Intergenerational gifting – why is equity release becoming a wealth management tool?

Equity release is widely acknowledged as a useful product for those who don't have savings or other assets to fall back on. However, over the last 3 years, a growing number of high net worth homeowners using equity release as a wealth management tool, with an average client age of 75 years old.

So why would a wealthy 75-year-old want or need equity release?

Let's start by clarifying what we mean by high net worth (HNW). The FCA definition is "a customer with an annual net income of no less than £300,000 or net assets of no less than £3,000,000, or whose obligations are guaranteed by a person with an income or assets of such amount." (FCA Handbook Glossary).

There are 3 reasons why this new niche market has emerged:

The cost of equity release has fallen dramatically from where it was ten, or even five, years ago. HNW individuals and their advisers are beginning to realise they can now access the wealth tied up in property at a historically low cost.

Products have evolved, with more flexible options than we've ever seen before. For example, customers now have the ability to make ad hoc interest payments, repay some of the capital borrowed, and use a draw down facility. This increased flexibility against what was previously a rather rigid, the illiquid asset has brought property wealth into broader financial planning discussions.

We're also seeing attitudes shifting:

Attitudes towards retirement are changing, with it no longer being seen as a 'cliff edge' moment. Many are choosing a more gradual transition away from work, or choosing not to retire at all.

Attitudes towards property wealth are also changing. Older homeowners have seen significant growth in the value of their homes, perhaps more than in their other assets, over the last three decades. That same set of consumers has seen a huge shift in the pensions landscape over the last 10 to 20 years. As a result, income in retirement often involves having various sources, including property, and for the wealthy, they may well flex between these sources.

Attitudes towards inheritance are changing. We are all living longer, and the age at which we inherit from our parents is steadily increasing into our 60s. The view that our property should be set aside as a legacy for our children when we pass away is slowly fading, as we increasingly realise the benefits of passing that wealth down much earlier in our lives.

How high-net-worth individuals are applying equity release:

Transferring wealth to the next generation

Transferring wealth effectively and efficiently is a concern, and using Equity Release in order to pass wealth down to children and grandchildren is becoming an attractive way for the wealthy to address this concern. This has to be done with great care, and we regularly find ourselves working hand in hand with wealth managers, financial planners, tax advisers and other trusted professionals to help clients.

Estate planning

For HNW individuals, equity release is becoming a key estate planning tool, as creating a debt against the main residence can lead to Inheritance tax savings. Home reversion plans may also have a role to play here, as the switch from owner to lifetime tenant could be an attractive IHT strategy.

The reality facing many wealthy homeowners, who have benefitted from the increases in the value of their homes over the last three decades, is that a huge chunk of that growth is liable for tax unless they do something about it. We have found ourselves working alongside a growing number of trusted professionals to assist them in estate planning for their clients. This is just one area where the overlap between equity release advice and other forms of planning advice requires careful input from two sets of experts.

Managing income

Another area where this overlap is happening is in advice on income. Property wealth can be used to top up income by using the draw down facility under a lifetime mortgage. For a higher rate tax payer, a lifetime mortgage with a draw down facility could present an attractive alternative to drawing from uncrystallised pension funds, as the cost is in the interest charged over a number of years, rather than a single, and potentially large, income tax payment. This gives both client and Wealth Manager the ability to make flexible decisions on the most tax-efficient, and cost-effective, source of funds.

In summary, equity release is being talked about more positively in wealth management circles and is being used in an ever-increasing range of ways to create flexibility and open up new solutions for high-net-worth homeowners.