

**“Every Mortgage
Payment Added to
Your Equity”**

**“YOUR HOME IS A
GIANT PIGGY BANK”**



Reverse Mortgages

Dangerous to your health?

The pit-falls and how to avoid them

Bob Adams, Director **InvestEd** Inc.
Associate Director, Puget Sound Chapter, BI
bob.at.seattle@gmail.com

www.bob-adams.net

Copyright 2010 Bob Adams

References

Updated handout available:
www.bob-adams.net

- *Consumer Reports* article September 2009
 - Reversals of fortune
 - *The next financial fiasco? It could be reverse mortgages.*
<http://tinyurl.com/CR-reverse-mortgages>
- Center for Retirement Research at Boston College
www.crr.bc.edu
- National Consumer Law Center (Article at end of handout)
www.nclc.org
- AARP
www.tinyurl.com/28FRFBR
~~http://www.aarp.org/aarp/broadcast/reverse_mortgage_inside_c_street~~

References:

Slide not in handout

- AARP: www.tinyurl.com/28FRFBR

in the SPOTLIGHT



A Reverse Mortgage for Less

The FHA's new HECM Saver program charges lower upfront fees. [Read](#)



Reverse Mortgage Alternatives

Explore all of your options before resorting to a costly reverse mortgage. [Read](#)



An Escape Route From Foreclosure

If you struggle to make your monthly mortgage payment, a reverse mortgage could be the solution to holding on to your home. [Read](#)

Borrowing Against Your Home

Download this consumer guide that explains reverse mortgages. Adobe Acrobat required. [Do](#)

Reverse mortgages

- The next financial fiasco?
- The sequel to the sub-prime mess?
- It could be reverse mortgages
 - A new kind of debt
 - Lenders shoulder almost no risk
 - Taxpayers are being tapped to subsidize the risk
 - Federal Insurance fund payout quadrupled in four years
- Baby boomers are prime targets
 - Haven't saved for retirement
 - At retirement age

Reverse mortgages

“While reverse mortgages can provide real benefit, they also have some of the same characteristics as the riskiest types of subprime mortgages—and that should set off alarm bells.”

John Dugan

Office of the Comptroller of the Currency

But there is Federal Insurance

- Pays when a loan goes into foreclosure
- Borrower fails to pay taxes
- Borrower fails to pay home insurance
- If proceeds don't cover balance owed
- When mortgage reaches 98% of loan limit
 - Limit is set at time of loan approval
 - FHA pays lender 98% of loan and is responsible for servicing loan while borrower lives at property (lender has no more responsibility)
 - Cost of this provision won't be known until property sold

But there is Federal Insurance

- Who pays for federal insurance?
 - Borrowers – premium added to mortgage total
 - Premium – up to \$6,000
 - Plus – 0.5% of principal each year
 - Plus the interest on total mortgage
- Does not protect home owner
- Only protects lender—paid for by owner

What are Reverse Mortgages?

- Loans against the equity in your home
- Borrowers make no monthly payments
- Can receive lump sum, monthly payments, or a credit line (It is a loan)
- No income or credit qualifications
 - Low-income seniors may qualify
- Borrower must:
 - Keep home in good repair
 - Pay property taxes and insurance

The good?

- Anyone 62 or over qualifies
- Can tap the equity in their home
 - No restrictions on the use of the money
- Any existing mortgage is paid off
- Loan is repaid when last borrower dies or moves – (Loan is immediately due)
 - What if market value is less than loan value?
 - Federal insurance makes lender whole

The not so good:

- Typical fees on \$300,000 home:
 - \$15,000 up front costs
 - Insurance premiums, broker fees, closing costs
 - \$15,000 long term costs
 - Insurance premiums, broker fees over life of loan
 - Added to loan value—interest paid on loan total

- Total expenses:
 - \$30,000 over life of loan
 - (1/6th amount borrowed)

The not so good: (continued)

- Interest rates are adjustable—monthly
 - Can increase 10% over life of loan
- Fees are folded into loan at the start
 - Interest is therefore paid on loan + fees, etc.
 - Origination fee
 - Mortgage insurance premium
 - Closing costs
 - Monthly service fee
 - (Next—example from AARP)

The not so good: (continued)

Slide not in handout

HECM Loan Costs at Life Expectancy for a 75-Year-Old Borrower in a \$250,000 Home

Total Amount Borrowed	\$67,742
Loan Costs	(12 year life expectancy)
Upfront Costs	\$12,000
Total Monthly MIPs	\$7,933
Total Monthly Servicing Fees	\$5,040
Total Monthly Interest Charges	\$111,056
Total Loan Costs	\$136,029
Total Amount Owed (Loan Balance)	\$203,771

The not so good: (continued)

- More complex than most home equity loans
 - Example: must not only understand complicated budget projections, but also make predictions as to his or her future financial needs
- Some brokers push costly long-term annuities
 - Big fees paid to broker
 - Can tie up retirement savings for years
- Counseling is a required part of the application process (not always free) (800) 569-4287
 - HUD approved counselors at 1-888-466-3487
 - <http://www.hud.gov/offices/hsg/sfh/hecm/hecm1ist.cfm>

The not so good: (continued)

- May have impact on a senior homeowner's eligibility for need-based government benefits programs
 - Supplemental Social Security (SSI) and Medicaid
- Payments should be spent during the month in which they are received (spend it first)
 - Payment can be considered "income," and count toward the resource limit under these programs

The demographics

- Since 1990 FHA has backed >500,000 Reverse Mtg.
 - Growth expected to continue
 - About 10,000 Baby boomers turn 62 each day
 - An alluring target
- This year (2010) 50 Mil boomers will be over 62
 - Qualified for reverse mortgages
 - Their historic saving rate—near zero
 - How will they retire?
- 80% own their own homes
 - Estimated equity: \$4 Trillion
 - Huge target

The ads:

- "Every mortgage payment added to your Equity!"
- "Your home is a giant piggy bank"
- "Use the money for anything you want"
- Pay off debts with tax free income"
- "Your family will still inherit your home"
- "Wake up to a whole new life"
- "Travel, or Do Something Special"
- "The loan is guaranteed by the government"

Reverse mortgages

- “These loans should be used as a last resort, not a first resort”

David Cotney COO Massachusetts Division of Banks

- “To use the equity in their home like an ATM or credit card is a recipe for disaster”

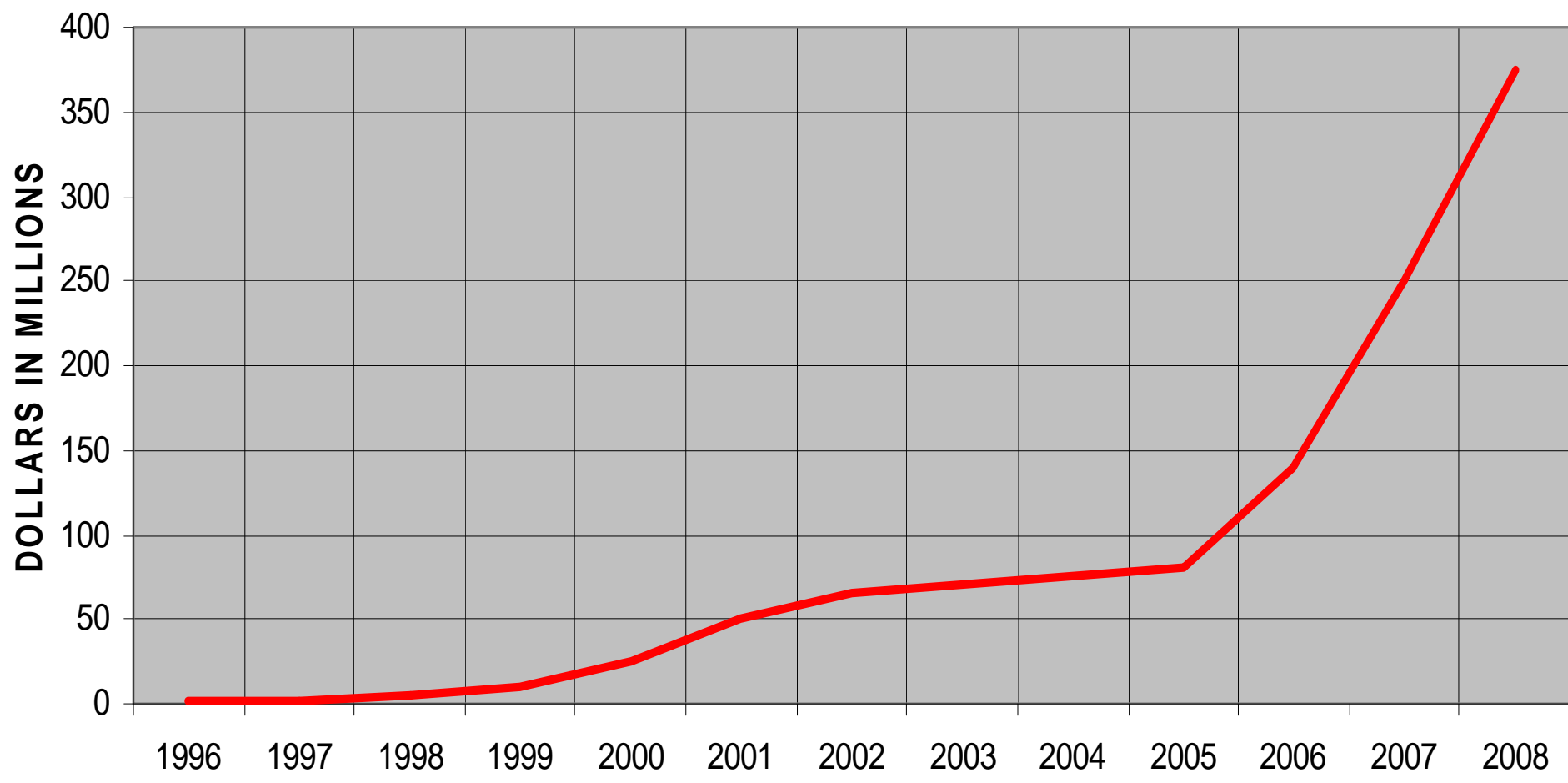
Chuck Gross, Conference of State Bank Supervisors

The Gotchas...for lenders

- Virtually none
- If borrow fails to pay taxes
 - FHA pays
- If borrow fails to maintain insurance & suffers loss
 - FHA pays
- If proceeds from sale doesn't cover balance owed
 - FHA pays
- Mortgage reaches loan's maximum lending limit
(equity is exhausted & borrower is still living)
 - FHA pays

Rising tide of mortgage claims

1996—2008



Bailing out the lender—guaranteed by tax dollars

Need cash—try other resources first

- For help:
 - Look for government & non-profit assistance
 - Property tax relief programs
 - Utility discounts
 - Fuel assistance programs
 - Energy efficiency programs
 - Energy efficient appliances, windows, insulation
 - Most states will match seniors with agencies
 - Check out: www.benefitscheckup.org

Need cash—try other resources first

- Draw money from other assets first
- Check for a real estate tax abatement program
- Consider home equity loan or credit line
 - Closing costs are a fraction of reverse mtg.
- Can't make payments?
 - Sell your home
 - Bank any remaining equity

Beware:

- Seniors with large equities are targets
- Never put your home in one spouse's name
- Beware of sales people's promises
 - Insurance sales people enticed to sell Rev. Mtgs.
 - "Cross-selling"
 - "We have loan originators making between \$25,000 to 50,000 a month."
 - There are no caps on fees on Cross-selling

Gotchas...for borrowers

- High fees
- Sales people with conflict of interest
- Don't be enticed to use money to buy annuities
 - Tie up money & pay very low return
 - Sales person collects sales fee
- Must act NOW!
 - Walk away

Why Reverse Mortgages?

- Need money to live on
- Exhausted all other money sources

- Use only late in life and if absolutely necessary—at least in your 70s or 80s
 - Interest rates are high
 - Fees are high
 - Proceeds are low

Counseling is not adequate

- Counseling is required for seniors
 - Government Accountability Office study:
 - 14 of 15 cases—not adequate counseling
 - 7 cases alternative funding not discussed
 - At least 5 HUD approved counseling agencies must be provided— 1 within reasonable driving distance
 - 5 additional that provide phone counseling
 - Counseling not required to be free
- Recommendation: Meet face-to-face with counselor

HUD Counseling guidelines

- Use Certified Counselor
 - Beware if they also sell reverse mortgages
- Counselors must:
 - Review borrower's finances
 - Document a budget based on expenses, income, total assets, debt
 - Discuss appropriate alternative to reverse mtg.
 - Discuss alternatives

Is a Reverse Mortgage for you?

- Need money to live on
- Exhaust all other money sources first
- Participate in counseling
- Be aware of costs
- Your heirs may receive nothing

- Recommendations:
 - Do not remove a name from ownership of home
 - Do not use proceeds to buy insurance, annuities or other forms of investments

5 Questions to Ask

1. Do you really need a reverse mortgage?
2. Can you afford a reverse mortgage?
 - ✓ Can be especially costly if you move in just a few years
3. Can you afford to start using up your home equity now?
4. Do you have less costly options?
 - ✓ Home equity loan or home equity line-of-credit
 - ✓ Sell and move to a less costly home
5. Do you fully understand how these loans work?
 - ✓ The risks to borrowers are unique

Is a Reverse Mortgage for you?

The final word:

- While they can be a tremendous benefit, reverse mortgages are not for everyone. They are expensive, particularly in the short run. Older homeowners should be encouraged to explore alternatives such as property tax credit and abatement, and eligibility for other programs. Those who wish to leave their property to their heirs may not want to deplete their equity. Sound, in-depth counseling on these issues is essential, and is required by the HUD program, and some state laws.

Is a Reverse Mortgage for you?

The final word:

- While they can be a tremendous benefit, reverse mortgages are not for everyone. They are expensive, particularly in the short run. Older homeowners should be encouraged to explore alternatives such as property tax abatement, and eligibility for other programs. Those who wish to leave their property to their heirs may not want to deplete their equity. Sound, in-depth counseling on these issues is essential, and is required by the HUD program, and some state laws.

Any Questions?