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Equity Release Schemes

Lower investment returns, poor pensions and increasing life expectancy are resulting in many individuals reaching retirement with far less capital and income than they may want or need for their lifetime. For those individuals, an Equity Release Scheme may be the answer.

What is an Equity Release Scheme?

The phrase Equity Release (ER) in this guide refers to a Home Reversion or a Lifetime Mortgage. Equity Release Schemes (ERS) will share common features such as:

- A lower age limit – generally you must be at least 55 years old before you can apply
- You will have the right to remain in your home for life
- You will receive a cash lump sum or an income for life, or a combination of these, from the ER company
- No repayments need to be made to the ER company until your home is sold (in the event of your death or moving into long-term care)
- The amount owed to the ER company will never exceed the value of your home (which is commonly called the 'No Negative Equity Guarantee')

Are there any alternatives to Equity Release Schemes?

- Move to a cheaper property: if you sell your property for £200,000 and buy a replacement property for £150,000, then you have released capital of £50,000 (less the costs involved with moving) whilst still owning your home
- Use existing savings: rather than using up part of your home, spend capital savings (where available)
- Approach family members: if you want to release cash from your property, might it be possible for, say, your children to pay you the funds that you need, and in so doing acquire an interest in your home? In any event, it is sensible to discuss ER with family members before proceeding with it
- Apply for all state benefits to which you may be entitled (such as Attendance Allowance, Pension Credit, Council Tax Benefit etc). If you already receive such benefits then be aware that taking out an ERS may affect your entitlement
- Contact Age UK and your local council for information on Grants which may provide funds to improve your home
- Take out an ordinary personal loan or interest-free mortgage: these usually involve variable rates of interest so be certain that you would be able to afford the monthly payments if interest rates increased

Where do I begin looking for an Equity Release Scheme?

Contact an Independent Financial Adviser (IFA) who has experience of ERS. We can recommend an appropriately qualified and experienced IFA to you on request.

What is the difference between a Home Reversion and a Lifetime Mortgage?

Home Reversion: You sell a percentage of your home to the ER company. The company will not pay you the full market value for that share on the basis that you will be allowed to remain in the property rent free for the rest of your lifetime.

In the event of your death or moving into long-term care, the property is sold and the company receives its specified percentage, with your estate receiving the remainder.

Advantage: you know exactly what the ER company will receive in the future in percentage terms, although the actual amount in pounds and pence will depend on property prices when your home is sold.

Disadvantage: if you were to die or move into care shortly after having entered into the scheme, then you would have sold a share of your home for a fraction of its true value. The ER company will also arrange the sale of your home.

Lifetime mortgage: this is a mortgage and so the ER Company will lend you money which is noted on your deeds.

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No monthly payments are made. Instead the interest is rolled-up each month, together with the amount of the initial loan. In the event of your death or moving into long-term care, your home will be sold and the mortgage debt, plus accrued interest, is repaid. The monies left over, if any, will be paid to you or your estate.

A fixed rate of interest is usual, although some capped rates are available (which are variable but cannot exceed a stated rate).

Advantage: you have absolute certainty (assuming a fixed rate of interest) what you will owe the ER company at any given time in the future. In the event of your death shortly after taking out the scheme, you are unlikely to have lost out quite as much as you would have with a Home Reversion.

Disadvantage: compound interest means you will be paying interest upon interest for years to come. To explain, in the first year of the Lifetime Mortgage you will only be paying interest on the amount you borrowed; in the second year, you will be paying interest on the amount you borrowed and on interest charged in year one, and so on.

Some ER companies try to reduce this disadvantage by offering a drawdown facility, whereby you borrow an initial sum of money but have the ability to draw further money when required. A new fixed rate of interest is agreed each time a further sum is withdrawn.

What happens if the mortgage debt exceeds the value of my home?

A Lifetime Mortgage should provide a No Negative Equity Guarantee so that the ER company does not have the right to sell your home in the event that the mortgage exceeds the value of the property. This protects you in the event of a sharp decline in property prices.

Will I be able to move house?

Yes, in most cases. If you want to move to a cheaper property, then the ER company will insist on a partial repayment (possibly including an early repayment charge) from the monies released in the event of a sale.

If you have a Lifetime Mortgage, the effect of compound interest and possibly falling house prices may mean you are restricted in where you can afford to buy. In any move, the ER company will want to approve the choice of the new property, and you will have to pay for all survey fees, legal fees and moving costs etc.

What costs are involved in taking out an Equity Release Scheme?

You will normally need to pay a non-refundable survey/valuation fee up front, plus administration fee. If you take advice from an IFA, then a fee will be due to them. This additional cost can benefit you greatly in the long-term if it means the most suitable scheme is selected for you. There will be legal fees payable which will differ between firms of solicitors. Ask for details up front, and always ensure the solicitor concerned has experience in ERS.

Some ER companies charge a completion fee, which is an additional fee added to the debt you owe them once completion has taken place. Whilst a completion fee will not necessarily alter the amount of the cheque you receive, it will alter the amount you owe the company over the years.

How long will all of this take to finalise?

A fair estimate is approximately four months from when you first look into which scheme to select. Clearly, you should not spend the money in advance of the completion date.

To help move matters along, you should instruct your solicitor in good time and provide proof of your identity and address, proof of household insurance and your title deeds, or if you have an existing mortgage then a contact address and mortgage account number for the mortgage company.

Is it all doom and gloom?

Absolutely not – ER has its place and can be very beneficial to many people. The information set out above, should not be taken as a warning against applying for such a scheme. Rather, it is intended to give a little detail on the subject to allow an informed choice to be made.

Key contacts

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