A guide to reverse mortgages

A reverse mortgage is a loan against the value of your home. You can use the loan however you like while continuing to live in and retain ownership of your home.

There may come a time when you'd really like to be able to take an overseas holiday, buy new furniture or pay off debts. With a reverse mortgage, you can use the equity you've built up in your home to do that.

It's up to you whether you take the loan as a lump sum, regular income or a combination of both.

Who can have a reverse mortgage?

Most reverse mortgage providers will lend you money if you are over 60 and own (and live in) your home. You don't need a current income to qualify. You can generally borrow between 15% and 40% of the value of your home, depending on your age, the age of any other borrowers and where your home is situated.

Repaying the loan

Although some providers allow you to make repayments at any time without penalty, generally you don't make repayments on the loan. All fees and interest are simply added to the loan balance each month.

If you aren't making repayments, the loan balance increases over time. This is known as 'loan capitalisation' which means you're paying interest on interest. It also means there's a risk of owing more than the value of your home. Some providers guarantee you won't have to repay more than your home's value, but this is generally subject to you maintaining your home in good repair.

You (or your estate) must repay the loan if you sell the home or die.

Things you should consider

- There is no way to know for sure how much you'll owe at the end of the loan.
- You may have to maintain the property to a standard required by the lender. If you don't, there's a chance you may default on your loan.
- If you're the sole owner of your home and you move or die, anyone who lives with you may not be able to stay in the home.
- You might not have enough money left over after paying the loan for aged care accommodation, or to leave an inheritance – so you should talk to your family before taking out a reverse mortgage.
- It could impact on any Centrelink or Department of Veterans' Affairs payments you might receive.
- It can be more beneficial to receive regular payments rather than a lump sum from the reverse mortgage.
- A good rule is to only borrow what you need.

Case Study – Kim

Kim is 70 years old and decides to borrow a lump sum of $100,000 at an interest rate of 8.32% per year. Kim's home is worth $400,000. Here's what Kim could owe at the end of various periods.

Number of years since Kim took out the loan	Here's what Kim's home may be worth if housing values increase 3.5% every year	Here's what Kim or Kim's estate could owe if the interest rate is 8.32%*	And here's what Kim could owe if the interest rate increases to 11%** after the first 2 years
5 years	$475,000	$154,000	$167,000
10 years	$564,000	$234,000	$290,000
15 years	$670,000	$356,000	$502,000
20 years	$796,000	$540,000	$869,000 Exceeds value of home, 'negative equity'

All figures rounded to nearest $1000
* assumes 8.32% interest applies throughout
** assumes 11% interest starts after 2 years and then applies throughout

Source: www.fido.asic.gov.au

IMPORTANT INFORMATION

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