Let's Talk

Police Mutual

Bank of Mum & Dad

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Parents have always supported their children emotionally and financially whilst growing up. In more recent years, with many young people struggling to save enough money for a house deposit, many parents, grandparents, or family members are helping them get on the property ladder financially with their deposit. This is known as the 'Bank of Mum and Dad' or 'Bank of Family'. This help could be through a gift, a loan, or by becoming a guarantor for the mortgage.

Having help to submit a larger deposit can significantly improve the mortgage approval chances and potentially secure a more favourable interest rate.

The Bank of Mum and Dad is even considered one of the UK's biggest lenders.

It's essential that parents and their children know the rules of how the Bank of Mum and Dad will work. Not only for their own financial protection, but also for peace of mind. It therefore makes sense to talk through the agreement before any money has been provided, regardless of how uncomfortable it may be. There are several things you may want to consider:

Deciding whether the money will be a loan or a gift - handing money over without making the intentions clear has the potential to cause long-term harm to the parent/child relationship. It's important for both sides to understand the terms. Is this a loan to be repaid back over a specified term or a gift that does not have to be repaid, as it's an advance on the child's inheritance? Even if both sides understand the money needs to be repaid, if timescales are not laid down, there may be frustrations if the parents feel their child is taking too long to pay them back.

If the money is a gift, and the parents are not expecting to get the money back, then it's important to speak to a solicitor for advice. A formal "Deed of Gift" could be set up, as there may be implications for Inheritance Tax.

If the payment is a loan, the parents may want to consider putting their intentions and expectations in writing. This may seem extremely formal for a transaction between a parent and a child but there are reasons why this is a good idea:

- This document can stipulate how much needs to be paid over what time period as well as whether any interest is due to be paid or not. This means that both parties enter the arrangement with a full understanding of what is expected of them. Legal help may be considered to draft the paperwork.

Just to be aware if the money is a loan, then the mortgage lender must factor this into their affordability calculations and so may lend less as a result.

Fairness – if you have other children, you may want to ensure they are treated the same.

Long-term financial wellbeing - Lending or giving away a substantial lump sum towards a house deposit may seem like a good idea in the current situation, but people's circumstances can change quickly. There could be future life changes which mean the money is needed:

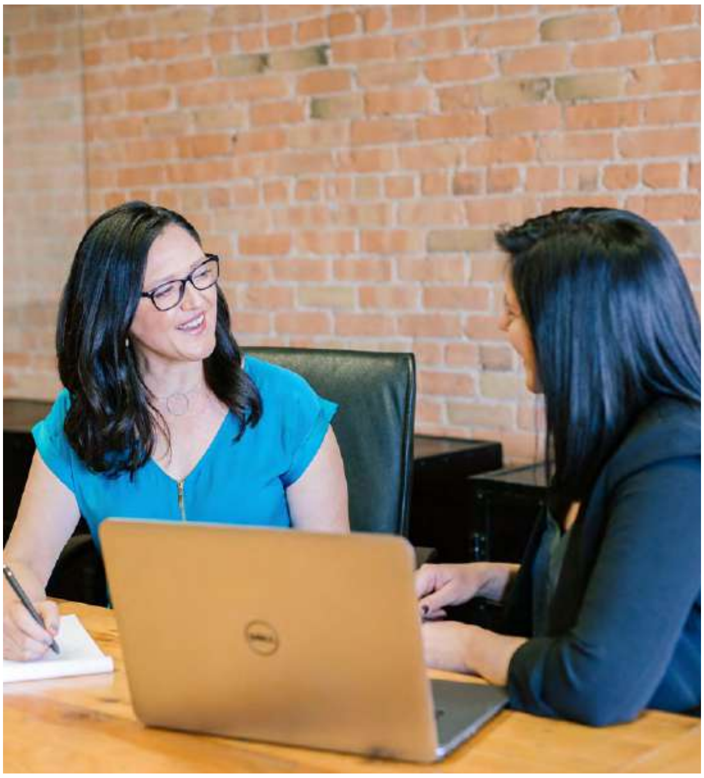
- **Relationship breakdowns** – this could be the breakdown of the parents or the child and partner. If the breakdown is of the parents, their decision to help their child would have probably been based on a joint financial future as a couple and things could look very different in the unhappy event of a marriage breakdown. It is also a worry that the child and partner may separate in the future. Something to consider, maybe the setting up a Declaration of Trust beneficial interest. This is a legally binding agreement that clarifies what each person pays towards deposits/fees/mortgage payments. Providing a legal record of who has paid what, which would be useful during a breakup of a relationship. Another reason for getting professional legal advice. They may also want to consider setting up a prenuptial agreement or cohabitation agreement.

- **Struggling to make the loan repayments** – while the children may be able to afford to make repayments in the beginning of the agreement, there could be many reasons why this could change. The birth of a child being one of them, with all the additional costs that this involves. Another reasons why the couple may struggle to make the repayments is due to losing their job or being on long-term sick from work. There are ways to protect against these types of situations, by having an income protection policy or redundancy policy in place.

- **Changes to the parents circumstances** - when parents make choices about how much they can afford to make available to their children it'll be in their current situation. Life events could change their circumstances, this could be due to ill health, having a major effect on their working life length and income. This ill health may also lead to substantial care bills later in life.

- **Negative equity** – while this isn't immediately an issue whilst the couple are still living in the home, consider what would happen if the home needs to be sold quickly.

It is therefore crucial before a parent decides to help their child or a child accepts financial help from their parent to consider all of these factors. Look out for your own needs and future desires and then consider the amount of help you can offer/accept. You may want to speak to a Financial Adviser and/or solicitor when making these decisions.



Tax

There are several potential tax issues that need to be considered before deciding to make a gift to support a house purchase.

Inheritance tax - if you gift money for a deposit to your child then there is no tax to be paid on it immediately. However, if the money is handed over as a gift, then there is the potential that an inheritance tax liability could be incurred if the giver were to die within seven years of making the gift and their estate is worth more than the inheritance tax threshold (currently £325,000).

There are several gifting allowances that can be utilised. In the current tax year (2024/25) £3,000 of income each year can be given away, this is known as your 'annual exemption'. In addition, gifts of up to £5,000 can be made to help with a child's wedding. Unlimited small gifts of less than £250 per person can also be given away without incurring inheritance tax. However, for gifts in excess of this amount then inheritance tax of up to 40% will be payable if you die within seven years of making the gift. For more details **click here**.

If a parent decides to become a joint purchaser of a property with their child, then it's important to consider the tax implications. The parents share of the value of the house will count towards the value of their estate for inheritance tax purposes on death.

You may want to consider producing formal paperwork with your child, as providing paperwork showing that the money was a gift and showing what date it was made can help in the event of later questions about inheritance tax.

Stamp duty on second homes - if a parent decides to buy a property with their child and are named on the deeds while already owning a property, they will be charged the higher rate of stamp duty which applies to purchases of second homes. Simply helping a child with a gift of a deposit will not incur this charge, nor will acting as a guarantor on the mortgage.

Income tax - if parents choose to lend money to their children and charge interest then income tax would need to be paid on the interest received. If this is the case, then a self-assessment tax return would need to be completed each year.

Capital gains tax - if the support of the parent is in exchange for 'taking a share' in the property and it is then sold at a profit then capital gains tax may be payable. Capital gains tax needs to be paid if a second home is sold at a profit that is more than the current threshold which is £3,000 current tax year (2024/25).

Other ways parents can help children get on the housing ladder

Not all parents may have access to a large lump sum of money, but they may be able to help their children with regular saving towards a deposit over a number of years.

Here are other ways you could help a child:

Open a Lifetime ISA - this product is aimed at helping people either purchase their first home or save for retirement. It's available for anyone between the ages of 18 and 40. The maximum that can be contributed is £4,000 per year and in return the government will top it up with a 25% bonus.

Equity release – for those with a lot of wealth tied up in their house then it may be possible to access a cash lump sum through an 'equity release' product. The amount of which will depend on the value of the property and the parents age.

Second charge mortgages/remortgaging – parents may be able to remortgage their property to release capital to lend to children. This can be done with a current lender or by moving to another one.

Acting as a guarantor - an increasing number of mortgage deals allow parents to act as guarantors on their child's mortgage or else have their savings used as security. There are two main types, guarantor mortgages, which enable a parent or family member to guarantee the mortgage repayments and family deposit mortgages, which allow a family member to deposit money into a savings account where it is held for a fixed period as security. During this time, if the borrower defaults the money will be taken from the savings account.

Disclaimer: This paper is intended to provide helpful information but does not constitute financial advice. Please speak to a financial and/or mortgage advisor before making any financial decisions.

This guide concentrates on helping children getting on the housing ladder but the Bank of Mum and Dad may be used in lots of other ways. Including, university costs, helping pay for weddings, costs of grandchildren, relationship breakdowns, as well as an emergency fund for many different reasons.

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