



REVERSE MORTGAGES

Clients best interests, benefits and pitfalls

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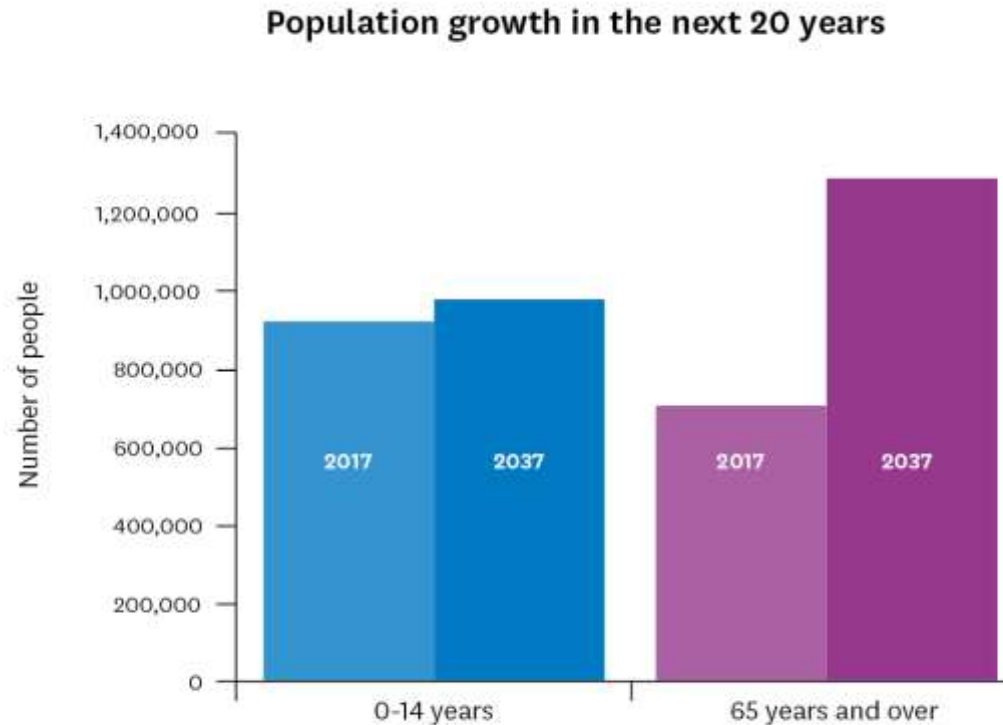


Learning Outcomes

- To understand how Reverse mortgages work
- Be able to identify clients that may benefit from a Reverse Mortgage
- Key benefits and risks with Reverse Mortgage
- Applying the five fingers of selling (of Financial Advice) to Reverse Mortgages
- Lawyers & accountants advice on RM - fee model
- How to diversify and grow your business by meeting the needs of this growing sector

NZ's Ageing Population

Source www.superseniors.msd.govt.nz



NZ's Ageing Population- where will they live?

- Retirement Villages
- With Family
- Renting
- Many will choose to remain in their own home

Reverse Mortgages – How do they work?

- Senior Homeowners (60yrs+), based on the youngest resident
- Borrow against the equity in their home
- Amount of funds available is determined by age of youngest borrower and value of home. (LVR's vary among locations and lenders)
- Funds can be made available via drawdowns to approved limit
- Interest on loan is capitalised and compounds
- Loan principal and interest is repaid when last nominated resident leaves the property

Reverse Mortgages – Relevant standards

Client first, benefits & risks of your advice

Question 1: what Code Standards are very relevant to regarding your advice on reverse mortgages?

Reverse Mortgages – Relevant standards

Client first, benefits & risks of your advice

Code Standard 1

An (AFA) adviser must place the interests of the client first, and act with integrity

Code standard 9 – suitability

Code Standard 10

Concise description of the principal benefits and risks... having regard to the characteristics of those services

Sufficient information to enable the client to make an informed decision as to the suitability of a financial adviser service

Code Standard 5

An (AFA) advisers must effectively manage any conflicts of interest

Code Standards 16,17,18 - competency

There is an obvious market /need for ADVICE in case of reverse mortgages

Reverse Mortgages – benefits

- Uses the capital value of their home - to provide another financial option
- Available on the residential property that they live in
- Designed for lifetime occupancy – with safeguards, rules, lending limits
- Relatively easy to get (if the capital value there in home)
- Easy to understand the cost (rule of 72 @7.8% your debt doubles in 9.2 years)
- Buys the home-owner time – in time of stress e.g. bereavement, illness, aging
- Gives the home-owner options – especially at a stage of life-transition when decisions to retain or sell the home are complex or unclear
- Provides available funds to cash-poor, equity-rich clients
- The owner retains 100% ownership of the home
- The owner can still benefit from any increase in property values (compared to license to occupy arrangements)
- Lenders often offer an Equity Protection Option where a senior may choose to protect a percentage of the eventual net sale proceeds of their home

Reverse Mortgages – risks?

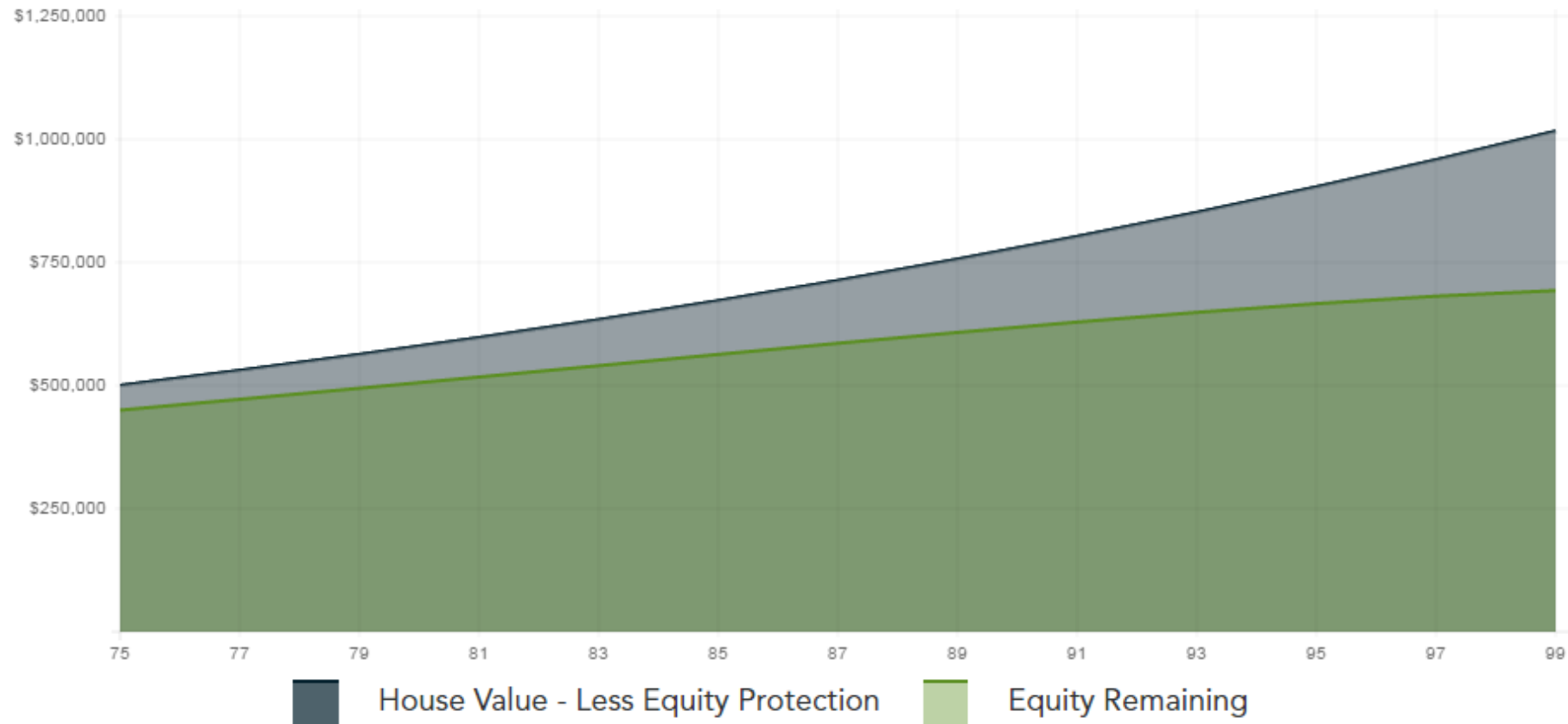
- RM are not widely understood by the NZ public – need for advice
- Owners may go into RM with poor or little financial advice – as to purpose, benefits, risks (e.g. even from their lawyer or accountant)
- Owners may draw down funds that are not immediately required (incurring interest-differential cost)
- Owners may draw down funds that are better sourced elsewhere (e.g. sale of other assets)
- Owners are not presented with alternatives that highlight the risks and benefits of their RM
- Other family members of seniors may not be informed on key benefits and risk to mortgage holder – which may lead to future confusion as to purpose
- Costs are not compared to other options

Compounding Interest and other costs

- The biggest financial cost associated with Reverse Mortgages is compound interest.
- At a rate of 7.8% an amount borrowed today will double in approx 9 years (time for compounded sum to double 'Rule of 72' $72/7.8 = 9.2$ years)
- Other costs are
 - Valuation fee
 - Bank Set up fee
 - Top up Fee (when accessing additional funds in future)
 - Clients own Solicitor cost

Aged 75 Home value \$500K draws 50K 3% property growth

How your equity and loan could look over time



Aged 75 Home value \$500K draws 120K 0% property growth

How your equity and loan could look over time



What clients want a reverse mortgage for...

- Benefits are more obvious (client first) for ...
- Restructure Debt
- Repay very expensive debt (e.g. credit card debt, personal loans)
- Frees up cash flow (e.g. by capitalising interest payments of mortgage)
- Funds for capital improvements on the home asset
- Funds for vital health interventions (e.g. Operations – Knee , Hip, Eye and more
- Funds for emergency costs
- Providing funds for better & enabling life-assets (e.g. safer, more reliable car)

Less obvious for...

- Travel, 'Lifestyle', discretionary expenses

What clients get

- Financial Independence
- Frees up cash flow
- Provides them time (to decide the future)
- Peace of Mind
- Dignity

Alternatives to a Reverse Mortgage

- Downsizing
- Using other assets
- Standard bank Loan
- Family assistance
- Using savings/investments
- <https://www.cffc.org.nz/retirement/retirement-villages/>

Client Segments

- Limited to no savings or savings that they will out-live
- Need to increase their monthly income
- Enjoying life to the fullest

Joy's story...

Joy is a widow aged 72

- Owns a home but has a \$35,000 mortgage still owing.
- Recently gave up part time work.
- Would like to keep home but can't see how....
- Her home is valued circa \$550,000.
- Son suggested she look at a reverse mortgage.

Outcome

- A reverse mortgage with an initial advance of \$55,000
- Repaid the mortgage
- Paid for dental work she had put off
- Covered set up costs of RM and gave her some money in the bank and an express top up facility

Peter and Marie

Peter and Marie are 76 and 74

- Own a mortgage free home.
- Are both fit and active and young for their age.
- Have \$20,000 savings in the bank.
- Have looked at downsizing but nothing as good as current home.
- Home is valued Circa \$650,000.

Outcome

- A reverse mortgage with an initial advance of \$30,000
- Paid for a more reliable car.
- Paid for a trip to Sydney to see the grandkids.
- Covered set up costs of RM and gave them an express top up facility.

Wally and Shirley

Wally and Shirley aged 83 and 81

- Built up a significant business during their working lives.
- Have an impressive home valued at circa \$2.5 Mill.
- Also own a holiday home value circa \$650k which all the extended family love to use.
- Wally and Shirley don't want to sell the holiday home and don't want to service a mortgage.

Outcome

Wally and Shirley took out a RM facility of \$450,000 drawing \$50,000 initially.

They continue to enjoy the standard of living they are used too.

Peace of mind

Each of the examples while different have similar characteristics

They want to stay in their home

Most who could benefit from a reverse mortgage are not aware they exist.

And all Financial advisers – Mortgage, Wealth or Risk based will come across these types of clients from time to time.

Case Study – the world trip?

1. John and Janice are aged 77 and 78 and are in good general health and are devoted grandparents. Family is very important to them and they have all three adult children living overseas
2. They have almost their entire equity tied up in their home in Tauranga with a recent valuation of \$900,000. They have been mortgage-free for five years and very keen to stay in their home until their mid-eighties. Although they have looked at license-to-occupy residential options in the region they far prefer to stay in their own home.
3. They have joint saving of \$50,000 in 6-month fixed deposit at the Bank
4. They are looking at a world trip next May that will cost \$60,000. They wish to visit and stay with their family in Canada, UK and Australia and enjoy the grandchildren. Although John and Janice are in general good health they are very keen to see the family before global travel gets beyond them.

What is your advice regarding their funding of their world trip?

What are the benefits of your advice?

What are the key risks of your advice?

Voluntary Code of Standards,

Ministry of Social Development

PRINCIPLES

- Consumer understanding
 - Full disclosure
 - No negative equity
 - Lifetime occupancy guarantee
 - Independent legal advice
 - Regular updates
 - Complaints process
-
- Lenders must comply with Responsible Lending Code revised June 2017

Key influencers

- **Family Members** – in your existing client base
- **Solicitors and Accountants** – in your networks
- **You!**

Resources

www.govt.nz/browse/housing-and-property/borrowing-against-the-value-of-your-home/reverse-mortgages/

<http://superseniors.msd.govt.nz/finance-planning/get-your-finances-sorted/income-options-for-retirees.html>

<https://www.seniorsfinance.co.nz>

www.consumer.org.nz/articles/reverse-mortgages



Q and A and True Story



Thank you

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