise, making it easier for you to budget. However, if rates go down you won't benefit and your payments will stay at the higher fixed rate. At the end of the fixed rate period the mortgage will normally revert to the lender's Standard Variable Rate which may be higher. There are generally early redemption penalties applied during the fixed rate period (and sometimes beyond), which can be quite punitive.

- **Capped Rate***
  Your payments are variable and often linked to a base rate, but they will not go above a set level (the 'cap') during the period of the deal. At the end of the capped rate period your mortgage will usually revert to the lender's Standard Variable Rate. There are often early redemption penalties during the rate control period (and sometimes beyond). These schemes do provide certainty of knowing that your payments can not rise above the capped level and you still benefit from rate reductions.

- **Collared Rate**
  These may be available in conjunction with a capped rate or a tracker (or both). Your payments are variable but will not fall below a set level (the 'collar'). Usually, there are no early redemption penalties unless it is used in conjunction with a capped rate or a tracker rate (or both). These schemes tend not to be very popular; if the scheme's rate is set at just above the 'collar' rate and you think rates will fall, you may not get the full benefit of a reduced payment.

- **Offset mortgage**
  Your mortgage account is coupled to your savings and the capital debt is offset against any deposits you hold with the mortgage provider. In most cases your main current account, savings account or both are linked in this way. Each month the amount in these accounts is offset against your outstanding mortgage before calculating the interest you owe, which can save significant amounts of money over the course of the mortgage term. You are unlikely to earn interest on the savings which are offset against your mortgage, but the tax advantages to certain groups of people (especially higher rate tax payers) can often be far more beneficial. These schemes can also be attractive to the self employed who accumulate savings over the year towards their annual tax payment. However, they are often charged at higher rates.

- **Flexible mortgage**
  These can be helpful if you have a variable income (such as the self employed) as you can vary the amount you pay each month and, in some circumstances, take payment holidays. The schemes often provide the facility for you to reduce your mortgage with lump sum payments without incurring an early repayment charge. Overpayments can be borrowed back in the future.

- **Cash-back mortgage**
  These can be useful if you need a cash lump sum. The lender pays you a lump sum shortly after you take up the loan. However, if you repay your loan in the early years you may have to pay some or all of this back. Typically interest rates are higher for this type of mortgage and they are less flexible.

* You should ensure that you will be able to afford any increased monthly payments in the future if the lender's Standard Variable Rate is higher at the end of the rate controlled period.

Administration

Once a suitable scheme has been selected and the application form submitted to the lender, there will be a number of processes which have to be undertaken before your mortgage will be granted and the property purchased:

- You will need a representative to carry out the legal work (or conveyancing) on the property, including local searches and drawing up contracts. You could use a solicitor or a licensed conveyancer.

- The lender will carry out a number of checks before making a mortgage offer. These include:

  - Reference checks. The lender may obtain written references from your employer and bank (or accountant if you are self-employed) and your current lender or landlord (if applicable).
  - Credit scoring. They will also run credit checks to assess your debt history and determine your credit worthiness.
  - Property valuation. The lender will usually have the property valued to make sure it is worth the price you have agreed to pay. If it is not, it could affect how much they will lend you. It is advisable, particularly for older properties, to obtain a more detailed report, such as a 'homebuyer' or full structural survey.

- **Mortgage Offer**
  When the lender is satisfied with the valuation and references, etc, they will make a formal mortgage offer - usually sent to you with a copy to your solicitor. Once you (or your solicitor on your behalf) have signed and returned the offer documents, your lender is committed to providing the money. The mortgage offer usually requires you to take out buildings insurance in case something happens to the property before you've paid off the mortgage.

- **Exchange and Completion**
  If you are buying a property, your solicitor can often agree a date for exchanging contracts with the seller's solicitor once you have received a formal mortgage offer. At this time you usually pay a percentage of the purchase price as a non-refundable deposit, which is negotiated between solicitors, and commit to paying the balance on the agreed completion date (when the property becomes yours).

What Costs are Involved ?

You will need to take the following one-off costs into consideration:

- Mortgage Advice Fee. Our minimum charge is £500 and you will be advised of the actual fee applicable to you before we undertake any work on your behalf. Please see our ***Mortgage Advice Process*** document for details of the service we provide.
- Stamp Duty Land Tax. The amount depends on the purchase price and is now charged at different rates depending on the proportion of the purchase price that falls into each rate band. The rates for residential properties with effect from 4th December 2014 are:

Residential property - purchase price	Rates of Stamp Duty Land tax
up to £125,000	0%
£125,001 - £250,000	2%
£250,001 - £925,000	5%
£925,001 - £1.5 million	10%
Over £1.5 million	12%

Example: *Property purchase price £425,000*

First £125,000 = 0%, Next £125,000 = 2%, Next £175,000 5%.

SDLT = £11,250 or 2.37% of purchase price.

- Solicitors fee, including Land Registry and searches. Costs vary between firms.
- Your lender will provide you with a mortgage ***keyfacts*** document, which will outline all of the costs involved in your specific mortgage package. These could include:
    - Mortgage arrangement and/or booking fees. This varies, by scheme and lender. Often such fees can be added to the mortgage.
    - Higher Lending Charge. This depends on the amount of your deposit relative to the value of the property and varies between lenders.
    - Valuation & survey fees. These are based on the value of the property, but the cost will vary between lenders and the type of survey you chose.
    - Early Redemption Penalties, which also vary between lenders and schemes.
- Estate agent fees.
- Removal Costs.

Early Repayment Penalty (ERP)

ERP stands for Early Repayment (or Redemption) Penalty. It is a fee charged to borrowers who wish to pay off all or part of their mortgage loan before the agreed date and is designed to compensate the lender for its costs in arranging the early repayment.

Not all mortgages feature these charges, but if they are chargeable this will be disclosed in the Mortgage Key Facts document. ERPs are most commonly applied to mortgages with a reduced or fixed interest rate for an initial term.

Finally

In addition you must budget for monthly costs, such as:

- Mortgage payments.
- Insurance for buildings and contents.
- Mortgage protection cover, such as life assurance and income replacement. Please see our ***Financial Protection Factsheet*** for detailed information.
- Council tax and utilities costs, etc.

Your home may be repossessed if you do not keep up repayments on your mortgage

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