How to use the budget pension loan scheme for aged care help

- AFR OPINION
- Updated May 16 2018

More people are retiring with a small home loan debt so they refinance it into a reverse mortgage to take the pressure off the cash flow. by **Bina Brown**

If you or a loved one have equity tied in property which could be used to live a better life or access care, then why not use it and let the beneficiaries sort things out after you have departed?

It is a concept that won't sit well for some.

For others it may be the only option – which is possibly why the government extended its existing Pension Loans Scheme (PLS) in this year's federal budget to include all eligible retirees while increasing the amount you can borrow.

It cements what many have been saying for a while: that the family home, as a store of wealth, has become the fourth pillar of the retirement income system.

The government clearly recognises that even with additional home care packages it also announced, there is still a considerable wait for the higher levels. And even if you get a higher level package it may not be sufficient to enable you to remain independent – hence the need to privately fund extra help.

Related Quotes

Funds released from accessing the equity in the home could fund in-home care needs such as showering and cleaning.

National Seniors Australia believes the eligibility changes will help improve access to the scheme, which will now be open to Australian residents of 10 years or more, of retirement age and who own their own home.

According to Aged Care Steps, under the new rules a couple on a full pension may be eligible to borrow up to $17,787 a year of income from the government (taking total payments including age pension up to 150 per cent of the full couple rate of age pension).

A single person on a part pension of, say, $400 a fortnight could borrow $961 a fortnight ($24,996 a year).

A self-funded retiree could borrow 150 per cent of the maximum pension entitlement which is equivalent to a maximum of $35,396 for a single person and $26,680 each for a couple – although you would have to ask why they would want to go into debt if they are self-funded.

What it will cost

With an interest rate of 5.25 per cent, the PLS is priced slightly lower than the 6.25-6.40 per cent being charged for reverse mortgages, another equity release product.

It also compares favourably to the 5.77 per cent charged on the daily accommodation payment (DAP) in residential care.

Darren Moffatt of Seniors First Reverse Mortgage Broker believes the extension will be of greatest benefit to full pensioners with no other options to increase their income.

But its scope is limited due to the fact that it doesn't offer lump sum funding, says Moffatt.

In the 12 years he has been assisting senior borrowers – his company has originated about 1500 reverse mortgages – he says most people want only a small to medium lump sum, often with further access to a "cash reserve" to mitigate longevity risk . The average loan is about $85,000.

Most borrowed money is used for debt consolidation, home improvements, a new car and then aged care.

With a reverse mortgage, borrowers use the equity in their home as security for a loan that can be taken as a lump sum or a regular income stream. The interest charged doesn't have to be repaid until you move out of your home or sell it, but the interest compounds over time, adding to your loan balance.

A "no negative equity" guarantee is a given.

Moffatt says more people are retiring with a small home loan debt that they can't afford to service, so they refinance it into a reverse mortgage to take the pressure off the cash flow.

Other loans to look at

What the PLS won't help with is the sizeable lump sum often needed by part pensioners and self-funded retirees for residential aged care (although it could help with the DAP).

There is another product: the aged care accommodation loan.

La Trobe Financial's Aged Care Loan is designed to fund the payment of the refundable accommodation deposit (RAD) for entry into residential aged care rather than sell the family home. It is a seven-year variable rate loan available to people aged over 80 who can access up to 50 per cent of the value of their home or a maximum $750,000.

When the borrower leaves the facility, the RAD is refunded back to La Trobe Financial, the borrower or the estate pays any accrued interest and the mortgage is released debt-free.

The loan can also be used to pay the DAP or part thereof.

Benefits of the strategy can include improving cashflow, pension and tax outcomes, retaining the property asset to pass on and bridging the period between entering aged care and a planned orderly property sale, says La Trobe Financial senior vice president Martin Barry.

Homesafe Wealth Release offers a debt-free equity release solution which general manager Dianne Shepherd says allows borrowers access to the equity in their home as well as the ability to protect a share of the future equity in their home for their own needs or as part of their estate planning.

The homeowner agrees to sell a share of the future sale proceeds of their home in return for a lump sum payment today which could then be used to pay for in home care. The product considers several factors such as age of the homeowner and the value of the home today, which then determines the amount which can be released as a lump sum. The process applies a discounted cashflow model to work out the available equity today and there are no ongoing fees.

With a debt-free equity solution, the share the provider receives on sale will depend on the sale price. By contrast, an accommodation loan, reverse mortgage and the PLS compound interest on to the debt so the interest rate is in effect increasing over time as the debt accumulates whether the value of the home rises or falls over time.

In a user-pays aged care system, it's not surprising the funding options are also growing.

Bina Brown is a director of aged care solutions company Third Age Matters.

AFR Contributor