

How to know when downsizing your home makes sense

You can use the equity for re-investing or purchases

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Source: The Kingsley Family

Brad and Karla Kingsley, who recently downsized from a large, waterfront home in South Carolina to a townhouse in preparation for retirement

Brad Kingsley downsized his \$1 million-plus waterfront home in Mount Pleasant, South Carolina, using most of the \$350,000 he had in equity to pay cash for a townhouse 3 miles away.

"We knew that paying [the house] off wasn't going to be a good use of that much cash," said Kingsley, a financial coach at [MaximizeYourMoney.com](#). "But we now have much less work to do in maintaining the house, and we can do some traveling if we want to and not worry about anything."

While purchasing a smaller residence can be a great way to lower monthly costs, it may not be the most economical option for everyone.

About 49 percent of pre-retirees didn't downsize in their last move, according to a [joint survey](#) by Merrill Lynch and Age Wave, with 30 percent of retirees actually buying bigger homes in retirement.

Those who said they wanted bigger properties cited more room for family members to visit and a more desirable home, which they could not afford earlier in life, the survey found.

When to stay put

"Typically the general rule [in retirement] is not to treat home ownership as an investment," said Pete Lang, a retirement, investment and tax advisor and founder and president of Lang Capital in Fort Mill, South Carolina. "It's better viewed as a living expense."

That means it's important to look at the monthly net cost of housing rather than size alone.

"For instance, you may have a couple who live in a rural area with a five-bedroom home who decides to downsize to a two-bedroom condo in the city. It is very possible that it would cost more, ... and may have additional costs such as condo fees," said DeDe M. Jones, a managing director of Innovative Financial in Lakewood, Colorado.

The high costs of housing in markets like California or Connecticut consume as much of 25 percent of retirees' income, said Jonathan Smoke, chief economist for [Realtor.com](#), which analyzed searches of listed properties by 65- to 74-year-olds.

Downsizing provides less opportunity in low-cost areas, especially in the Midwest, South and many areas of the Northeast. In those areas home prices, taxes and insurance tend to be lower, so retirees won't see any financial gains from moving, Smoke said.

For others, there are considerations about estate planning and capital gains.

"A large capital gain might negate the benefit of a downsize," said Jim Ciprich, a Morristown, New Jersey-based wealth advisor for Regent Atlantic.

For example, a couple who bought their home in 1970 for \$80,000 that is now worth \$800,000 could be subject to a big [capital gains tax on the proceeds](#). The IRS excludes capital gains of \$250,000 for an individual or \$500,000 if married and filing jointly. Anything above that amount is subject to a 15 percent capital gains tax. If a couple already has over \$466,950 in ordinary income in the year they sold their home, they are subject to a 20 percent tax.

For that reason, if a retiree plans to pass down the property, it may be better to have the gain stepped up at death depending on the age of the retiree.

Determine whether to stay with a few changes

Aging in place can be viable, even if modifications need to be made. Such improvements can be cheaper than moving into a new home, said David Rae, a Los Angeles-based financial planner and author of FinancialPlannerLA.com.

For example, the national average cost of building a wheelchair ramp is approximately \$1,500, while the average cost to install an elevator was about \$5,300, according to HomeAdvisor.com, which helps homeowners find qualified contractors.

Because of rising home prices in her Maryland neighborhood, Greta Mosher, 60, could not buy a smaller home nearby free and clear from the proceeds of her current one. She has a lower monthly housing liability now than she would if she took a small mortgage on a new place. So instead of moving, she is exploring adding a first-floor master suite or carriage house to her home to make it easier to live in as she and her husband get older.

"The cost of selling is high. Moving is not cheap," she said. "We might as well stay."

"It's more about rightsizing rather than downsizing," said Rae. "People often like where they live, and want to find ways to stay there."

Take the emotion out of the downsizing decision

Of those who didn't plan to move, 54 percent of those surveyed by Merrill Lynch said it's because they love their home.

"The reasons most empty nesters are reluctant to downsize tend to be emotional ones. They feel comfortable there, it's where their children grew up, it's their home," said Brian Davis, a real estate blogger at SparkRental.com and former vice president of ezlandlordforms.com, but the decision is better made based on financial and health reasons.

"There is the age-appropriateness of the property itself. Older adults are better off moving to a single-story home while they are perfectly healthy, before stairs begin to pose a risk," he said.

Staying in a house with more maintenance than you can handle can cause its value to decline, Davis said.

A [Voya Financial survey](#) suggests many retirees understand the financially practical reasons for downsizing, with 39 percent of respondents saying they had adjusted or would adjust what they spend on housing in retirement. Of this group, 27 percent selected scaling down to a more cost-effective home.

If a retiree sells and buys another home for half the price, he or she could invest the proceeds, Lang said. Those gains could be re-invested. This takes a big portion of your housing expense out of the liability column of your balance sheet and into the income column, though some retirees may have to move away from their current location to achieve that.

"If it's a larger, more expensive home, there will be greater expenses that will be a bigger drain on your savings," Lang said. "If you have to sell it in the future, will you be able to sell it?"

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