

INFORMATION AND KNOWLEDGE BASE

LIFE RIGHTS

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“Don’t walk in front of me – I may not follow, don’t walk behind me – I might not lead; walk beside me as a friend” – Albert Camus

- Chapter 21 -

LIFE RIGHTS

21.1 Introduction

Lately life right purchases have come under fire and is seen by many as a bad option when considering moving into a retirement village. This statement is only true if the initial price of the life right is incorrect when compared to the full title purchase option or a rental option available in the same village.

Chapter 8 – Property Ownership and Management, is a good chapter to look at before continuing with this chapter.

Life Rights in a nutshell:

- Life Right is an upfront investment made by an individual to purchase the right to occupy a property within a retirement community.
- In return, you get to enjoy all the benefits that the village has to offer without the responsibility of maintaining your property or managing the responsibility that would usually come with the services provided.
- When this Right is resold, the original Life Right purchaser or his/her estate will be refunded a portion of the original purchase price. This refund varies from one retirement village to the other.
- Your rights are protected under the Housing Development Schemes for Retired Persons Act of 1988 (HDSRP).

The following article gives a good understanding of what life rights are all about:

Life rights - Gaining a deeper understanding 06 September 2021 Candice Wernick, CFP®
Associate Financial Planner, BDO Wealth Advisers

It is more and more common for retirement units to be sold on a 'life rights' basis. But still many retirees do not fully understand the concept

It is that time of your life. You have worked hard, and now it is time to settle into your retirement. Besides deciding on your retirement home, you must make sure you can afford the lifestyle you would like to live. After working hard for decades, you certainly deserve it!

Lots of retirees opt to move into a retirement village due to the security and 'resort-style' living. In many retirement villages, you will find that you can only purchase a 'life right' in the complex.

This may be an entirely new term for you. Or it may be one you have heard about but never entirely understood. This article will fill in the blanks by helping you to understand what a life right contract is and look at the financial pros and cons.

What is a life right?

A life right is a contract entered into where you, as a retiree, purchase the right to live in a home in a retirement village for the remainder of your life, and the developer retains the unit's ownership. Upon your death, the right reverts to the developer who will resell the unit. The amount that your deceased estate will receive on your death as compensation is outlined in the contract. A couple can also enter a life right contract. In this case, the right extends to both partners and is enjoyed until the death of the last surviving partner.

Retirees who enter a life right contract are protected under the Housing Development Schemes for Retired Persons Act 65 of 1988 (HDSRPA). The Act states that you must be at least fifty to enter a life right contract, but retirement villages do sometimes have their own (higher) minimum entry age.

The contract details all the rules and limitations of purchasing the life right, as well as what compensation you will receive when you pass away or decide to move out of the retirement village. It is crucial to fully understand all the terms and conditions laid out in the contract to ensure you are not caught out.

Pros

Less admin. Lower costs.

Buying a life right in a retirement village is usually more affordable than buying an equivalent unit outright. This is ideal if you have less capital available. What's more, as the property is not being transferred into your name, no transfer/bond costs will apply. Finally, the owner is responsible for the maintenance and upkeep of both the unit and the village. This takes a huge burden off you – both in terms of cost and effort.

Plan ahead

If a new development, it is also required by law to provide a two-year cost estimate of all levies. We all know budgeting is super important, especially when you are retired. This is a great advantage as it enables you to plan your monthly spending more accurately.

Fringe benefits

Most retirement villages offer a range of added benefits. These include daily meals, coffee shops, cleaning services and libraries, among other things. We would advise looking into the costs (if

any) associated with these additional facilities, as they may provide an opportunity to reduce your budget.

Cons

Financial fine print

The contract states the amount you/your estate will receive on termination of the life right. This amount may be your purchase price plus a percentage of any profit made on the resale of the unit. But it could also be less than the amount you paid. If you are unsure about the terms of the contract, chat with your financial planner or consult a legal professional to help you understand the return on investment. If you really want to live in a particular property, you may be prepared to take a financial hit, but please make sure you understand the fine print before signing on the dotted line.

Nothing to bequeath

When you (or your surviving partner) dies, you cannot bequeath the life right to anyone in your Will. The right will revert to the developer, and they will, in turn, resell the unit. You will however be paid what is due to you in accordance with the contract.

If you've entered a life right contract as a couple, no compensation is payable after the death of the first spouse. The life right simply continues in favour of the survivor. Only on the death of the last surviving spouse will an amount become payable to that spouse's estate. The life right contract cannot be 'split.' This means that the estate of the first spouse to die receives no benefit or compensation. This is an especially important consideration if you and your partner/spouse have different provisions in your wills.

Potential delays

As you are not the homeowner, the owner must arrange the resale of your unit. In some agreements, only once it is sold will the proceeds be paid to your estate. While this does take some admin off your executor's hands, it can lead to a delay in your estate being wound up if the developer struggles to sell it. What is more, your estate will still be liable for the levies until the unit is sold.

The bottom line

As life rights grow in popularity, there is a particularly good chance you or a loved one will enter into this kind of contract. In this article we have provided a basic overview of the concept and looked at a few of the main financial considerations to consider before purchasing a life right. To ensure that your golden years are just that, I would encourage you to speak to a Certified Financial Planner® before entering a life rights contract. Making the right decision will have a lasting impact for both you and your heirs.

21.2 Various models in use in the industry

The retirement industry has developed and implemented many models with each model having its own conditions, rights, and obligations. Here are the diverse options that are currently in operation. A combination of all the options is also in use.

- A discount on the purchase price compared with a full title purchase price.
- The equivalent of the full-title price is paid.
- The purchase price is seen as a deposit and depletes over a period in full or a portion thereof. This is then the 'income' to the owner.
- The life right owner is paid back the full purchase price plus a part of the profit made on resale.
- A deferred management fee is payable on resale. This is in most cases a % of the selling price and the number of years the owner occupied the residence. The fee is payable on departure.

21.3 Rental vs Life Rights

Life rights are sometimes described as rental paid in advance. This might be a valid argument but then, the life right owner is entitled to the same benefits as the tenants. Here are some of the benefits they should enjoy:

- External maintenance of the unit and communal areas.
- Internal repairs as and when required
- Internal maintenance such as painting, and replacements caused by normal wear and tear.
- Garden services.
- All the other services enjoyed by a tenant.

21.4 Contracts

See **Chapter 2** for details of what needs to be included in a life right contract. Copy of an example of a life right contract is available form robwesseloo@mweb.co.za on request.

21.5 Financial fairness

To ensure that both the owner and the purchaser of a life right equitably dealt with, you can use two models to evaluate this fairness.

- Compare a life right purchase to a full title purchase over a period.
- Compare a life right purchase with a rental agreement over a period.

The following element and assumptions must be used in comparing a life right purchase with a full title purchase:

- Purchase price of both the life right and the full title price of the property. Square meters and market related square meter prices can be used.
- The expected period of the life right.
- How much is refunded to the life right purchaser after the period.
- Estimated Inflation.
- Expected property price inflation.
- Time value of money.
- Cost of purchasing a property and yearly maintenance cost thereof.
- Net rental income % on investment.
- Levies payable.

The full title owner and the life right owner should be in the same financial position at the end of the chosen period. The model is available at robwesseloo@mweb.co.za

The following element and assumptions must be used in comparing a life right purchase with a rental agreement:

- The rent payable of the property or similar property.
- The expected period of the life right.
- Estimated Inflation.
- Expected property price inflation.
- Time value of money.
- Levies payable.

The life right owner and the tenant should be in the same financial position at the end of the period that was chosen. The model is available at robwesseloo@mweb.co.za