WOLFE & CO.
— SOLICITORS —
EST. 1894

Market Street
Skibbereen
Co. Cork, P81 W603

Tel: +353 (0)28 21177
Fax: +353 (0)28 21676
E-Mail: info@wolfe.ie
Web: www.wolfe.ie

EQUITY RELEASE SCHEMES

Equity Release Schemes are arrangements that allow property owners to borrow money based on the value of their homes and defer payments for a defined period, or until after a defined event, usually the death of the borrower or the sale of the property. In this context "Equity" refers to the value of your property less any mortgages you may owe. Generally speaking, these schemes are aimed at older people who are also home owners and this article has been prepared with such people in mind.

Whether an equity release scheme is appropriate for any individual will depend on a number of factors which should be considered carefully before signing up to any such scheme. The schemes can be very attractive at first glance as they appear to offer money up front with little downside during the lifetime of an elderly person who may be considering such a scheme. However financial advisors often warn that the schemes offer poor "value for money", depending on the details of the facilities on offer.

On the other hand, the schemes are sometimes very welcome ways for older property owners to enjoy a better standard of life based on the value of their property where they are not concerned about what they may be leaving in their estate following their death. An arrangement that may be very suitable for one person's circumstances may be totally inappropriate for another and it is highly advisable that you consult with a financial advisor and your solicitor before you take any steps to avail of an equity release scheme.

Equity Release Schemes were very popular back during the "boom years" as spiralling property prices meant that they were very profitable arrangements for the companies offering such schemes and could be very convenient for older property owners who wished to retain their properties but raise money from them. Their popularity waned substantially during the recession and, at the time of writing, they are not very common but may make a comeback as property prices begin to show signs of positive growth.

The Main Types of Equity Release Schemes:-

Life Time Mortgages or Life Loan – This is a Mortgage at an interest rate which is fixed for a specific period and on which interest is compounded during the term of the loan, rather than paid each month by the borrower. A Life Loan is designed so that, normally, it may not be reduced or redeemed until the death of the borrower.

Home Reversion Schemes or Equity Sale – Such schemes entail the transfer by a home owner of a share in their property to the company providing the finance. The amount paid by the finance company will be less than that value of the share transferred, and normally is paid to the person partly as a capital lump sum and partly as income or entirely as income.

Elderly home owners may require substantial funds for a variety of reasons for example to undertake work to their home, pay medical expenses or just to enjoy what money may allow them to do. Such elderly home owners who need substantial funds but cannot repay a loan due to lack of income, advanced age or poor health are those who may seek to avail of an Equity Release Scheme product. With the interests of all home owners but especially elderly home owners in mind this brochure will briefly outline the features of each of the two Equity Release Schemes.

Life Time Mortgages

A Life Time Mortgage allows you to borrow money against the value of your home. You make no repayments and you continue to own and live in your home. The loan is usually paid from the proceeds when your home is eventually sold following your death or when you move out. Life Time Mortgages will in general allow you to borrow between 10% and 45% of your home's value. The older you are, the higher the percentage you can borrow. If all of the loan is not required at once it will normally be cheaper in the long run to take the money in instalments as it is required. If approval has been granted for a large sum and it is taken all at once, you will be charged interest on the whole loan. If only an instalment is taken you pay interest on that instalment. Some providers of Life Time Mortgages also allow a mixture of both lump sum and instalment payments. The Mortgage will require to be discharged when you sell the property, you move out of your home permanently (for an example to reside in a nursing home) or following your death. Again, some Life Time Mortgage providers require that if you move out of your home for a period of say six months you will be required to pay off the Mortgage. Interest rates on Life Time Mortgages are usually 2% to 3% higher than the standard Mortgage rates because you are not making regular repayments. Interest is charged on the amount you borrow and is added to that amount. Each month after that you are charged interest on what you have borrowed plus the interest added from previous months. This is called "compound interest". Therefore, the amount of interest charged increases over time as the amount you owe grows. Your Mortgage can therefore mount up quickly and the longer it lasts the more it grows.

As already stated with the Life Time Mortgage Scheme you are charged interest on any money you borrow and the longer your Life Time Mortgage lasts the more money you will pay back. There are two types of Life Time Mortgages and it is important to be aware of the differences between them. Fixed Rate Life Time Mortgages – where interest is fixed at a set rate for a number of years or the life time of the Mortgage or Variable Rate Life Time Mortgages – where the rate of interest will fluctuate with interest rates generally.

To summarise, the advantages of this scheme are that you can raise cash through a Life Time Mortgage and continue to own and live in your home, you don't have to make repayments. As you continue to own your home and benefit from an increase in market values and you are able to avail of instalments as you may require monies

thereby reducing the interest that will be added to your Mortgage. The disadvantages appear to be that you will be charged a higher rate of interest than on a standard repayment Mortgage, as you make no repayments interest builds up quickly and the longer you live in your home the more your loan grows which may result in a substantial repayment to the scheme provider when your home is sold.

Home Reversion Schemes

With this variety of Equity Release Scheme you agree to sell a share of your home in return for a cash price. The price will be less than the market value of the share of your home that is being sold. It is important to be aware that you are not borrowing against the value of your home as with the prior explained scheme but are actually selling part of your home. For example, if you decide to sell a 40% share of your home to such a scheme provider on the ultimate sale of your property they would receive 40% of the proceeds either when you move out or when you die. The remaining 60% will go to you, or to your estate after your death. It is a condition of such schemes generally that you can live in your house for the rest of your life and there is no restriction on how you spend the money. It is also a general condition that if you already owe money on an existing Mortgage you will be required to pay this off before proceeding with the Home Reversion Scheme. The Home Reversion Scheme, as opposed to the Life Loan or Life Time Mortgage, requires you to take the money as a lump sum and it cannot be taken in instalments. The Home Reversion Scheme will end when you permanently move out of your home; move out for a certain period of time as specified in the agreement; you die or you sell your home which ever happens first.

The amount the Reversion Company will get when your home is sold also depends on the type of Contract you have with them. There are two such Contracts – Fixed Share Contracts which means that the percentage of your home the Reversion Company own is fixed from the start and cannot change, no matter how long you live or the value of your property at the time of the sale. Variable Share Contracts mean the longer you live the less of your property you own. With the Variable Share Contract you can get a bigger lump sum of money when you first sell your share of your home but the percentage of your home the Reversion Home owns automatically increases every year and you will not get any other payments.

Clearly therefore the advantages of the Home Reversion Scheme is the ability to raise cash by selling part of your home but continuing to live in it. You do not pay rent for the share of your property which you have sold to the provider of the Reversion Scheme. It is not a loan and there are no repayments and you are not charged interest. The disadvantages of such a scheme are that the money you will receive will be much less that the market value of the share in your property, you won't benefit from the full increase in the value of your home if property prices rise – you will only benefit from an increase in the value of the share you still own.

As previously indicated, Equity Release Schemes can be controversial due to their nature and the age profile of the people who typically avail of them. For example, it was reported in January 2008 that the Financial Regulator received a record 3,500 queries in one month for advice on Equity Release Schemes where Financial Institutions lent money to elderly home owners in return for a share of their house. The Financial Regulator has warned many times about the complexities of the

numerous Equity Release Schemes available for older people to release cash from the value of their home.

A further warning was issued by the then Consumer Director of the Financial Regulator's office, Mary O'Dea, who said that the benefit of Equity Release Schemes are that they provide cash to meet current needs but the risk is that consumers may not have enough left to cover long term health or care needs. That report urged all consumers as does the writer to look at all their options and to take independent advice before signing to any schemes of this nature.

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Market Street, Skibbereen, Co. Cork - web: www.wolfe.ie
Tel: 028-21177, fax: 028-21676, e-mail: info@wolfe.ie