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Mortgage holders need to look at insurance cover

A NEW study undertaken by Royal London has found that thousands of families who fell into arrears on their mortgage during the recession may now be underinsured on their mortgage protection policy. The leading protection specialist contends that this is potentially the case for these homeowners regardless of whether they are still in arrears or have entered into restructuring arrangements with their lender.

The impact of the recession resulted in around one-in-eight mortgage holders, at its highest in 2013, falling behind on their payments. According to the Central Bank of Ireland the current number of private dwelling houses which are classified as restructured stands at 118,477, as at December 2017.

According to Barry McCutcheon, Proposition Lead at Royal London: "Many families who were struggling to make their mortgage commitments would have entered into new agreements with lenders. We believe a significant proportion of these 100,000 plus families may not have reflected these changes in their mortgage protection cover, and therefore have become underinsured as a result.

"This means that if either of the mortgagees were to pass away, the surviving partner could be left with a shortfall on their mortgage, at a time when they can least afford it — which understandably, would be a great source of shock and worry for this person."

Royal London also says there are a number of situations where mortgage holders in arrears enter into special agreements with their banks, where it would be necessary to review or amend the mortgage protection cover in place to avoid any underinsurance.

The following, which are designed to help the homeowner stay in their home:

- Interest Only – over one year (probably beyond two years) regardless of whether the term is extended or repayments are increased in the remaining years.
- Interest Only – up to one year.
- Reduced Payment (less than interest only).
- Reduced Payment (more than interest only).
- Term Extension.
- Arrears Capitalisation.
- Payment Moratorium.
- Deferred Interest Scheme.
- Split Mortgage.

Royal London says that as mortgage protection policies generally cannot be restructured, in most cases a new policy would need to be put in place to reflect the fact that the mortgage isn't reducing or to match the revised mortgage agreement.

Barry advised: "Mortgage protection policies are a low-cost but relatively inflexible product designed to decrease in line with a typical capital and interest mortgage. But when those payments are interrupted or reduced, then there's a likelihood that a gap will grow between the outstanding mortgage including arrears and the policy cover.

"This is because the assumed capital repayments have not been made. With people so focused on getting themselves to a point where they can afford the mortgage, it's understandable if they have not thought to check whether their existing mortgage protection cover is still sufficient. Even those that have managed to get their mortgage back on track could have an issue."

Royal London looked at a couple who had taken out a €300,000 mortgage for 30 years in 2004, the couple also took out the equivalent amount of mortgage protection. In 2014 their bank agreed to switch them to interest only for four years and they then return to full repayment in 2018. Should either pass away the individual left behind would currently have a shortfall of €11,569 — that being the difference between what they owe and what a typical mortgage protection policy would cover.

When the interest only period ends, the lender will re-establish repayments in one of two ways. They may extend the term sufficiently to ensure that if the homeowner resumes the monthly repayments at the original amount the loan will clear, usually after an extra couple of years. Or they can increase the regular repayment amount so that the arrears are repaid over the original mortgage term. Either way, there's likely to be a shortfall. The higher the repayment, the quicker the shortfall may reduce.