

THORNLEYS SOLICITORS

EQUITY RELEASE



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BENEFITS OF EQUITY RELEASE

An increasing number of people are considering the benefits of Equity Release as a way of improving their lifestyle in retirement, without the cost and upheaval of having to move house. Given that the home is, for most people, their biggest asset, it is not surprising that equity release is an increasingly popular choice for older homeowners. Also, many people have less money in retirement than they had planned for.

Equity Release enables people to live a more comfortable lifestyle in retirement and allows them to **'unlock'** the **equity** (the difference between any mortgage they may have and the value of their home) tied up in their home without having to move house. They can use the money for any purpose, such as to supplement their income, make a large purchase, carry out home improvements, have a holiday or even make gifts to their family. Equity Release is used mostly by older homeowners who either have paid off their mortgage altogether or have only a small amount left to pay.

ARE YOU 'RICH' IN CAPITAL BUT 'POOR' IN INCOME?

As the value of shares and investments have dropped by 30% over the past three years as has the 'real' value of their pensions, house prices have soared by 70%. Many people are finding themselves **'rich' in capital but 'poor' in income**. Furthermore, attitudes towards inheritance are changing, for many families it is no longer needed or expected.

People are now looking for ways to offset their fall in investment and reduced income with the rise in the value of their home, consequently the equity-release market is growing rapidly.

As the market grows it is expected that more people will look to Equity Release not only as a way of utilising their main asset, **their home** more effectively, but also as a useful way of spending their money in their lifetime and possibly reducing Inheritance Tax that may be payable by their estate after their death.

Rapidly rising house prices can have significant financial implications for some people. Successive Government policies have seen the real value of the Inheritance Tax threshold (IHT) eroded and many homeowners face the pressure of managing any potential IHT liability for their estate.

THE DECISION SHOULD NOT BE TAKEN LIGHTLY!

The decision to take out an Equity Release plan should not be taken lightly, and it is important that if you are considering taking out such a scheme you discuss it with your family and take advice from legal and financial advisers. **Even though equity release suits many people it may not suit you!**

Any income or capital received from an equity release scheme may result in a reduction or loss of benefits in any Pension Credit or Council Tax Benefit that you receive.

WHO CAN APPLY FOR EQUITY RELEASE?

Equity release schemes are generally only available to people who have paid off their mortgage (or have only a very small mortgage) and own their house outright. The minimum age tends to be 60 but some providers will lend to people who are 55 or over whereas some providers insist you are at least 65. Some companies may only accept applications from people living in freehold houses rather than in flats or maisonettes and others may only accept applications from people whose properties have been constructed with certain materials.

Whatever type of Equity Release scheme you use, you will remain responsible for repairing and insuring the building. If you sell a share of your home to a reversion company it will expect you to maintain your home to a reasonable standard in order to protect their investment. You will also remain responsible for paying for building insurance and will still have to pay Council Tax.

There are two main types of equity release plans available on the market today both of which offer clients significant benefits and issues:

LIFETIME MORTGAGES HOME REVERSION SCHEMES

A **LIFETIME MORTGAGE (also known as a 'roll-up' plan)** enables older homeowners to raise a **cash lump sum, regular income or a mixture of both**, by taking out a loan against a portion of your home to release a lump sum or regular income and the loan is secured on your home. Interest is charged on the debt but there are no monthly repayments. Interest 'rolls up' and the loan and interest is repaid on death or earlier if you move into a care home and your property is sold. There is usually a choice of fixed or capped variable rates of interest. By choosing a regular income rather than a lump sum you accrue less interest as interest is charged only on the amount you actually receive. If the plan is jointly between a husband and wife, the loan and interest is repayable on the death of the survivor.

Different providers offer different terms and any available loan would depend on its value and your age. Some providers limit the borrowing, the younger you are the less equity you can to release, as younger people are likely to accrue interest over a longer period, which increases the risk that they will owe more than the house is worth. Most provider's, offer a guarantee that protects you from negative equity which ensures that neither you nor your estate has to make up any shortfall between the selling price of your home and the amount of the outstanding loan.

It is vital that you thoroughly check the terms and conditions before signing up to a lifetime mortgage and you ensure that they suit your needs. You need to check whether you can move to another smaller house in the future, or even sell up completely and move into rented sheltered housing/residential care in which case early repayment penalties will be charged.

Any lump sum that you receive will be tax free, but any income you receive will be subject to income tax. Also, if you release equity from your property but give the funds away to a family member, it might affect your future eligibility for assistance with care home fees.

Other ch

anges in your circumstances may affect the plan, for example if someone comes to live with you after the plan is taken out such as a younger family member/friend moves in to provide companionship or care. In this case, the plan would still come to an end on your death. This would mean that the house would probably have to be sold.

The main **advantage** of a **lifetime mortgage** is that because you still own your home, you benefit in any increase in value. The **disadvantage** is that what you will eventually owe on the loan is unknown, as this depends how long it is before the house is sold. Most, if not all, of the value of your home could be eaten up by debt.

As their name suggests lifetime mortgages are designed to last a lifetime, so if you sell your property and repay the loan early you are likely to face substantial early repayment penalties.

Lifetime mortgages are by far the most popular form of equity release. Three-quarters of all equity release plans currently sold are Lifetime Mortgages.

HOME REVERSION SCHEMES offer homeowners the ability to sell a certain percentage of their home to a reversion company for **a fixed amount, which can be taken as cash, a regular income (fixed or increasing) or a mixture of both.**

You can remain living in the property until you die or move into a care home. You do not receive the full market value of your property (usually you receive 40%-60% of your home's current valuation) rate because the reversion company allows you to live in your home for your lifetime and it cannot recoup its money until the property is sold, which may not be for many years.

The older you are when you take out the plan, the more the company will pay as your life expectancy will be shorter and the company's investment is not tied up as long as with a younger person.

Under a Home Reversion scheme there are no monthly repayments and no interest accumulates. You would be granted a lifetime lease which enables you to continue living in your home for the rest of your life, the lease would end if you moved into long-term care.

It is possible that **under certain Home Reversion Schemes** you may receive a higher purchase price for your property in return for which you pay **an ongoing rent** while

you live in your home. **You need to ensure that you could afford any rent payment that is asked of you.**

Some reversion companies offering lump sums aim to find a buyer for your home. If a buyer has to be found, this can delay the process. Find out from the company how quickly they can purchase your home (or part of it).

Although Home Reversion Schemes are not as popular as lifetime mortgages many people prefer this method of releasing equity from their home particularly if they want to pass on some inheritance. You can sell between 30%-90% of the rights of your home, and are guaranteed that a percentage of its value is left for your estate when the property is sold. The Reversion Company then receives the percentage value of your home which you transferred to it.

The **advantage** with a Home Reversion Scheme is that you know from the outset what proportion of your home's value you retain and what is available to pass as an inheritance to your estate after your death.

The main **disadvantage** is that your estate will not benefit fully if house prices continue to rise and it receives much less than the market value of the part of the home that you sold.

REGULATION

In the past Equity Release Schemes received bad press from the media. Today however, the schemes are now much safer for the consumer. In 1991 Safe Home Income Plans (SHIP) established a Code of Conduct for all its members to use when advising clients on Equity Release. Also in October 2004 certain types of Equity Release plans (**the lifetime mortgage type**) became regulated by the Financial Services Authority (FSA) and there is also a Mortgage Protection Code that all mortgage lenders must follow.

Under FSA Regulation, if you take out a Lifetime Mortgages you will have a process for recourse should things go wrong, as providers must subscribe to a complaints procedure and you will be able to seek compensation through the Financial Ombudsman.

Regulations under mortgage schemes ensure that you client cannot lose your home whatever happens to its value; that your solicitor oversees the transaction and ensures that you understand the plan that you are signing up to; what costs are involved; how your tax position and entitlement to State benefits may be effected; and your options in the future.

At present, Home Reversion Schemes do not fall under regulation because they are not a 'mortgage' type product. Failure to regulate Home Reversion Schemes denies you access to the Financial Ombudsmen Service if things go wrong.

The FSA also warn that equity-release schemes are riskier than standard mortgages as they can restrict the freedom to move house and it can be difficult to switch companies if you are unhappy with their terms.

It is **vital** that if you are considering taking out Equity Release you first **seek independent legal and financial advice** so that you are fully aware and understand your financial obligations beforehand. The legal process is a fundamental part of the application and the majority of providers **require you** to have legal representation.

Whilst a lifetime mortgage may be just right for some people, others may be better served by a home reversion scheme and for some people an equity-release scheme may not be suitable at all!

You may have other investments or assets which could boost your income or give you the lump sum you need or may even feel that still the best way to release the equity in your home is to buy a smaller one and use the profit you make on your home to enjoy your retirement. You may even be eligible to claim Welfare Benefits such as Pension Credit or Council Tax Benefit.

Finally, if you need help with repairs or adaptations to your home you might want to find out if you can get help from your Council. You could consider applying for a Home Improvement Grant and there are various agencies around who would be able to advise you, such as Care and Repair or the Home Improvement Trust (Tel: 0115 934 9511).

You should look at all your options before you embark upon Equity Release and ensure the decision you make is the right one for you!





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Our Private Client team at Thornleys have the specialist knowledge and expertise in these matters. They can advise and help you with your specific needs and requirements.

FOR FURTHER INFORMATION:

On Elder Client issues please see our **Factsheet 11 - Community Care Issues**; on Wills generally please see our **Factsheet 1** on Lasting Powers please see our - **Factsheet 8** and on Inheritance Tax please see our **Factsheet 3**

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