Regular saving mounts up to a decent deposit

Case Study

BUYING her first home in the summer was reward for years of putting money to one side; yet it came as a surprise to Vicki Green when she discovered she'd saved enough for a mortgage.

Vicki, of Edinburgh, had been saving in easy access and Isa accounts for several years – and with particular diligence over the past four years – without aiming specifically to build up a deposit for a home.

"It was only in the back of my mind to look at buying something, I have never been desperate to get on to the housing ladder. I always hoped to be able to do it, but only if I could comfortably afford it."

But when her financial security was boosted by a change in job circumstances, Vicki, who works in financial services, decided this year to ask her bank, Clydesdale, if she had managed to save enough to get a mortgage.

"I asked if they would offer me a loan; if they couldn't I would happily have walked away. I only wanted to buy in the middle of Edinburgh and wasn't desperate enough to live anywhere just to be able to buy, but they said they could offer a certain amount based on my deposit, so I knew it was possible."

After the mortgage restrictions of the past three years, in which affordable loans requiring deposits of 10 per cent or less have been scarce, Vicki had expected to need more savings before being able to buy a home without stretching herself.

Shortly after speaking to the bank and realising that she had enough for a deposit, Vicki started looking around for potential flats.

She finally bought one near the Leith area of the capital in August, with a 5.99 per cent mortgage from Clydesdale that required a 10 per cent deposit.

"I saw horror stories about deposits so I was surprised that it wasn't too difficult to get a mortgage with just 10 per cent to put down. I already banked with Clydesdale, which made it more straightforward, and the whole process was far easier than I had anticipated."

JEFF SALWAY

which last week was cut from 6.99 to 6.19 per cent, fixed over three years and with a £599 fee.

The average house price for those taking out the mortgage in the first half of this year was £97,650, according to Clydesdale, meaning buyers would need a deposit of just less than £5,000.

A buyer taking out a £100,000 loan with a 5 per cent deposit would face mortgage repayments of £655.97 a month. The bank also has a 90 per cent LTV mortgage at 5.99 per cent over three years, again with a £599 fee.

But while the low interest rate environment has helped many existing homeowners, it has become harder to save the deposits required, with cash accounts unable to keep pace with rising prices.

Carroll said: "Saving a deposit is a tall order at the moment for first-time buyers with these other pressures on their income. To save for a deposit, first-time buyers have to make sacrifices and put aside money that they could be spending on other things, sacrifices that many current home owners didn't have to make to the same extent in recent years."

A high proportion of first-time buyers are turning to relatives, housebuilder initiatives or government-backed shared equity schemes.

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Many of Scotland's housebuilders have in recent years sought to boost first-time buyers by offering shared equity schemes, part-exchange or direct financial assistance. Carronvale, Cruden, Bellway, Barratt, Kier and Taylor Wimpey all have shared equity deals on certain developments in Scotland, some in tandem with the Scottish Government's low-cost initiative for first-time buyers (Lift). However, these are only suitable for some buyers and have their drawbacks.

Carroll said: "Shared equity schemes can be attractive to property purchasers who are keen to enjoy a sense of home ownership and do allow first-timers to get a foot on the property ladder.

"They are generally restricted to modern-build properties however, with builders retaining ownership of the remainder of the property."

More recently there's been a shift towards longer-term policies. For example, Stewart Milne has developed a range of small one and two bedroom homes aimed at the first-time buyer market. The move is predicated on the reluctance of lenders to offer high LTV mortgages on flats for first-time buyers, particularly newbuilds.

John Slater, group managing director at Stewart Milne Homes, explained: "Houses, meanwhile, fall within a different lending criterion, which offers a higher LTV up to 90 per cent.

"Therefore, we have created a range of one and two bedroom house-styles within a first-time buyer price bracket, which ensures mortgages are obtainable and deposits are much more manageable."

Stewart Milne is also among several builders offering deferred payment plans, which help lower the deposit requirement while also reducing the LTV and, therefore, the cost of the mortgage.

Top Ten Tips

Making the most of property to top up your pension pot

A GROWING number of small business owners are buying their business premises through their pension fund, amid cash-flow worries and restricted bank lending. And it can make a lot of sense – rental income can build up tax-free within a pension and there's no liability for capital gains tax on sale.

But there are some things to think about first, however. Hazel Brown, a director of Carbon Financial Partners in Edinburgh, offers her top tips on buying property through your pension.

1 PERMISSABLE INVESTMENTS
There are fairly stringent rules on what is a permissible investment within a pension scheme.

Residential property is generally not permissible, but in some cases residential accommodation within a commercial property is allowed. Ensure the property you intend to buy is suitable. Falling foul of regulations could result in severe penalties.

2 DUTY OF CARE
The trustees of any pension scheme have a duty of care to members. Investments must be in accordance with the objectives of the trust which is, ultimately, to build a retirement fund.

The purchase price must be at least as much as the market value and the asset must provide potential for income and capital growth. Any benefit to the seller, even if a member, must be ignored.

3 CONTRIBUTIONS
The maximum contribution to a pension is 100 per cent of your annual earnings up to a maximum of £50,000 a year. You can utilise your entire pension fund to purchase a property and, if required, can borrow up to 50 per cent of the net assets in the plan. You can substitute "cash" contributions with the property itself.

As of April this year you can carry forward any unused allowance from the previous three years, giving a total maximum contribution of £200,000 in the current tax year, so you could get all the property into the pension and receive tax relief on the value.

4 TYPE OF SCHEME
Do you have the right pension scheme? Stakeholder and most personal pensions will not allow property as an investment, whereas a self-invested personal pension (SIPP) and small self-administered scheme (SSAS) will.

Consider all your future aspirations – both personal and business – before deciding which pension scheme to put in place: transferring to and from different pension schemes can be very costly.

5 COSTS
In addition to the purchase price, you will need surplus capital to cover associated costs. These include surveyor, solicitor, pension provider, financial adviser and bank fees (for arranging any necessary borrowings). Make sure you're aware of all costs before you decide whether the investment is worthwhile.

6 LOSS OF BUSINESS ASSET
Holding assets in a pension scheme keeps them safe from creditors. However, should you need security, or a higher valuation, for business projects and borrowing, you can't use the property as it belongs to the pension scheme trustees.

7 TAKING BENEFITS
Think about how to take your pension benefits at retirement.

Property is an illiquid asset and offers little flexibility in terms of income produced or capital. Not being able to lease the property could cause income to cease and a rushed sale could force acceptance of a lower value.

8 EXIT STRATEGY
If the purchase is a combined project – using collective SIPPs or through a multi-member SSAS – consider the difficulty of different retirement ages and needing access to benefits at various times. Think, too, about what would happen if you all fell out. An additional agreement can deal with such situations.

9 TAX ON DEATH
If you die before taking pension benefits, the property can be passed to your estate in lieu of a return of the pension fund. There is no tax liability at this point, but on distribution to beneficiaries (other than a spouse) the amount is assessable for inheritance tax.

A discretionary trust can help to mitigate this liability. If you have started taking pension benefits, a tax deduction of 55 per cent will be applied to your fund on death.

This is likely to be higher than passing on a property held outside a pension scheme. If your loved ones will be totally dependent on your pension fund for income on your death, holding more liquid assets is advisable.

10 ALTERNATIVES
Look at all the options. If your motivation is to release capital for business projects, bear in mind that certain pension schemes are able to make loans to the sponsoring employer.

Although the terms are fairly restrictive and security is required, interest rates are very competitive.