

6 steps through the equity release maze

Introduction

If you are retired and fully own a valuable property but are short of ready cash, you may be wondering about equity release, a method of extracting a tax-free cash sum from the value of your house while you continue to live in it. The money released can be spent however you like – on home improvements, a new car, holidays, to eke out your pension or to help your children or grandchildren onto the property ladder. Sounds good? Well – read on and judge for yourself.

1. How does it work? You would normally have to be 60+, in good health and own a mortgage-free, freehold house to qualify. Your life expectancy will be assessed and your home independently valued beforehand. Equity release is aimed at the asset-rich, cash-poor pensioner reluctant to move from the family home, and there are two distinct types: lifetime mortgages and home reversion plans. But beware: any sum borrowed now will diminish the value of your estate on death.
2. How do lifetime mortgages operate? These are the most popular form of equity release and allow you to borrow a sum of money which is secured on your home and paid back – with interest - when the house is sold. Compound interest on the loan is rolled up and quickly accumulates. Say you have a house valued at £300,000 against which you borrow £80,000 at a fixed rate of 6%. In the first year you will owe £80,000 + £4,800 interest; by the 3rd year you will owe £89,800 + £5388 interest. After 20 years, your initial loan of £80,000 could incur a repayment of £256,000. You will also have to pay commission, plus solicitor's fees and may be required to carry out some home improvements up-front.
2. What about home reversion? Here, you sell part of your home for much less than its true value to a specialist company in exchange for a cash sum. If you have a home valued at

£200,000 and want to sell 50% to a reversion company, you will be lucky to get £40,000. You will also have to hand over the title deeds. You can later sell another portion if you like, and can normally release between 15 –55% of the present value of your property, depending on your age and health. On your death, the reversion company pays a proportion of the sale price – not the full amount of your retained proportion - to your estate.

3. How does this affect dependants and relatives? Your spouse or partner can continue to live in the house after your death, but only if their name is on the title deeds. Adult children or others residing with you would not normally be able to carry on living in the home. Before signing up, you would also need to be very sure that the amount of debt will never exceed the house's value. Also, your heirs must understand and accept that their inheritance will be greatly diminished by the equity release plan.
4. What about state benefits? Be very careful here as you will lose these after taking out equity release if the extra income received puts you above the benefits level. Your actual pension will be unaffected but any pension credit, housing or council tax benefit could well disappear. You will also still be responsible for council tax and all utility payments, plus making regular home improvements to maintain your home's value. Equity release providers make regular inspections to ensure you are keeping the property in good repair.
6. How is inheritance tax reduced? Any equity release plan instantly reduces the value of your home, both to you and your heirs. But to save IHT you have to be sure that the amount of interest you or your estate pays on the loan does not come to more than the IHT saved. If you keep the money in the bank it will still count towards IHT; likewise, if you give it to your children it will only become IHT-free after seven years. In 2007, IHT is levied at a

flat 40% on all estates over the threshold of £300,000. Below this, estates do not attract IHT.

Jargon buster

1. Lifetime mortgage. This is a mortgage which quite literally lasts for the rest of your life, and interest continues to roll up until the day you die.
2. Drawdown plans. A variation of the lifetime mortgage where you draw on funds as and when you need them rather than taking the entire amount at once.
3. Home Reversion Plans: here, you sell part of your home for much less than its true value to a specialist reversion company.
4. Home income plans: the generic name for commercial equity release, covering all the ways in which money can be released from your home.
5. Protected Equity schemes: these guarantee that the amount you owe will never exceed more than a certain proportion of the property's value.

Liz Hodgkinson is the author of *Safe As Houses? The Homeowner's Guide to Property, Inheritance and Taxation*. Published by Kogan Page, £11.99

Where to go for help

The Equity Release Information Centre

Tel: 0800 298 6288

<http://www.askeric.org.uk>

Independent Equity Release Advice

Tel: 08080 555 500

<http://agepartnership.co.uk>

The Help the Aged Equity Release Service

St Leonards House

Mill Street

Eynsham

Oxford X29 4JjX

Tel: 01865 733009

Email: equityrelease@helptheaged.org.uk

Web: www.helptheaged.org.uk/equityrelease

ends

