3 Reasons Why Renting Can Be Smarter Than Owning a Home in Retirement

If you're nearing retirement, it's likely that renting is a distant memory. But if your retirement plan includes making a move, renting might be a sweeter financial and lifestyle fit.

Among households with someone at least 65 years old, 8 in 10 are homeowners, according to Harvard's Joint Center for Housing Studies. Yet retirement sometimes calls for flexibility, whether that's the ability to downsize in your current location, relocate to be closer to the kids and grandkids, or chase better weather and/or a lower cost of living in another state. And these moves become harder if they necessitate putting your home on the market.

Use Your Gains to Stretch Your Retirement Savings

While homeownership is the dominant housing choice, more seniors are renting today. An analysis of government data by RENTcafe reports that the percentage of renters at least 60 years old increased more than 40% in the 10 years through 2017. That exceeded the 31% growth rate for homeowners of the same age**.** And some big cities saw more than double the average renter gain: renters ages 60+ rose more than 80% over the decade in Austin, Phoenix, Fort Worth, and Jacksonville.

If the cost of renting is lower than your annual housing costs, that's obviously a financial win. (Factor a 3% annual rent increase into your calculations.) Moreover, if you have a boatload of equity in the home, selling today and renting means you could pile your gains from the sale into your pot of retirement savings. The profit from the sale can make it easier to delay starting Social Security until age 70 to lock in the highest possible benefit.

The first $250,000 in capital gains from the sale of a home you have lived in for at least two of the past five years is tax free. (The capital gains exclusion is $500,000 for married couples filing a joint tax return). Even better, your cost-basis can be increased by the value of capital improvements you made to the house.

“When someone wants to retire and is on the edge of not being able to have the lifestyle they want or fears running out of money in their 90’s, I recommend they consider renting,” says Maria Erickson, a certified financial planner in St. Petersburg, Florida.

Erickson says selling sooner rather than later may be smart, given we’re long into an economic recovery that has lifted real estate markets in most parts of the country. “In a recession, your home value can go down, and selling becomes harder.”

Don’t Underestimate the Cost of Home Ownership

If you’re thinking about selling your home and buying another, make sure you’re realistic about the costs involved. Plan to own without a mortgage? Great, but remember you’ve still got property tax, maintenance and insurance to contend with.

“When people come to me with a budget, the number one missing item is home maintenance,” says John Crumrine, a certified financial planner based in Shallote, N.C. He says clients lose track of how much they spend on this because it’s not a fixed monthly outlay. He advises budgeting 1% to 2% of your home’s value for annual maintenance costs, and adjusting it for inflation.

Moreover, you may find that home projects and chores that are DIY today—garden and lawn maintenance, swapping the storm windows in and out, gutter cleaning etc. – may become difficult down the line. Hiring help for those chores will add to your ownership expense.

Carefully consider the rising cost of property tax if you live in an area where property values tend to increase at a strong pace. You should also review your 2018 federal tax bill. That was the first year the $10,000 limit on state and local tax (SALT) deductions –which includes your property tax tab – was in play. If the limited SALT deduction caused your bill to rise, and you are concerned about that cost in retirement, selling and renting may improve your after-tax cash flow.

Homeowner's insurance can also become a rising cost. Erickson says in Florida, climate change and the potential impact on homeowner's and flood insurance is increasingly on the radar of her retiree clients.

Another red flag for those considering a new home purchase in retirement is if you will need a sizable mortgage. Crumrine says if you have plenty of guaranteed income –Social Security, a pension, perhaps an annuity—he doesn't have a problem with retirees carrying a mortgage. But that presumes you make a down payment of at least 20% to 30%. A reality of retirement is that you may find yourself needing to move unexpectedly at some point due to changing health. "A down payment of 5% or 10% is a red flag," he says.

If you have to sell soon after buying, or during a period when home values are down, there's a chance the sale price will not cover repaying the mortgage balance and the typical 5% to 6% sales commission to your real estate agent. "The worst situation is if you have to sell sooner than expected and need to bring money to the closing." There's less of a chance of that happening if you put at least 20% down.

And if you've been mortgage free for a few years, you might not be aware of new developments: chances are that if you take out a new loan, you won't be able to claim the mortgage interest deduction. That's because new tax law that went into effect on 2018 returns raises the standard deduction to $24,400 in 2019 for married couples filing a joint tax return ($12,200 for single filers). Unless your mortgage interest and other deductible expenses such as charitable donations are more than those limits, it won't make sense to itemize.

Appreciate the Beauty of a Low-Maintenance Lifestyle

"There is a beauty to living in a rental and sending the landlord a text when something needs to be replaced or repaired, says Beth Agnello, a financial planner in the Winston-Salem, N.C. area. "The older we get the better that fits in. My advice is that you don't want to have this huge commitment to a home unless you've decided it really rings your bell."

That can be especially true for single homeowners who don't have a partner to share the work it takes to maintain a home. (Married couples should give careful thought to how the surviving spouse will fare as a solo homeowner.)

Renting allows you to test-drive your retirement life. Agnello says clients put a lot of time and effort into saving for retirement, but haven't really planned what the day-to-day of living in retirement will look and feel like. Even if you're thinking of downsizing in the same area, renting gives you time to get acquainted with your retirement self. "This is a wonderful time to have flexibility. And flexibility means cash. Cash gives us the flexibility to change our minds," says Agnello.

You can also test drive a new area. Whether you're heading to your dream retirement location, or making a big switch from city to country or vice versa, don't overcommit at first, Crumrine says. "I see people who retire, buy a house on the beach and then a year later realize they would rather be at the next beach up the coast. But they are locked in."

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