



ROSE

Financial Planning

FREQUENTLY ASKED QUESTIONS (FAQs)

The following guide has been produced to answer many of the standard questions that clients ask of us FS on a day to day basis with regard to raising a mortgage secured on a property in Spain.

1) Are 'Interest Only' mortgages available?

Yes, and the term for the 'Interest Only' (IO) period ranges from 1 year to 5 years. Before the Credit Crunch products with terms to 30 years were available and perhaps these return. However, the schemes offering longer term IO (10 to 30 years) are far more restrictive than those for shorter terms (1 to 5 years) as the Spanish lending market has yet to fully adjust to the British way of thinking in this respect.

After the initial IO period the mortgage automatically switches to a Repayment or Capital and Interest type for the remainder of the mortgage term. For example, if a mortgage is arranged over say, 30 years with an IO period of 5 years, from Year 6 the mortgage will switch to a Repayment over the remainder of 25 years. The rate of interest will still be the same i.e. monthly reviewable to annually fixed, but you will be asked to start repaying the capital as well as the interest.

At this stage, we have numerous choices open to us and it is a good idea for you to review matters with us;

- i) Allow the mortgage to transfer to a Repayment type and start to repay the capital. However, this is not always good IHT planning (see Question 2) below).
- ii) Ask the bank to extend the IO period. There is no guarantee that they will allow this but market conditions then may make them find in your favour.
- iii) Consider a remortgage and switch to another lender. The downside to this, of course, will be the costs attached in doing so. It is therefore important to consider your long term requirements when planning the detail of your mortgage.

2) Why would I want an 'Interest Only' mortgage as opposed to a Repayment (Capital and Interest) mortgage?

The mental approach to this is different than the normal rationale applied to borrowing in the UK. Your NEED to think 'Spanish' and NOT British! The benefits are often very different;

- i) In Spain there is a 'sleeping giant' of an issue which most home owners are simply unaware of: Inheritance Tax (IHT). Go to Question 12) for a guide to this VERY IMPORTANT issue.

It is so important that any property acquisition in Spain cannot adequately be considered unless this subject is understood.

- ii) Interest rates for mortgages in Spain are comparable to or lower than in the UK and, in most cases, the capital and income employed to either meet interest payments or repayments emanates from a £ income or capital base.

That being so, there is a benefit to retain as much capital as possible in £ and invest it for a higher return. For example, even a cautious investment into a deposit account can generate an interest rate return of 7% as at the date of writing. With an average Euro mortgage rate of say, 4% the net return is at least 3% per annum. Over a standard term of 25 years, that will gross up to 75% of capital employed. If the mortgage is for €100,000 by way of example, that equates to a massive extra income of €75,000.

iii) Interest paid is normally allowable against income received for the purpose of calculating Income Tax for tax residents in Spain. Therefore, the longer an IO period is run, the greater the interest paid and hence, the tax saving. Remember, that there is also an added income via the reduction of capital employed as mentioned above.

iv) There is a potential exchange rate risk in holding an asset (your Spanish property) in a foreign currency (Euros) against the natural income and capital base (normally £ for the majority of our clients).

Therefore, by keeping the liability (your Euro mortgage) as high as possible for as long as possible, there is an offset which can mitigate against negative exchange rate movements.

3) What is the normal interest rate payable for a Spanish Euro mortgage?

Rates are normally set against the European Central Bank index (Euribor) ranging from monthly to annual review or the Spanish Cajas rate with a margin and re-fixed annually. This helps cash flow projections. It is often common to see a discount offered for the first year, but be sure to always check the margin over the index after the initial period. You could end up paying more you see (the proverbial 'sprat to catch a mackerel').

Hence, the current first year rate will range from circa 2.5% for low IO terms and Repayment mortgages. For longer IO periods a premium may be charged by the lenders, so that the average rate will be circa 3%.

Fixed rates are available from 1 to 5 years currently (again, pre Credit Crunch, up to 30 years and these products will return in time).

4) What documents do I need to show?

ID.	Passport and either a Residencia Card (for Residents) or an NIE (ID number for Non Residents). Rose FS will assist in arranging any NIE needed.
Proof of Income	Pay slips x 6 months P 60 Pension Letters Rental income contracts Investment income schedules Tax Assessment (Self Employed) Accountant's Statement of Affairs (Self Employed)
Bank Statements	x 6 months (for all bank accounts, UK and Spain)
Existing mortgages	x 6 months statements
Remortgages	Existing Escritura Original Compraventa (Purchase contract) Recent valuations Quotations for any works being financed or property being purchased Latest existing mortgage or loan statements being consolidated
Purchases	Compraventa (Purchase contract) Property details Solicitor contact details Estate Agent details
Insurances	Existing Buildings & Contents policy Life Assurance policies

That all sounds a lot but, in most cases, many of the documents will not apply.

Also, we FS need only COPY documents and not the originals. However, the original passport, NIE or Residencia will be needed at the Notary for legal completion of the process.

The application process can be actioned from a distance via post, fax and e mail. You do not physically need to meet a mortgage adviser and we will complete the process of determining your needs by phone.

5) What are the costs of arranging a mortgage?

Arranging a mortgage in Spain is slightly more expensive than in the UK and broadly you should allow 6% of the mortgage amount needed as follows;

1%	Lender fee (minimum)	
1%	Broker fee (minimum €1,000)	
1%	Notary/Registration	
2%	AJD Mortgage tax	
0.15%	Valuation fee	Up Front
€500	Booking fee	Up Front

As you can see the only monies needed by ourselves to apply for the mortgage are the Valuation and Booking fees. All other costs are due at completion and will be deducted from the mortgages advance over the new current account with the lender.

6) What is the cost of repaying the mortgage early?

Redemption penalties, as they are formally called, are relatively inexpensive in Spain. The norm is for 0.5% for partial or full repayment. Some lenders offer 0% redemption fees.

7) Do I need to use a specialist Spanish and English speaking solicitor?

For Remortgages, where you are switching lenders, or simply releasing capital/equity from your home or debt consolidating, no! The process is relatively simple and does not warrant the extra cost of using a solicitor.

However, for a Purchase, using such a professional is **STRONGLY** recommended. We FS will happily recommend a firm.

8) Do I need to be in attendance at legal completion of the mortgage and/or purchase?

The short answer is no, although this is always recommended.

The legal completion is known as 'Notarisation' as the relevant deeds or 'escrituras' will be executed by a Notary. He or she will be a government appointed officer with the authority to witness and sign legally binding agreements.

If you cannot or do not want to be in attendance at the Notary it will be necessary for a 'Power of Attorney' agreement to be given to a trusted third party. We FS will happily act on your behalf although, for Purchases, we would request that your solicitor act for you. Also, for Purchases, a 'General Power of Attorney' is recommended as this gives much broader powers (for example, to open and run a bank account) rather than a standard limited power.

9) Do I need a Spanish bank account for a mortgage?

Yes. All banks insist on opening a Current Account to sit alongside the mortgage in order to receive monies in and pay the mortgage.

As part of the process heading towards Notarisation, you will need to execute the account opening forms. The sooner this is done, of course, the better.

10) Are there any mandatory or suggested insurances for a mortgage?

Yes. The only mandatory protection or insurance policy required by all banks (and this is the same in the UK) is Buildings Insurance. All banks will want to see this in place and will even insist upon arranging it themselves.

In addition, it is **STRONGLY** recommended that all mortgages are protected by a) Life Assurance and b) Income Protection to ensure that the mortgage and underlying asset, your home, is adequately protected.

You will not want to buy a property and only lose it from an accident, illness or disability beyond your control!

All our clients will be interviewed by an Independent Financial Advisor in this respect.

11) What if my income is low or I cannot prove my income?

This is not an uncommon problem but there are normally ways around the issue and requirements of the lender.

Lenders look at 2 risks when determining whether a mortgage application is acceptable to them;

- i) You and your ability to meet monthly mortgage payments.

This translates into a) the credit worthiness of the applicant (the lender will run checks) and b) provable, regular income.

- ii) The Property.

This translates to a) the percentage they lend you against the valuation that they will carry out and b) the property state, type, etc.

For the Self Employed proof can sometimes be difficult because a good Accountant, in preparing the books of accounts, will try to keep net profits and hence, tax as low as possible. However, the combination of the latest books, Tax Assessment and a Letter of Comfort or Statement of Affairs from the Accountant, with sight of recent banks statements, will normally do the job.

If your income is low still, or because of a low wage, pension, rental or investment income, we can look to use a third party (normally a working child, sibling or parent) to add the weight of their own income acting either as a co-applicant on the mortgage or as a 'Guarantor'. Again, they do not need to come to Spain to execute any legal documents; this can be achieved via a Power of Attorney from a distance. Rose FS will arrange this.

It is important to mention two things here;

- i) The co-applicant(s) is at risk, as are you, if you do not keep up the repayments of the mortgage. That needs careful explaining to them.

However, often, the addition of a Guarantor actually diminishes such a risk as mortgage payments can be normally extended over a longer period, especially where the main applicants are elderly.

- ii) The Guarantor does NOT need to be added to the property deed. In other words, the ownership of your property need not be undermined by you using a third party to financially support your application.

HOWEVER, rather than using a 3rd Party as a Guarantor, we may be able to elect for a 'Self Certification' of income mortgage albeit that these are not presently readily available due to the effect of the 'Credit Crunch' and more cautious lending.

12) Am I too old for a mortgage and what is the maximum term to repay?

Many elderly clients think they are too old to apply for a mortgage, despite the fact that maximum age for repayment is 80. This is not so! See 11) above.

By either a) using a third party to either come onto the application or to act as a Guarantor (as above) or b) electing for a 'Self Certification' of income scheme, the emphasis of the lending assessment of risk is either taken away from the more elderly applicants to rely on the added third party (normally a child) as per a) or even just to the property itself b).

This is often good Inheritance Tax planning as any debt outstanding on a death reduces the tax payable.

Alternatively, we have access to specialist 'Equity Release' and 'Lifetime Mortgages' which do not require a monthly payment from you.

So, if you are in the position of 'wanting' or 'needing' access to some of the capital locked into your home, with or without a monthly payment, we have products and solutions to suit!

13) Do I need to be worried about Spanish Inheritance Tax?

Worried, no! Concerned, yes! Understanding the issue and how to overcome it is more than half of the battle!

The vast majority of people that buy in Spain, especially the British, make an assumption that the IHT regime in Spain is the same as in the UK. This is simply not so. It is massively different and to understand a) the issues and it's potential impact on you and your family and b) how it is so easy to address, is a danger to say the least!

The primary differences between Spanish and UK IHT regimes are threefold;

- i) There is no spouse exemption on the family home
- ii) The IHT allowances lie with the beneficiary(ies) and not the deceased
- iii) The standard personal allowance in Spain is just €15,958 versus £312,000 in the UK. A huge difference!

The effect of IHT means that, as most people buying in Spain are non-resident for tax, the risk of having to pay IHT is high.

However, IHT is levied on the 'net worth' of the recipient and the benefit being received, so by keeping the mortgage at a high a level as possible, the taxable exposure is reduced. A Repayment mortgage decreases over time which has the directly opposite effect of increasing IHT exposure.

Even if the preference is for a Repayment it is wise to consider IO as an alternative for the IHT mitigation as above, and indeed to consider as long a term as possible, perhaps by bringing would-be beneficiaries onto the mortgage so that they, in turn, can benefit when the property passes to them on death of the current owners.

There are various routes to resolving the problem or IHT mitigation that can and should be considered;

- i) Maximise the Interest Only mortgage (as above)
- ii) Effect Life Assurance (normally Whole of Life). This is normally written in Trust in favour of the end beneficiaries not to not avoid tax but rather to make sure that funds are available to meet the tax bill.
- iii) Add beneficiaries to the property deed. Because tax is calculated according to the distribution of the deceased's share of the property (or other assets) and the classification of the end beneficiaries, it can make sense to add the beneficiaries early so that each person has a smaller share and, hence the IHT tax exposure reduced.

The issues arising by doing this though are several;

- i) By changing the owners of a property there may be a Capital Gains Tax payable. So timing is important.
- ii) You may not be comfortable in gifting part of your home away, even to your children! Having said that, the concern could be overcome, at least to a degree, by taking a 'General Power of Attorney from them so that control lies with you. But these powers can be cancelled at any time so you need to be comfortable with whom the arrangement is made. Or you can use a 'Usufructo' agreement which gives you life tenancy in the property.

Finally, it is critical that you effect a Will here in Spain. This is because there is a default mechanism that will decide the fate of your estate if you die without one. That could mean that people may benefit in a way that you had not intended! We will recommend a solicitor to assist.