WHICH? TESTS EQUITY RELEASE ADVICE

Undercover investigation finds 'experts' giving advice that could leave pensioners out of pocket

PHOTOGRPAHY BY: MATT WALFORD

While most of us hope that pensions and life savings will pay our way in retirement, one in three people plan to part fund it using their home.

Equity release schemes unlock value in your home, but they're complex and many people seek advice to see if they're right for them.

However our investigation has revealed that many financial advisers who sell equity release products offer inadequate and inconsistent advice.

WHAT WE DID

We posed as potential customers (see 'Which? Research', right) and visited advisers who are qualified to recommend equity release products to test how good the advice was.

We expected them to question us thoroughly about our outgoings, discuss the products in detail, make clear what products they were able to recommend, their fees and to discuss alternatives. They should also discuss the effects on benefits, long-term impact and exit penalties.

We conducted 22 visits, including a snapshot of five advisers from the biggest providers of equity release products: Aviva, Equity Release Assured (LV), Just Retirement. 15 were to independent financial advisers, intermediaries, and two to national debt charity the Consumer Credit Counselling Service (CCCS).

WHAT WE FOUND

■ Most advisers failed some of our tests, but there was no clear difference between the

THE THREE MAIN EQUITY RELEASE SCHEMES EXPLAINED

1 LIFETIME MORTGAGES

Lifetime mortgages let you borrow a lump sum against the value of your property whilst allowing you to stay in your home.

Unlike a typical mortgage, you don't make regular payments. Instead, the interest charged is compounded and added to your loan. The loan and interest is repaid when the house is sold as a result of death, or if you leave for medical reasons, typically when entering a care home.

Some of the schemes will also allow you to pay off the interest each month.

2 DRAWDOWN OR 'FLEXIBLE' LIFETIME MORTGAGE

The dominant form of equity release, and the leading growth area, making up 61% of the market. Identical to a lifetime mortgage scheme, except that rather than just having access to an initial lump sum, the lender also offers a drawdown reserve. Arranged at the outset, this lets you withdraw smaller amounts at short notice. You only pay interest on what you borrow, not the full reserve. It was recommended in the vast majority of our visits.

3 HOME REVERSIONS

Home reversion schemes, which are typically only offered to those over the age of 65, let you sell a percentage of your home to the provider for a lump sum.

The difference between this and a lifetime mortgage is that you are effectively selling a portion of your house rather than borrowing money. This means that you have certainty over the percentage of your property you'll be left owning when you die. With a lifetime mortgage, the interest can keep rolling up until you owe the entire value of your property, whereas with a reversion plan, you know that if you sell 50% of your property, your estate will always be left with the remaining 50%.

The disadvantage with home reversion plans, however, is that you'll sell the portion of your home for less than it's worth – 40% wasn't uncommon last time we reported on this issue.

Additionally, it's worth bearing in mind that if the value of your property rises, the equity release provider will take all the upside on their share of the property.

providers and IFAs, with some good and bad in both groups. Of the two Aviva visits, one was almost perfect and the other was average, Equity Release Assured (LV) was poor on one visit and average on the other, and our visit to Just Retirement was poor. Only CCCS passed all tests.

- Four advisers offered wholly inadequate advice.
- 12 advisers (IFAs, tied and multi-tied advisers) gave inconsistent advice with some key failings.
- While only CCCS passed all our tests, four other advisers were almost perfect.
- One adviser suggested that our 75-year-old researcher – who was looking for a bit of money to carry out essential maintenance – instead take out significantly more and invest it. This was incredibly risky advice as investment returns after tax are unlikely to beat the borrowing costs of releasing equity.
- Common problems included advisers not adequately disclosing their status and fees, bad fact finds (see right) and not properly discussing benefits, exit fees and alternatives.

WHO THEY ARE

The advisers we looked at were all qualified to discuss equity release and regulated by the Financial Services Authority (FSA), under the Mortgages and Home Finance: Conduct of Business (MCOB) rules.

What they should say The rules demand that advisers say whether they can recommend the full range of available products or not, consider whether the product is right for the consumer and discuss other ways to raise the funds they want. The Aviva advisers were tied advisers, meaning they can only recommend Aviva products, while Just Retirement and Equity Release Assured (LV) were multi-tied advisers – so they recommend a range of, but not all, products. All IFAs and intermediaries we spoke to looked at the whole market, as did the CCCS.

What they did say Less than half the advisers tested carried out a full discussion of their status (which providers they looked at), how they were regulated and their fees – essential for any form of financial advice.

On three visits to multi-tied advisers they failed to adequately disclose that they could only recommend a certain range of products. Three advisers didn't discuss their fees (which can come to about £900). Some others failed to provide an initial disclosure document to our researchers, which presents their status to the client – a potential breach of FSA rules – and one told us he'd forgotten to pack it. The best advisers talked us through the document, highlighting fees, regulation and their status.

FACT FINDING

What they should say The adviser should take you through your income, debt and spending, from council tax to food and shopping costs to get a full picture of your circumstances.

What they did say The majority did this, but five failed this test by not taking income, debt and savings into consideration, or not going into sufficient depth. Frequently, queries were limited to asking our fieldworker 'do you struggle to make ends meet, or do you get by'.

This is insufficient – good advisers should analyse your income or debt level before recommending a potentially risky product such as equity release.

WHAT THEY RECOMMENDED

What they should say A thorough discussion of equity release should include a description of products; an explanation of the interest rates and how they're compounded; the limits and drawbacks of schemes; the costs; and recognition that house prices can go up or down.

What they did say 12 visits comprehensively dealt with these issues, but many advisers we tested, tied and independent, didn't.

WHICH? RESEARCH

We used two scenarios in our research. In the first, we asked our mystery shoppers to pose as a couple in their mid-60s, recently retired and with a reasonable disposable income. They said they were looking to borrow around a quarter of the value of their home as a lump sum to conduct non-essential home improvement works, like building a conservatory. We wanted the adviser to consider future consequences given their relatively young age, but to discuss equity release as a possibility.

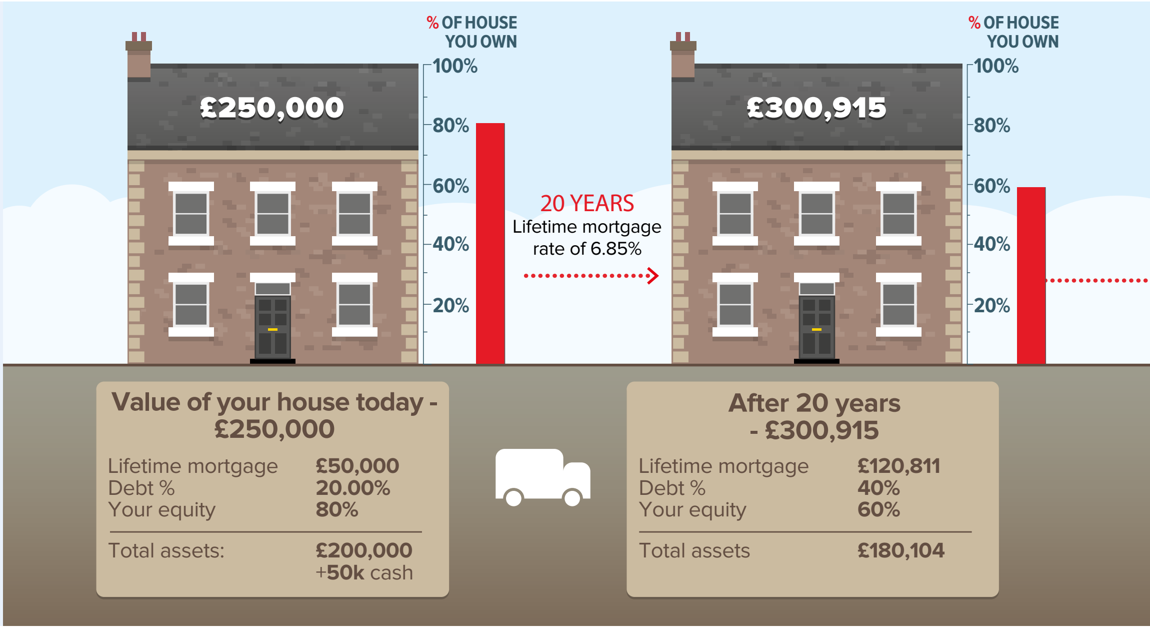
In the second scenario, we used a single person in their 70s, with a far lower income of a state pension and no savings, looking to release £10,000 for essential repairs and a little income. In this scenario we were looking for the advisers to discuss local authority grants and particularly the interaction with benefits, before making a recommendation.

LIMITING YOUR OPTIONS

This infographic shows the cost of equity release over 20 years and how it can limit the options of those who want to move or pay off the debt.

In this scenario we show the effect of releasing £50,000 from a £250,000 house now. Within 20 years, taking house price rises of 1% a year into account, the debt will have ballooned from 20% to 44% of your property value.

But exit and moving fees also have to be considered. All figures shown are at today's prices and adjusting for inflation of 2% per year.



Most advisers gave a detailed description of the products they recommended, but nine failed to adequately discuss all basic features. Three failed to properly describe the interest rate payable on the money released from your home and how your debt would grow – it typically doubles after every 10 years (see 'Limiting your options', above). One underestimated the interest cost by half, stating that with '£10,000 to start with, after 10 years the amount outstanding may be £15,000'. Few discussed other limitations such as not being able to take out other borrowing on the property and the need to maintain the property.

In six visits only, Lifetime Mortgages were considered and Home Reversions were either quickly dismissed or, in three instances where our fieldworker would have been eligible, weren't mentioned. Home Reversions can be costly, but we would have liked to have seen a balanced discussion of the pros and cons of each scheme. When it came to discussing house prices, we found that six advisers failed to mention that house prices could go down and assumed they would increase. One independent adviser said, 'House prices will start to move up again, supply and demand… dictates that will happen.'

Some people may also be concerned about the impartiality of the advice they get from a tied or multi-tied adviser. We found the advisers in all Just Retirement and Equity Release Assured visits recommended the products they were linked to, Just Retirement and LV.

In all these cases it's possible the products were the best, but it's an issue to consider when speaking to a tied or multi-tied adviser.

ILLUSTRATION BY: PAUL BUTT

> IT'S ABOUT LONG-TERM VALUE AND LONG-TERM VALUE CAN INCLUDE THINGS LIKE FUTURE FLEXIBILITY DEPENDING ON WHAT THE PLANS ARE, WHETHER YOU MIGHT WANT TO REPAY EARLY OR MOVE.
>
> **FINANCIAL ADVISER OFFERING EXCELLENT ADVICE**

NO ALTERNATIVE OFFERED

What they should say Equity release isn't always the best option if you're looking for money and advisers are required to discuss the alternatives. This could be anything from downsizing, taking out a personal loan or standard mortgage, to asking family for help or looking into local council grants.

What they did say Ten advisers failed to mention alternatives to equity release properly.

For the 12 visits we made using the second scenario, only four mentioned the possibility of speaking to the council. But this is an essential first step before considering equity release, and not mentioning it potentially breaches MCOB rules. Contrast this with the CCCS, which after going through its disclosure document said 'Let's look at alternatives first', then thoroughly discussed council grants and benefits.

LOSING YOUR BENEFITS

What they should say Withdrawing a lump sum can affect your benefit allowances. The impact can be complex, and need not be negative, but must be considered and discussed by advisers.

What they did say Eight advisers failed to discuss the interaction between equity release and benefits entitlements. More worryingly, five we spoke to using the second scenario failed to mention the effect withdrawing a lump sum could have on benefit allowances. This is another potential breach of MCOB rules. Withdrawing a £10,000 lump sum, as in our second scenario, could see you lose pension credit. Seven advisers in the second scenario explained this properly.

LIVING FOR TODAY

What they should say As the name suggests, lifetime mortgages are designed for life, so the adviser should make clear that exit penalties can be costly, ranging up to 25% of the original loan.

What they did say Nine of the 22 advisers we tested failed to properly explain exit penalties, even when product features were being discussed. Market leader Aviva's exit penalties are complex and vary, as they're linked to gilt-prices, but most advisers (including two who recommended Aviva) didn't mention this. One told us, 'You're never tied to it [the product], if you want to repay the plans or switch the plans' but failed to mention exit penalties at all.

We found inconsistencies in how advisers

You die or enter a care home

Value of house	£300,915
-Equity release debt	£120,811
-Cost of sale	£9,172
Cash remaining	£170,932

Pay off debt and quit scheme

Value of house - debt	£180,104
-Estimated exit fee	£12,500
-Cost of sale	£9,172
Equity remaining	£158,432

Transfer Lifetime Mortgage

Value of house	£300,915
-Equity release debt	£120,811
-Moving cost	£16,157
Equity in your new house	£163,947 (61%)

Lifetime mortgage - average fixed rate (6.85%)

Reversion (selling 56.08%)

Projected property value

This chart shows what a couple aged 65 would owe if they released £50,000 from a home worth £250,000, using either a Lifetime mortgage or home reversion scheme over 25 years.

The value of the home increases by 1% per year. There is an assumed underlying rate of inflation of 2% per year.

described how equity release would affect our researchers' options in later life, despite 10 of our 22 visits being with fieldworkers aged 65 or younger. Only a few satisfactorily explained the effects of equity release on future choices. On the most basic level, it affects inheritance, but it can also reduce your downsizing options, which may be important in future (see graphic, above).

DRAWDOWN SCHEMES

Drawdown or flexible equity release products (see 'The three main equity release schemes explained') operate like an overdraft facility, allowing you access to a larger sum of money you don't pay interest on until you draw on the income. Almost all the advisers we spoke to actively encouraged having such a facility.

The key benefit is that you only pay the arrangement fees of setting up an equity release loan (typically about £1,500) once, and having a reserve facility could be useful in an emergency. But many advisers based their calculations on the maximum available, not what we asked for. The fact that extra funds can so readily be accessed may act as a temptation. This could prove costly, especially given how quickly interest grows on equity release products. Perhaps tellingly, some advisers are paid by commission based on amounts borrowed, and in some cases more commission may be offered when more equity is subsequently drawn down.

WHICH? SAYS

Changes are afoot, (see 'Expert View') but SHIP and the FSA, which regulates the market, must do more. Spiralling interest and the difficulty of leaving a scheme can restrict choice should your needs change, so equity release should be treated cautiously, with proper, varied advice sought.

This is most clearly the case for low-income homeowners using equity release for repairs, or those on benefits. Low-income homeowners seeking to maintain their properties to a reasonable standard should approach their local council as there may be better solutions on offer such as council grants or improvement loans.

There are fledgling equity release schemes that allow smaller amounts to be borrowed, such as Age UK's scheme. The Joseph Rowntree Foundation is piloting a scheme for those on pension credit in partnership with a number of councils. Those concerned about paying for care home fees should contact their council about deferred payment schemes, which like equity release let you keep your property while the council pays care home fees. It recovers the fees from the proceeds when the property is sold.

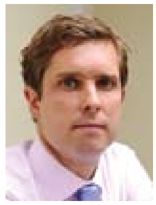
Our advice

For those with high-value properties with a reasonable income but little savings, equity release can be an option. But anyone considering it should discuss it with family and rule out other options first, before speaking to a number of advisers.

We found the CCCS offers the best advice, but you can find specialists at financial planning.org.uk or findanadviser.org where you can search for IFAs with an equity release qualification. Get written information including an 'Initial Disclosure Document' and a 'Key Facts Illustration' at the start of the meeting.

EXPERT VIEW

A COMPLEX PRODUCT



Equity release is complex and expensive, so it's crucial the advice that goes with it is of the highest quality and that advisers explain the risks and alternatives. We found the advice isn't good enough, leaving us to worry that many sign up to products without understanding the implications. We heard some good and some excellent advice, but plenty of visits weren't.

The market has improved in the past 20 years and we no longer hear of people paying back more than their property is worth, but there's still a problem with how equity release is sold.

Industry body SHIP wants to expand to include those who sell equity release. This will help monitor the quality of advice, not just products. There is a need for extra scrutiny, but if SHIP is to have an impact, it must hold to account those who don't abide by its code of conduct. And we would like to see the Financial Services Authority to get a better grip on standards. There's still a long way to go until this market works for consumers.

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