Is a reverse mortgage right for you?

Drawing on the equity in your home, a reverse mortgage is like a loan to yourself—and one you won't have to repay while you're alive. We walk through the benefits and disadvantages to help you decide if a reverse mortgage is the right solution for you.

Many Canadians are "house rich." Their net worth appears healthy (the average tops $675,000), but in reality, a large chunk—sometimes 50% or more—of that wealth is tied up in their homes. Factor in the nation's growing personal debt (according to Statistics Canada, we collectively owe $1.77 for every $1 in disposable income), and it isn't surprising that interest in reverse mortgages is growing.

A reverse mortgage is one of several options we have for borrowing money against a home's equity. (Your equity is the present-day value of your home, minus mortgage principal or other debt tied to your home that's remaining to be paid down.)

In the past, reverse mortgages were viewed with skepticism; a loan you don't have to repay as long as you live simply seems too good to be true. But for Canadians in specific financial circumstances, a reverse mortgage can be a practical solution.

This guide looks at how reverse mortgages work, and which types of people could benefit from them, to help you decide whether it might be a good option for you.

What is a reverse mortgage?

A reverse mortgage is a financial product that allows you to borrow from the equity in a home you own, while continuing to own it and live in it.

In Canada, if you're age 55 or older, you live in your home for more than six months of the year, and your home is appraised at the lender's minimum required amount or higher, you are eligible to borrow up to 55% of its value. For example, Equitable Bank*, which is one of only two financial institutions currently offering reverse mortgages in Canada (specifically in British Columbia, Alberta, Ontario and Quebec), stipulates that the borrower's home value be at least $250,000, and your reverse mortgage principal (the amount you borrow) must be at least $25,000. There are no monthly repayments required until the mortgage is due.

You can get a reverse mortgage even if you already hold a conventional mortgage on your home. However, once you receive the money from your reverse mortgage, you must use a portion of it to pay off your previous mortgage, along with any other liens (debts attached to the property). This ensures the reverse mortgage lender is your first priority for repayment, when that time comes.

How does a reverse mortgage help homeowners access funds?

Homeowners who qualify for a reverse mortgage can receive the funds in the following ways:

- as a one-time lump sum;
- a large amount upfront, followed by smaller amounts that you can schedule (e.g., monthly or annually) or request at your convenience.

In either case, reverse mortgage borrowers will receive the cash tax-free.

As with a conventional mortgage, there are setup fees with a reverse mortgage, which you should factor into your decision about whether to use one. The Equitable Bank Reverse Mortgage Eligibility Calculator is a good place to start. In less than a minute, it will give you an accurate estimate of the amount of funds available to you.

You don't need income to qualify for a reverse mortgage, and you can choose from a variety of terms, and a fixed or variable interest rate. (As of August 2020, Equitable Bank's 5-year, fixed rate, lump-sum reverse mortgage was posted at 3.79%).

Who is a reverse mortgage for?

There are a few scenarios where a reverse mortgage can be a solid option. Let's take a look:

Retirees who need extra income

Because the cost of living is high in many parts of the country, it's hard for people to buy a home, pay it off, raise children *and* save for retirement, says Annie Kvick, a Certified Financial Planner with Money Coaches Canada in North Vancouver. This can leave many short of cash in retirement, when they have fewer borrowing options because they're no longer receiving income.

A reverse mortgage is one tool retirees can use to pay for expenses like groceries, home repairs or medical care, Kvick notes. It's also an option for retirees who are covering their expenses, but want to gift money to someone now, rather than waiting to pass along those funds in their will.

However, Kvick notes, it's important to have a plan for using reverse mortgage funds—otherwise, she says, "you might spend too much in the early years and then run out of money."

Retirees who want to stay in the family home

Many people prefer to stay in their family home when they retire, and for good reason. "You've created a community, you have friends there, it may be close to shops and hospitals, and it's also costly to sell and buy [another] home," says Kvick.
A reverse mortgage can help you stay in your current residence, whether you need the loan money to pay for daily expenses, property maintenance, or renovations to make your home more accessible in terms of mobility.

House-rich Canadians who need help with cash flow

Another scenario where a reverse mortgage may be helpful is if you are house-rich but cash poor, and life deals you a blow, such as a job loss, a divorce or the death of your partner.

If you need a bit of financial help, a reverse mortgage might be one way to bridge the gap until you have other options, like income from a new job, or you're able to qualify for government assistance, like Old Age Security, or able to access registered retirement savings. "You might not qualify for a normal mortgage or line of credit," Kvick says, due to restricted income, for instance.

Financially savvy people who are ready to "decumulate"

Spending your money well in retirement (decumulation) takes careful planning and, in some cases, it may make sense to use a reverse mortgage to access the equity in your home as part of that plan.

"You have to look at your overall picture, your tax bracket, how your investments in your RRSPs are doing," Kvick explains. "They might be doing well and [so] you don't want to cash them out; or they might have a loss and you don't want to sell them [until they've rebounded]." In such cases, a reverse mortgage can provide cash flow until your investments are where you'd like them to be in order to begin drawing on them.

Deciding if a reverse mortgage is right for you

As with every aspect of retirement planning, Kvick says it's important to have a clear understanding of your overall financial picture.

Considering a reverse mortgage is part of a larger financial decision when it comes to your home and your family. As you discuss this option with your loved ones, you'll be better prepared to make a decision that's right for you. A reverse mortgage can be a useful financial tool, if it is used as part of a plan that takes into account what the funds will be used for; how much you can count on from other sources of income, including government benefits, registered retirement savings and other investments; as well as how and when the reverse mortgage will be repaid. Working through the numbers with a financial professional can help set you up for success.