Retirees flock to reverse mortgages to tap equity in their homes

By John Collett
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The number of participants in the federal government's reverse mortgage scheme has grown more than five-fold in less than two years as more retirees tap the equity tied up in their homes to pay for living expenses.

Just 768 people had accessed the scheme at the end of the 2018-19 financial year but their numbers swelled to 4039 by the end of March this year.

A government-run reverse mortgage helps retirees live more comfortably
CREDIT: *JIM DAVIES*

The Pension Loans Scheme (PLS) allows those who have reached age pension age to top-up their income, where their family home (or other real estate) is put up as collateral. When the house is sold, the loan is repaid from the proceeds.
However, the scheme has to approached carefully. As the loan is not repaid until the sale, interest is capitalised and over time and the debt can grow to erode a large part of the property's value.

The government-backed scheme is conservatively managed but, from the middle of next year, it will come with a "no negative equity guarantee", meaning borrowers will not have to repay more than the market value of their property.

The maximum income that can be received under the scheme is 150 per cent of the full age pension. It is open not only to full and part-pensioners but also self-funded retirees.

It means a full-rate pensioner can receive a maximum income top-up that is equal to half of the age pension. For a self funded retiree, the maximum is equal to the 1.5 times the full age pension.

For part-pensioners, the cap is somewhere between, depending on how much of a part-pension is received.

The payments are not assessable for the age pension means test.

The loan can only currently be drawn as an income stream. However, from the middle of next year, participants will also be able to access up to two lump-sum advances in any 12-month period, up to a total value of 50 per cent of the maximum annual rate of the age pension.

It is not yet clear whether the lump sum withdrawals will be available to existing participants, or whether the no negative equity guarantee will be retrospective.
Katja Hanewald, Hazel Bateman and Katie Sun, of the School of Risk and Actuarial Studies at the University of New South Wales (UNSW), expect access to lump-sum payments will increase the attractiveness of the scheme. That is because many retirees would like to make large purchases, such as a new car, home improvements or repairs.
Figures cited by the academics show about two-thirds of PLS participants at the end of last year were full-rate pensioners, with most of the rest part-pensioners. Uptake by self-funded retirees is relatively small.

“The Pension Loans Scheme plays an important role, as the family home is typically a retiree’s largest financial asset,” the UNSW authors say.

“Schemes that allow people to unlock their housing assets – such as the PLS – should be far more popular than they are.”

One criticism of the scheme the authors make is that the variable interest rate of 4.5 per cent on the loan is too high and should be cut. It is lower than private sector reverse mortgages but significantly higher than the record-low interest rates for regular owner-occupier mortgages.