

4th Phase of Retirement 2nd Through 15th Year

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Once you have transitioned into retirement and gotten accustomed to your retirement spending routine, the issue of how to deal with debt becomes important. First, short-term debt should have been retired, whether it is credit card debt, auto loans, personal loans, etc. before retirement. A larger consideration is always mortgage or no mortgage. Some consider it important to pay off the mortgage before considering retirement, others buy their dream home after retirement. There is no single answer. First, if you can comfortably cover the mortgage payments from your retirement income why use up assets to pay the mortgage off? Second, if you own your home you can always: (a)refinance, (b)establish a home equity line of credit, or (c)take a reverse mortgage to generate cash and continue to live in the home. Of course, you can always sell the home, buy-down or perhaps you already own a second home to generate cash. There is currently favorable tax treatment on capital gain on your primary residence if you have established it as a primary residence for 2 years out of 5 years immediately preceding the sale. As a couple, you can exclude a gain of \$500,000 and as a single owner you can exclude a gain of \$250,000 before capital gain taxes are due. If you are planning to sell a home that you either own or have sizable equity in and are purchasing a new home consider taking a mortgage for the new home, and investing the money from the current home. This provides you with liquid assets (the interest, and rate of return would be taxable income) but the interest on the mortgage would be tax-deductible. Additionally, your property taxes and hazard insurance would be escrowed. If either you or your spouse died, the survivor, if they so wanted, could pay off the mortgage with the proceeds from the sale of the first house.

Reverse Mortgages

Some are not familiar with reverse mortgages and yet a recent study by the National Council on Aging found that 13 million older homeowners are candidates for a reverse mortgage.

A reverse mortgage is a loan against the value of your home that you do not have to repay until you move, sell or die. For the Federally-insured reverse mortgage, everyone on the title to the house must be at least 62 to qualify. A reverse mortgage can be paid as a lump sum, line of credit, lifetime monthly payments or a combination of the three. Reverse mortgages do have closing costs (the Federally guaranteed Home Equity Conversion Mortgage averages 2%). There is also a mortgage insurance premium of 2% of the value of your home. Add appraisals, title searches and other preparation fees and the total closing costs can tap 5% of the value of your home. In addition to the costs of a reverse mortgage remember that it must be paid off when the home owner moves, sells or dies. This usually means that upon the death of the owner(s), the mortgage company recovers the value of the payments made which can equal the full value of the home. Therefore, the heirs would not inherit the home short of paying the reverse mortgage company.

The amount you can borrow in a reverse mortgage hinges on your age, the home value, and interest rates. The older you are, the more you can borrow. Some reverse mortgages are now available for second homes. World Alliance Financial has introduced "Simple 60" for those as young as 60 years old. The FHA's Federally-insured reverse mortgages aren't available for anyone under age 62.

You do not have to explain what the money from the reverse mortgage will be used for. However, too often, retirees are urged to use the money to take out a deferred annuity. Deferred annuities "are almost always inappropriate for seniors, as they can tie up retirement savings far beyond one's life expectancy," Senator Herb Kohl (D., WI) said during a recent Congressional hearing on reverse mortgages. Single women - who account for about 45% of reverse mortgage borrowers - according to an AARP study, may be particularly susceptible to such advice.