CALGARY HERALD
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Home value can provide retirement cash flow

Calgary Herald January 26, 2011

Greg Bandler of HomEquity Bank specializes in helping Canadian homeowners over age 60 start reverse mortagage.
Photograph by: Ian Willms, For Postmedia News

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For Postmedia News

Market downturns and the cost of raising families have left many Canadians strapped for cash in their retirement years. But some may be sitting on an asset that can add gold to their golden years.

Their homes have appreciated in value over the years, and can be used to add to people's cash flow. One way in which a principal residence can do this is through a reverse mortgage. Available to Canadian homeowners age 60 and older through HomEquity Bank, which administers the CHIP Home Income Plan, homeowners can borrow up to 40 per cent of the appraised value of the home in which they're living.

Interest rates in the CHIP program begin at 4.5 per cent, and no principal or interest payments are required for as long as the homeowner or spouse lives in the home. The full amount only becomes due when the homeowner and spouse both die, when the home is sold or if both move out. And they have the option to repay the principal and interest in full at any time.

"They can use the money for anything they want," says Greg Bandler, HomEquity Bank's Toronto-based senior vice-president. "They can use it for living expenses, they can invest it for income or they can use it to maximize their RRSPs."

And the money they receive from a reverse mortgage is tax-free, he adds. "It isn't added to their taxable income so it doesn't affect old age security or guaranteed income supplement benefits they may receive."

For certain people, reverse mortgages make sense, says Wilmot George, director of tax and estate planning at Mackenzie Financial Corp. in Toronto. "It's for those who can't work and have little cash flow, and want to remain in their homes and community."

But reverse mortgages come at a cost, he adds. "Their interest rates are higher than home-equity lines of credit, and their setup costs — appraisal fee, independent legal advice, and closing and administrative costs — add up to about $2,500."

The money homeowners take out of the home, plus the compound interest bill, means reverse mortgages may not be suitable for those who want to leave inheritances.

"Reverse mortgages don't require regular payments, which looks like an upside," George notes. "But this usually means holders forget about this cost, and when they sell the home or pass away, a large part of the equity in the house has been chewed away."

But Bandler says some of his clients take out reverse mortgages precisely because they want to help the younger generation — now, while they're alive.

"And often it's the adult children who approach us," he adds. "They may be living in another city and can't be physically there to help their parents, but they want them to have money to pay for services they need."

A home-equity line of credit, offered by most major banks, may be a cheaper alternative. Unlike reverse mortgages, they can also be obtained on a property being rented to someone else. The RBC Homeline Plan gives its clients the ability to unlock up to 80 per cent of the equity in homes they own with clear titles.

"If a homeowner has a cash-flow problem, he can free up $400,000 from a home worth $500,000, and put this money in an income-generating investment," says Debbie Ehrstien, a financial planner with RBC Wealth Management Ltd. in Calgary. “And, as with all loans taken for investment purposes, the interest is tax-deductible.”

The RBC Homeline Plan charges the prime rate plus 0.5 per cent, which as of late December, translated into 3.5 per cent.

The downside of such credit lines is they require regular interest payments. And banks look at income level, among other factors, in assessing applications. Income is not a factor in getting a reverse mortgage.

“And HELOCs (home-equity lines of credit) will eat away at inheritance assets as well,” George notes.

But there are still other options for Canadians whose assets are chiefly in their homes.

Downsizing to a smaller residence is one of them. There will be real estate fees and moving bills to pay, and leaving a longtime home and familiar community can be difficult for older people.

“But selling a $1-million home and buying another for $500,000 will allow a couple to invest some of the equity they’ve built up to generate cash flow,” Ehrstien says.

Selling a home and still living in it is yet another option. George suggests working with a real estate agent to find a purchaser who is interested in an investment property and is willing to rent it back to the original owner.

“This can be a win-win situation for both parties,” he says.

He also suggests renting out part of a home for additional income.

“This income will be taxable,” he says, “but any expenses incurred, such as renovating and maintaining the rental space, will be tax-deductible.”

And those who are determined to remain in a longtime home may be able to sell other assets that aren’t generating income, George adds, such as jewelry, art work or a vacation property.

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