Article rank | 26 Apr 2012 | Toronto Star | BRYAN BORZYKOWSKI SPECIAL TO THE STAR

She uses reverse mortgage to renovate

No interest paid for now, but a big sum at the end

After 41 years living in the same Thunder Bay house, Sandra Petzel and her husband decided it was time to renovate.

BRENT LINTON/TORONTO STAR

Backing in: Sandra Petzel with grandchildren, Emily, 10, left, Oliva, 6, and Grace Jarvis, 10, in her Thunder Bay home of 41 years.

They had, however, just purchased a lakefront cottage, so money was tight.

To finance the work — they have to replace the wires, windows and the place needs a paint job — they decided to try a relatively unknown financial product, one recommended to Petzel by a friend. They took out a reverse mortgage. “It gave us some pause,” she says. “We spent a couple of weeks thinking about it, but I felt comfortable.”

Areverse mortgage is a loan, taken out by a homeowner and based on the value of the person’s abode. It doesn’t have to be paid back until the house is sold.

Interest accrues, but not a dime is owed — no interest or principal — until the homeowner moves.

Because no payments need to be made, only people 55 and older can tap into this product. Any younger and so much interest would accumulate that it would be impossible to pay back.

Arthur Krzycki, director of public relations for Toronto-based Homequity Bank, one of the only companies that offers a reverse mortgage in Canada, says, in most cases, people in their 50s and 60s are only allowed to take out 30 per cent of the equity in their home. Seniors in their 70s can take out half. The reason it’s not more, he says, is that they don’t want homeowners to owe too much interest and use up all the equity in the house. Homequity also doesn’t want to lose money — if the sale won’t cover the principal and interest, it will cover the difference. Reverse mortgages are different than a home equity line of credit. Firstly, the latter has rates more in line with traditional mortgage rates, around 4 per cent for a fiveyear term. Homequity's rates start at 4.5 per cent for a one-year term; you'll be charged 5.75 per cent interest for a five-year term. You can also get a bigger loan with a line of credit — about 80 per cent of the value of the house — but you have to pay interest every month. It's also hard to get a line of credit if you're not bringing in any income; as you don't owe anything until the house is sold, reverse-mortgage companies don't care as much about employment status. It's a useful tool for people who need some cash and can't get, or don't want, a line of credit. "Some people pay off debts; others use it for their own investment purposes," says Jim Murphy, president and CEO of the Canadian Association of Accredited Mortgage Professionals. Petzel was attracted to the mortgage because of the payment terms. She wants to redo her place to sell it. She took out $48,000 — she says her home is worth about $160,000 — and hopes that, with the upgrades, her house will sell for more than what it's now priced at.

The idea, she says, is that, while she borrowed 30 per cent of the value in her home, she'll end up owing less than that, even with interest, if the place appreciates.

The risk is that it won't sell for more. A disadvantage is that it eats into how much money you, or your kids, will get when the house is sold.

"If you've got kids in their 40s expecting to inherit the home, then they only get what's left," says Dennis Mitchell, chief investment officer with Toronto's Sentry Investments. "Instead of getting $400,000, they could get $20,000."

So far, reverse mortgages aren't well known, but Homequity does more of them every year. Mitchell says people, generally, aren't thrilled with the idea of not paying interest and having it accumulate.

They are also not offered by banks, although most of Canada's major financial institutions have referral agreements with Homequity.

Petzel's just started renovating her house. So far, she's satisfied with the way she's financing the work.

"We get to reinvest without having to be out any cash. It's not costing us anything right now to do this."