Freedom 55 Financial

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QUADRUS

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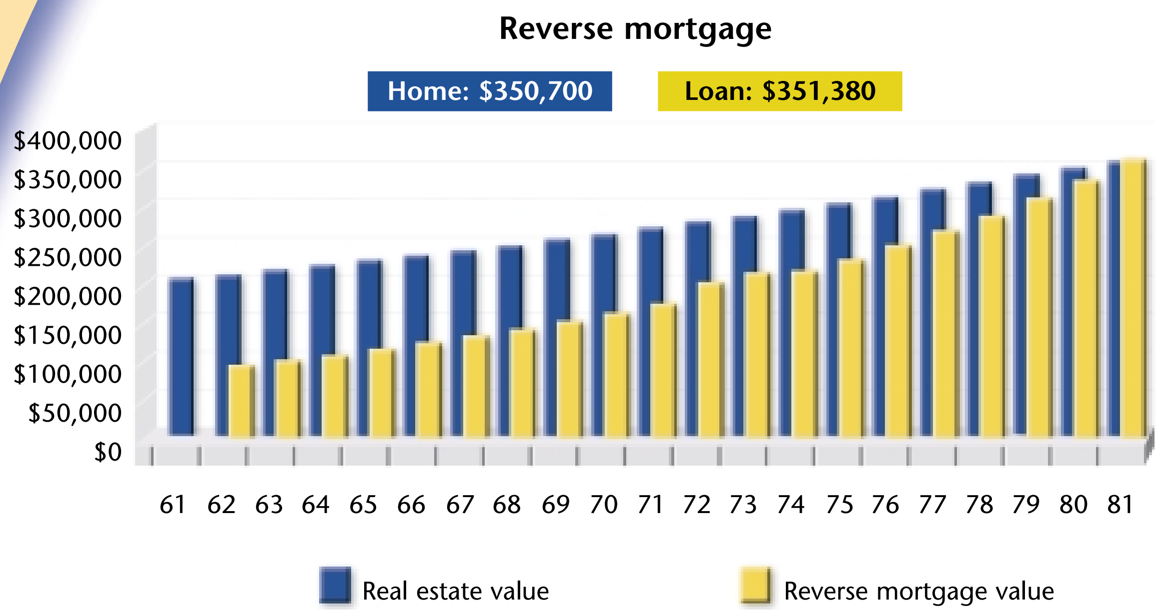
Reverse mortgages – the costs may outweigh the benefits

A reverse mortgage is an agreement allowing a homeowner to borrow against home equity and receive tax-free payments, without being required to repay until the home is sold.



- Value of the client's home at age 62 is $200,000
- $80,000 reverse mortgage is secured at an assumed annual compounded interest rate of 8.1 per cent
- Assumed three per cent annual growth on home

After 19 years, the original reverse mortgage loan, plus accrued interest, has grown to $351,381 leaving no residual home equity. At point of sale, the full value of the home will be owed to the lender.

What happens to your debt when you take out a reverse mortgage?
Just like interest on savings, compounded interest on debt grows exponentially. Without repayment of principal and interest, the interest is added to the amount owed (your reverse mortgage loan balance) and continues to compound until you sell or until your estate transfers to your heirs.

As shown in the illustration, the nature of compound interest and lack of repayment in a reverse mortgage can erode the equity in your home in a relatively short period of time – a problem if you're planning to leave your home to your heirs. In short, reverse mortgages can be a very expensive way to finance your retirement needs. Be sure to carefully consider potential drawbacks to retiring with a reverse mortgage.

See other side…

- Interest accumulated may potentially erode all equity in your home.
- Some reverse mortgages charge heavy exit penalties for opting-out early.
- Interest rates can be substantially higher than conventional mortgages – about 1.5 per cent higher in the case of a standard five-year mortgage.
- Additional costs for appraisals and legal fees may apply.
- If you choose a plan that requires repayment on a specific date (known as a "fixed-term" reverse mortgage), you must be confident in your ability to repay the loan on that date. If you are unable to do so, you may need to sell your home to meet the conditions of the loan.
- Home owners still remain responsible for property taxes and home repairs.

If you want to leave an inheritance to your heirs, you may want to consider alternatives to a reverse mortgage, such as downsizing to more affordable housing or establishing a homeowner line of credit, co-signed by your heirs. A homeowner line of credit would allow you to take out money as you need it. (*Solutions Banking* offers a competitive and flexible homeowner line of credit.)

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