Case Study

Plan Money

Title: Parents Assisting Children with Property Purchase

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We all remember that first exciting step onto the property ladder; our first home. I bought mine in 1990 when the affordability issues were not the purchase price because prices were closer aligned to earnings than today. Neither was it the deposit because even 100% mortgages were commonplace. The affordability issue back then was mortgage repayments, with interest rates at an eye-watering 14.5%.

Today's first time buyers face different affordability issues. Interest rates are at a persistent all-time low but according to the Halifax; in 2012 the average first time buyer property was £140,000 and required a deposit of 20%. With such high outlay it is no wonder that the average first time buyer is now age 30.

Many parents are investigating ways to help their children buy a first home. In doing, so there are considerable issues to be aware of and variables to understand. Options include; gifting from savings or investments, re-mortgaging, being a guarantor, shared mortgages, Equity Release and downsizing.

When helping out in this way, all parties need to understand a very obvious point; is it a true gift or a loan? It is not uncommon for a loan to be made to children with only loose assumptions about how and when it will be repaid. Unless analysis of future capital and retirement income requirement is undertaken, the impact of sporadic repayment could impact significantly upon future lifestyle. It may be assumed that the parents are not heavily reliant upon the capital they are loaning, however; lack of planning and awareness of potentially unfavourable events may prove otherwise. For example; investment return expectations not fulfilled, pension annuity incomes lower than expected or poor health.

If parents decide to be guarantor or are party to a child's mortgage, careful attention is required to understand the impact on any future re-mortgage plans for the parents.

Since the credit crunch, lending criteria has changed dramatically and people who may be retired or close to retirement may not find obtaining a mortgage easy, despite abundant equity and seemingly comfortable income. An often overlooked factor is that mortgages should be protected by life assurance and not necessarily just on the mortgagor, but the child to whom the parents have lent the capital. Furthermore, broader insurances should be considered if the child's ability to repay the capital is reliant upon their ability to work.

Taking it a step further, what if the child buys a property with a partner and that relationship breaks down? How might this impact upon the repayment of the loan to one set of parents?

Shared ownership schemes are an alternative to ‘the bank of Mum & Dad’. Buyers take a mortgage for a share of the property and pay rent to a Housing Association on the remaining share, buying more at a later date. With shared equity schemes a loan covers the deposit and a mortgage covers the rest with no interest due on the loan for five years. There are various criteria for both schemes and neither is without risks.

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