Assessing Reverse Mortgages as a Viable Retirement Security Alternative

Holly Bedwell
Margaret Carden
Nicole Kibble
Sean Stalpes

Workshop in Public Affairs
Spring 2009

Robert M. La Follette School of Public Affairs
University of Wisconsin-Madison

For additional copies:
Publications Office
La Follette School of Public Affairs
1225 Observatory Drive, Madison, WI 53706
www.lafollette.wisc.edu/publications/workshops.html
publications@lafollette.wisc.edu

Table of Contents

List of Tables and Figures

Foreword

Students enrolled in the Workshop in Public Affairs at the Robert M. La Follette School of Public Affairs, University of Wisconsin–Madison, prepared this report for the Chicago office of the U.S. Government Accountability Office.

The report examines the history, key features and the financial advantages and costs of reverse mortgages, specifically of home equity conversion mortgages (HECM). Reverse mortgages provide a means for seniors to access otherwise illiquid housing equity without selling their homes. Loans based on a share of housing equity are made available to homeowners with payback required only upon the sale of the house, which may not be until after the death of the owner. HECMs are reverse mortgages that insure lenders against the loan exceeding the value of the house when sold and borrowers against the lender defaulting on promised payments. The authors document the rapid growth in reverse mortgages as a result of the availability of HECMs and discuss how recent changes in housing prices and interest rates may affect the liability of lenders, borrowers and the U.S. Department of Housing and Urban Development (HUD), which offers the insurance component of HECMs. The authors conclude that reverse mortgages may grow in importance as a source of retirement income for the larger, and less debt adverse, baby boom cohort. They conclude that better data are needed to understand who holds reverse mortgages and for how long. They further conclude that understanding how demographic trends and recent housing price changes influence the demand for reverse mortgages and HUD liabilities is an important issue for GAO to examine.

The authors' training is part of the La Follette School of Public Affairs' two-year graduate program that leads to a master's degree in public affairs. Students study policy analysis and public management, and they pursue a concentration in a public policy area of their choice. They spend the first year and a half taking courses that provide them with the tools they need to analyze public policies. Although acquiring a set of policy analysis skills is important, there is no substitute for doing policy analysis as a means of learning the craft. Public Affairs 869, the Workshop in Public Affairs required in the program's final semester, provides graduate students that opportunity. While improving their policy analysis skills, they collaborate to contribute to the capacity of public agencies to analyze and develop policies on issues of concern to Wisconsin residents.

The students in this workshop were assigned to one of three teams. One group worked on this report, while the others collaborated with the Wisconsin Department of Children and Families and the Wisconsin Department of Health Services.

Michael Hartnett and Sharon Hermes in the Chicago GAO office first suggested this topic and were consistently available to the students throughout the semester. I am very grateful for their enthusiasm in working with the La Follette School of Public Affairs to offer this experience to its students. This report would not have been possible without their assistance. The acknowledgments section thanks other individuals who supported the students as they pursued data and policy insights. I add my gratitude to the appreciation expressed there.

The conclusions herein are those of the authors alone. The topic they address is large and complex, and this report can only add insight from an analysis that is necessarily constrained by the semester time frame. Nevertheless, much has been accomplished, and I trust this will be useful as GAO considers issues of retirement income security.

The report also benefited greatly from the support of faculty and the staff of the La Follette School of Public Affairs, especially that of Publications Director Karen Faster, who edited and managed production of the report. A University of Wisconsin–Madison Division of Information Technology Engage grant supported the travel and other additional costs necessitated by collaborative work over time and distance.

Karen Holden
May 2009

Acknowledgments

The authors would like to thank the U.S. Government Accountability Office in Chicago, particularly Michael Hartnett and Sharon Hermes, for providing us with guidance and support throughout the process of creating this report. The authors would also like to thank J. Michael Collins at the University of Wisconsin–Madison and Chris Herbert at Abt Associates for taking the time to speak with us and help guide our research. Finally, the authors would like to thank Karen Holden and Karen Faster at the La Follette School of Public Affairs for their efforts in editing the content and format of this report.

Results in Brief

Reverse mortgages were developed for use as an income security alternative during retirement. They allow seniors to convert their home equity into cash income. Three major types of reverse mortgages exist today: home equity conversion mortgages (HECM), proprietary reverse mortgages (commonly known as jumbo reverse mortgages), and single-purpose reverse mortgages. HECMs make up more than 90 percent of the reverse mortgage market and are the primary focus of this report.

As the number of HECM loan originations grows, the various risks that HECMs present to borrowers, lenders, and the government must be recognized. These risks include the uncertainty of life expectancies, changing interest rates and housing values, and the financial stability of the lender. The HECM program alleviates these risks by creating a secondary market in which the U.S. Department of Housing and Urban Development (HUD) insures many of the uncertainties associated with reverse mortgages, primarily problems that occur when the loan balance exceeds the property value (crossover risk). However, while HECM originations have continued to grow during the economic recession, so too has HUD's short-term liability to insure crossover.

Federal safeguards have been established specifically to protect borrowers. Borrowers, who must be 62 and older, represent a group more likely to be targets of predatory lending. As a result, borrower protections include a heavy emphasis on counseling to ensure borrowers are well informed of the unfamiliar calculations, rules, and regulations of HECMs.

Borrowers of HECMs have become younger and wealthier. The majority of borrowers choose to receive reverse mortgage payments as lines of credit. In contrast to regular monthly payments, a line of credit allows for immediate withdrawals to pay off existing mortgages with the remaining line preserved for expenses. Changes in borrower characteristics should be analyzed for their effect on public policy, particularly for HUD liabilities and the appropriateness of lines of credit for longer term income security.

This assessment of reverse mortgages provides the U.S. Government Accountability Office with a picture of the state of reverse mortgages from multiple perspectives: borrowers, lenders, and the government. We conclude that reverse mortgages represent a viable retirement security alternative, as long as borrowers are willing to incur the high upfront costs, and rules and regulations are enforced. This conclusion rests on two assumptions: that borrowers will be well-informed about these costs and that housing prices will recover from recent declines. Better data collection on the experiences of borrowers and new data on borrower outcomes as loans terminate will provide further clarity. Monitoring the evolving secondary market will be necessary to evaluate emerging products to determine their effect on reducing upfront costs and other consequences. Finally, the economic recession and the housing market decline will create a new landscape, one that needs to be evaluated in terms of risk to HUD and how borrowers may be affected.

Background and History

While housing is an asset held by more than 80 percent of the near-elderly and accounts for about 40 percent of net worth, this equity is not easily accessible as a source of income after retirement.[1] Housing equity value has gained increased attention with the recent economic crisis and housing market collapse. The erosion of Americans' retirement security and the approaching retirement of the large baby boomer cohort make it important to explore income alternatives for retirement security. As a relatively new mortgage product, reverse mortgages present somewhat unknown risks and benefits to seniors.

Reverse mortgages allow elderly American homeowners to remain in their homes and tap into their home equity to receive cash payments from lenders. Reverse mortgages are the opposite of traditional forward mortgages in that the borrower receives payments from the lender instead of making payments. A reverse mortgage borrower's equity decreases over time, while the loan balance rises as the lender makes cash payments to the borrower. Interest on the increasing loan amount is added to the outstanding balance. Hence, reverse mortgages are considered "rising debt, falling equity" transactions.

The development of "reverse mortgages" as a tool to enable seniors to use home equity for cash began in the 1970s. The first programs were sales-leaseback transactions, in which a property was sold to a new owner, who simultaneously leased the property back to the seller, who became a renter of the home he or she had owned.[2] However, only a few loans of this type were made, and the transactions had the disadvantage of being complicated and costly to negotiate.

The reverse annuity mortgage was another option made available during the 1970s. Under this plan, home equity was used to secure a loan used to purchase an annuity that provided the borrower with monthly income less the mortgage interest charged on the loan. During the borrower's lifetime, only the interest on the loan needed to be paid.[3] Repayment of the loan principal was not required until the death of the owner, the sale of the property, or a prescribed date.[4]

Reverse annuity mortgages carried some of the risks that reverse mortgages have since attempted to mitigate. Fluctuating market interest rates on the borrowed amount was a major risk, because the borrower could end up owing the lender more than the amount of the annuity payment if interest rates increased during the life of the loan. This would defeat the borrower's purpose of taking out a reverse

---

1 Coronado, Maki, & Weitzer, 2007.
2 Congressional Research Service (CRS), 2008.
3 An annuity is purchased with the loan proceeds, and then the borrower receives a monthly income, less mortgage interest.
4 CRS, 2008.

annuity mortgage. Even small increases in interest rates could seriously erode the net value of the annuity payments.

Uncertain mortality also presented risk for borrowers and lenders. Borrowers who died soon after taking reverse annuity mortgages would have incurred high upfront costs but only a small number of monthly annuity payments. To insure against this possibility, borrowers could purchase a 10-year certain annuity option. This option continued monthly payments for 10 years after the reverse annuity mortgage was issued. Payments would be made to the borrower during her or his lifetime or to the borrower’s estate for the remainder of the 10-year period, if the borrower did not survive the full 10 years. The lender faced the risk that total payments to the borrower could exceed the home’s equity if the borrower lived longer than expected. By the beginning of the 1980s, while it was recognized that a reverse mortgage was a very innovative tool for seniors to access home equity, risks to lenders and borrowers needed to be addressed for the product to become more useful and widely used.

What Are the Various Types of Reverse Mortgages?

There are three major reverse mortgage products:

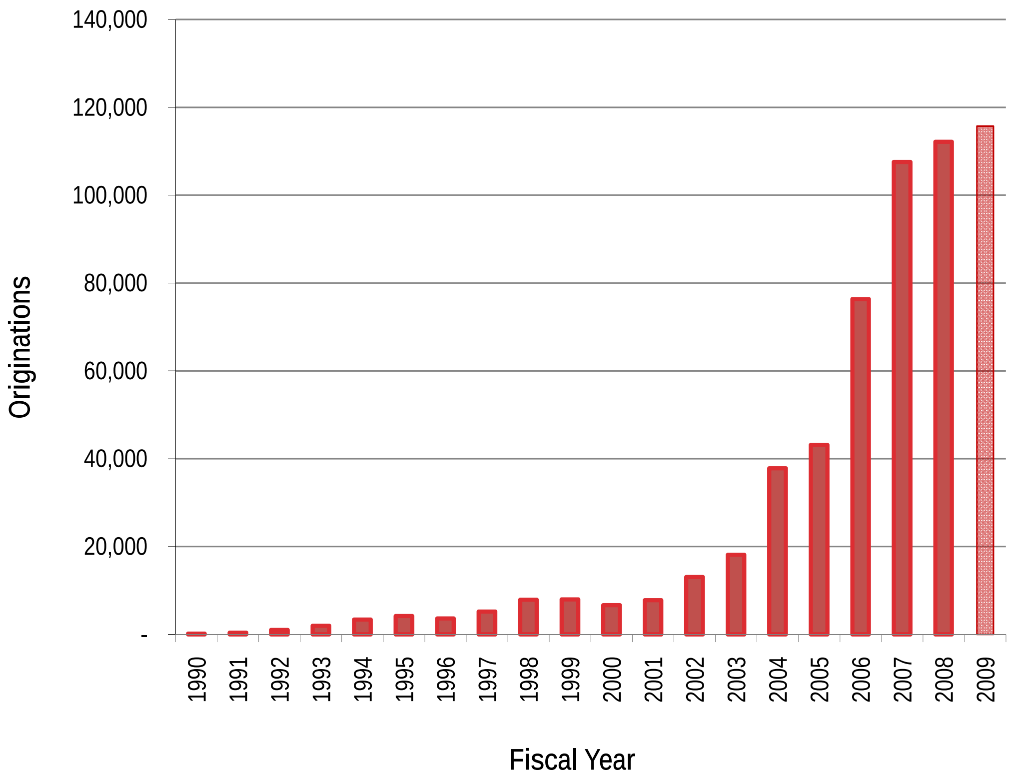
- Home equity conversion mortgages (HECMs), which are federally insured reverse mortgages, backed by the U.S. Department of Housing and Urban Development (HUD);
- proprietary reverse mortgages, which are private loans backed only by the companies that develop them;
- single-purpose reverse mortgages, which are offered by some state and local government agencies and nonprofit organizations.

HECM program

With the passage of the Housing and Community Development Act of 1987, the federal government became directly involved in the reverse mortgage market. This act authorized the Home Equity Conversion Mortgage Program as a demonstration. The HECM program was the first nationwide reverse mortgage program to offer the assurance of lifetime occupancy to elderly homeowners through a federally guaranteed loan. The U.S. Department of Housing and Urban Development (HUD) guaranteed lenders the agency would purchase the excess loan balance upon loan termination or if the lender could no longer finance the loan. Congress made the program permanent in 1998 and increased the number of allowable outstanding loans to 150,000 annually.[5] Growth in the HECM program was initially slow, with annual numbers of new loans remaining below 8,000 until 2002. Growth has since increased, with large gains in the last couple years. From 2006-2007, the number of approved HECM loans increased from 76,282 to 107,367, an unprecedented 42 percent increase. Figure 1 represents the growth of HECMs since their inception.

[5] Rodda et al., 2000.

Figure 1: HECM Volume (Cases Insured) by Fiscal Year



Note: Data for 2009 are projected.

Source: National Reverse Mortgage Lenders Association (NRMLA), 2009.

The key feature of the HECM program is that the Federal Housing Administration (FHA) insures the loans, mitigating much of the longevity and property value risk present in the reverse annuity mortgage program. The insurance protects lenders, in the event that the final loan balance exceeds the proceeds from the sale of a home, and borrowers, by continuing monthly payments if the lender defaults on the loan.[6] A HECM is also a non-recourse loan, meaning that a borrower can never owe more than the value of the property at the time the loan is repaid. That is, lenders cannot access the income or other assets of the borrower to recover the excess loan amount.

HECM loan borrowers may choose from five payment plans:

- Tenure: equal monthly payments as long as at least one borrower lives and continues to occupy the property as a principal residence.
- Term: equal monthly payments for a fixed period of months selected by the borrower.
- Line of credit: installments at times and in amount of borrower's choosing until the line of credit is exhausted.

[6] CRS, 2008.

- Modified tenure: combination of line of credit with monthly payments for as long as the borrower remains in the home.
- Modified term: combination of line of credit with monthly payments for a fixed period of months selected by the borrower.

All payment streams have the same present value at origination,[7] but the payment amounts are different because borrowers exhibit different age and other risk characteristics in addition to choosing different ways to access their equity. Each form of payment carries different types of uncertainty and therefore presents different advantages and disadvantages for borrowers. [8]

The line of credit option is by far the most popular reverse mortgage payment option. Eighty-seven percent of borrowers chose line of credit plans in 2007, while 4.5 percent chose modified-tenure, 3.7 percent chose tenure, 3.3 percent chose modified-term, and 1.5 percent chose term.[9]

Some reasons for the popularity of line of credit plans include:

- Ability to pay off an existing mortgage. This can be done with all types of payments, but only the line of credit offers the flexibility to receive a large initial payment, which may be needed to pay off a mortgage;
- Greater flexibility than an annuity for accessing income to deal with unexpected large expenses;
- Amount of money available to the borrower increases over time if the credit line or lump sum is left untouched.

That most borrowers select the line of credit option suggests that borrowers prefer the certainty of being able to access a line of credit when additional income in unpredictable amounts might be needed instead of supplementing their income with regular monthly payments. This contrasts with the original purpose of reverse mortgages, which were intended to function more like an annuity and provide a continuous monthly income supplement. Term payment plans are clearly the least desired by borrowers, despite the fact that monthly payments are higher with term plans than with the more back-loaded tenure plans. This suggests that most borrowers anticipate longer term or unexpected income needs that could not be met with regular monthly payments over a relatively short fixed period. It may also be that homeowners more readily understand the line of credit because of the similarity to home equity loans.[10]

---

[7] Origination is the overall administration process of setting up a mortgage, including the preparation of documents.

[8] See Appendix A for a comparison of payment options and their advantages and disadvantages.

[9] National Bureau of Economic Research (NBER), 2008.

[10] All payment options have the same net present value. Borrowers choose their payment options

The requirements of the HECM program reflect the inherent features of a reverse mortgage (and annuities that would be paid) but also the insurance features HUD provides. These requirements, which are quoted here, may be found at the HUD website. [11]

Individual requirements

- Be 62 years of age or older
- Own the property outright or have a mortgage balance small enough to be repaid by the HECM loan proceeds
- Occupy the property as a principal residence
- Not be delinquent on any federal debt
- Participate in a consumer information session given by an approved HECM counselor

Mortgage amount based on

- Age of the youngest co-borrower
- Current interest rate
- Lesser of appraised home value or the FHA HECM mortgage limit

Loan requirements

- No income or credit qualifications are required of the borrower(s)
- No repayment as long as the property is the principal residence
- Closing costs may be financed in the mortgage

Eligible property requirements

- Must meet all FHA property standards and flood requirements
- Single family home or 1-4 unit home with one unit occupied by the borrower
- HUD-approved condominium
- Manufactured home that meets FHA requirements

---

based on their needs and the features of each option.

[11] U.S. Department of Housing and Urban Development (HUD), 2009a: http://www.hud.gov/offices/hsg/ sfh/hecm/hecmabou.cfm

Calculating the HECM loan[12]

HECM loan amounts are determined by the value of the home, the age of the borrower, and the cost of the loan (fees and the interest rate). The maximum amount a borrower can receive from a reverse mortgage is termed the principal limit.[13] Calculated at the time of the loan origination, the principal limit is based on the maximum claim amount, the expected average mortgage interest rate, and the age of the youngest borrower. A principal limit factor, which adjusts for longevity and interest risk, is applied to the maximum claim amount to obtain the loan principal limit. This amount, less fees to be paid, is the net principal limit that may be borrowed.

More specifically, a maximum claim amount is the lesser of a geographically specified FHA mortgage limit or the appraised value of the home.[14] As of February 24, 2009, the FHA loan limit was $625,500.[15] Borrowers with home values exceeding the loan limit only have access to $625,500 of home equity. HUD specifies the interest rate used to calculate loan advances, and the rate varies according to the interest-adjustment the borrower chooses.[16] If choosing a fixed rate loan, which can be received only as a single lump-sum payment, the loan's accumulation rate will remain fixed at the initial interest rate through the life of the loan. For an adjustable rate loan, the interest rate at which the loan (or unused line of credit) accumulates will be adjusted over the life of the loan.[17] Once the principal limit is calculated, upfront costs that are subtracted include the origination fee, the mortgage insurance premium HUD requires for these insured loans, service fees, appraisal fees, and other closing costs. The mortgage insurance premium is a 2 percent charge on the maximum claim amount that insures against the risk (incurred by HUD) of the loan balance exceeding the home value at loan termination plus a 0.5 percent monthly charge on the loan balance. The initial principal limit minus costs yield the net principal limit, which is the amount the borrower can take as a lump-sum at closing. The net principal limit equals the maximum line of credit available at closing if the borrower pays all costs and does not choose to receive regularly scheduled monthly advances. The net principal limit also determines the tenure or term annuity amount that will be paid monthly to the borrower, if these payment options are chosen.

---

[12] The National Bureau of Economic Research (2008) gives a detailed description of the loan amount calculation and its variables on pages 8-14 of their publication.

[13] Scholen & Belling, 2006.

[14] NBER, 2008.

[15] HUD, 2009b.

[16] The expected rate is the sum of the lender's margin and the U.S. Treasury securities rate adjusted to a constant maturity of 10 years. The lender's margin is the difference between the one-year Treasury rate and the initial rate on the loan. See Appendix B for a more detailed explanation of the HECM calculation.

[17] Scholen & Belling, 2006.

HECM loans as income

A reverse mortgage allows borrowers to spend their home equity how they wish. Borrowers may choose to use their reverse mortgage payments for expenses such as health care, supplemental income, home improvements, grandchildren's college tuition, or travel.[18] Borrowers may even sell their homes, purchase less expensive primary residences, and transfer their approved HECMs to their new homes.[19] However, borrowers must be able to cover the sales price of the new home, closing costs, and HECM fees with the proceeds from their reverse mortgage.[20]

Reverse mortgage payments are not considered income for federal and state tax purposes.[21] Likewise, these payments are not considered income or earnings in determining Social Security or Medicare eligibility.[22] However, Supplemental Security Income and Medicaid recipients must spend the entire reverse mortgage payment received each month or risk having benefits from those programs reduced, under these programs' means-test provisions. If a borrower receives a lump sum payment and does not use the full amount within a month, the excess payment could be considered a countable resource and may affect Medicaid eligibility.[23]

Repaying the HECM loan

Repayment of a HECM loan is not required until the borrower dies, sells the home, or has not lived in the home as a primary residence for 12 consecutive months, including nursing home stays. Repayment of the loan may be required if the borrower fails to pay property taxes or to maintain the home.[24]

Any home equity remaining after the loan is repaid is available to the borrower (or in the case of death, as inheritance). The amount of remaining equity depends on a number of factors, including how much the loan costs, how much and when the borrower received cash payments, the interest rate charged on the accumulating loan balance, and changes in the home's value. All reverse mortgage debt must be repaid before heirs may inherit the home. Only the used portions of a line of credit and monthly annuity payments received are considered payable debt. The flexibility in withdrawal timing that a line of credit provides enables borrowers to access funds just prior to a move (or death). In some cases the remaining line of credit may be greater than the residual equity remaining

[18] NRMLA, 2006.
[19] The HECM for Purchase program was made effective in January 2009 to allow seniors to purchase a new principle residence and obtain a reverse mortgage in a single transaction.
[20] HUD, 2009c.
[21] National Reverse Mortgage Lenders Association (NRMLA), 2006.
[22] CRS, 2008.
[23] NRMLA, 2006.
[24] HUD, 2009d.

in the home if the borrower was not to use the remaining credit.[25] This added advantage of a line of credit may be another reason this payment option is the most popular among borrowers.

Misconceptions about HECM

One popular misconception is that once a borrower enters the HECM program, he or she must relinquish his or her house ownership to the lender. The borrower retains title to the house and pays back only the lesser of the loan balance or proceeds from the property sale. The borrower remains the residual claimant on the value of the property. The lender cannot evict the borrower from her or his home if the loan value exceeds the home's (or equity) value.[26]

A second misconception is that the high costs associated with HECM loans make them a "relatively bad deal for borrowers."[27] One reason a HECM costs more than a regular forward mortgage is because of the mortgage insurance premium HUD collects at origination and during the life of the loan. This provides valuable protection for the lender and the borrower against losses incurred should the loan balance exceed the property value. "Even though lenders are the direct beneficiaries of this insurance, borrowers also benefit in the form of more favorable loan terms and consumer protections," compared to the jumbo reverse mortgage described below.[28] Additionally, the insurance protects borrowers against lender default.[29]

Non-HECM options–Cash Account Jumbo Plan, Senior Equity Reverse Mortgage, single-purpose reverse mortgage

In addition to the HECM reverse mortgage, jumbo reverse mortgages, also known as proprietary reverse mortgages, are private options designed to appeal to homeowners with high home equity values. The Cash Account Jumbo Plan is available in 24 states and Washington, D.C.; and the Senior Equity Reverse Mortgage is available in Arizona, California, Delaware, Georgia, Maryland, North Carolina, South Carolina, Texas, Virginia, and Washington, D.C., through the Bank of America.[30] These plans generally tend to be similar to HECM, with some variations.

Unlike the HECM, which has no minimum limit, the Cash Account Jumbo Plan requires a minimum home value of $75,000 and does not offer borrowers the option of lifetime monthly payments. The Jumbo Plan does, however, offer a

[25] Scholen & Belling, 2006.
[26] NBER, 2008.
[27] HUD, 2008a.
[28] Ibid.
[29] NBER, 2008.
[30] CRS, 2008.

line of credit as long as the borrower lives in the home, with a 5 percent annual growth in the balance. The Jumbo Plan is marketed primarily to homeowners with property values exceeding $450,000, providing an option to borrowers with property values above the HECM loan limit. The Senior Equity Reverse Mortgage is also marketed to homeowners with high property values, and like the HECM, those payments may be dispersed in a lump sum, as monthly income, a line of credit, or any combination of those.[31]

Fannie Mae used to offer the only proprietary reverse mortgage available on a national basis, known as the Home Keeper reverse mortgage. With the passage of the Housing and Economic Recovery Act of 2008, Fannie Mae discontinued its Home Keeper product as of December 31, 2008. The legislation expanded the HECM program by increasing loan limits and authorizing their use for home purchases. As a result, Fannie Mae no longer saw a need for the Home Keeper product.[32]

Single-purpose reverse mortgage products generally have the lowest costs, but are severely limited in terms of scope and availability. These reverse mortgages are offered by state and local governments and by non-profit agencies that dictate the single purpose of their use. For example, agencies may issue these reverse mortgages only for the purpose of paying off property taxes or for making home repairs or improvements. Single-purpose reverse mortgages are also often limited to low- to moderate-income borrowers. Our reports does not discuss these in depth due to their limited availability and use, and because they do not fall under federal regulation. At present, the HECM program is by far the most popular reverse mortgage option, with private options shrinking as additional amendments make the HECM program more appealing to borrowers and protective of borrower and lender interests.

Comparison of fees of reverse mortgage options

Loan costs and payment options vary significantly among reverse mortgage products. A portion of the upfront costs of HECMs fund FHA insurance, a protection for borrowers that outlive their loan balances. In general, jumbo loans are more favorable than HECMs for borrowers who do not plan to stay in their homes for long, because of lower upfront costs and the decreased need for insurance. Due to jumbos having no home value limits, borrowers with more than $625,500 in home equity are able to access a greater proportion of their home equity. Senior equity reverse mortgages generally have lower costs, but they include stricter guidelines, such as only being able to use the payments to pay property taxes or make home repairs. They also offer payment options in the form of a monthly payment, line of credit, or a combination of the two. Table 1 compares the three major reverse mortgage products in more detail.

---

[31] CRS, 2008.
[32] Reverse Mortgage Daily, 2008.

Table 1: Comparison of Reverse Mortgage Products

	Home Equity Conversion Mortgage	Cash Account Jumbo	Senior Equity Reverse Mortgage
Minimum Home Value	Not applicable	$75,000	Not applicable
Maximum Home Value	$625,500	Not applicable	Not applicable
Payment Options	Term, tenure, line of credit, modified term, modified tenure	Line of credit	Monthly payments, lump sum, line of credit, or any combination
Minimum Withdraw	Not applicable	Borrower can draw on line of credit in full or part; minimum draw is $500	Not applicable
Availability	Nationally	24 states	10 states
Interest Rates	Monthly-adjusted = one-year Treasury rate + 1.5% Annually adjusted = one-year Treasury rate + 3.1%	Six-month London Interbank Offered Rate + 5%	Six-month London Interbank Offered Rate + 2.95%
Adjusted	Borrowers' choice – monthly or annually adjusted. Fixed rate for lump sum only	Semi-annually	Varies
Capped	Annually adjusted rates may not increase more than 2% per year or 5 percentage points over life of loan	6% above original rate	18%
Marketing	Homeowners age 62+	Home values > $450,000	"High" property values
Monthly Service Fee	$30 per month (annually adjusted interest rates), $35 per month (monthly-adjusted interest rates)	Except in Illinois and Maryland	$25 per month
Origination Fee	>$125,000 = $2,500. $125,000+ = 2% of first $200,000 + 1% over $200,000. Origination fees capped at $6,000	Standard option = 5% of first $500,000 + 1.5% of next $500,000 + 1% in excess of $1 million Zero point option = no origination fee	1% of home value, or $10,000, whichever is less
Closing Costs	Varies by home value	Capped at $3,500	Not applicable
Mortgage Insurance	2% of home value or FHA loan limit; whichever is less, + 0.5% per month of mortgage balance	Not applicable	Not applicable

Source: CRS, 2008.

Jumbos and Senior Equity Reverse Mortgages are attractive to seniors with more expensive homes because there is no maximum claim amount, whereas the HECM is capped at $625,500. However, jumbos and Senior Equity Reverse Mortgages continue to make up less and less of the reverse mortgage market for three reasons:

1. They are not government-insured, thus they are less likely to be offered by lenders. This can also make them more expensive to borrowers, as lenders often charge higher interest rates to leverage their risk.
2. Home values are declining, thus adding to lender risk.
3. There is a very small secondary market for these loans.

Trends in Reverse Mortgages: Who's Taking Them Out, Why, and Market Trends

The background section of this report has shown the growth in the number of reverse mortgage loan originations. However, several other important trends should be discussed when examining reverse mortgages. The first part of this section reviews who takes out reverse mortgages and how characteristics of these individuals have changed in the past two decades. We next use data from the AARP National Survey of Reverse Mortgage Shoppers to examine the reasons households choose reverse mortgages and what barriers caused them not to choose one. Finally, we look at the most recent years of growth in the reverse mortgage market and explore how the recent declines in housing prices and economic conditions may affect that continued growth.

Who is taking out reverse mortgages?

During the past two decades, the mean characteristics of reverse mortgage borrowers have changed. HUD data indicates that borrowers have become younger. The average age of borrowers has decreased from 76.6 years in the early 1990s to 73.5 years in 2007.[33] During the same time period, the proportion of single female borrowers has declined from 57 percent to 45 percent, and the proportion of couples has increased from 28 percent to 37 percent.[34] Borrowers also have greater home values, with the average home value in the HECM program increasing from $121,300 to $261,900. Changes in borrower characteristics can be ascribed in part to the federal government raising the FHA loan limits. This allows for higher loan limits paid over borrowers' longer lives.[35]

The population eligible for reverse mortgages will continue to grow as the baby boom cohort enters and moves through retirement. The baby boom cohort is larger than its predecessor cohort, potentially less averse to acquiring and holding debt, and therefore, is expected to be more willing to use reverse mortgages (that is, borrow against their equity) to supplement their retirement income.[36] As borrower characteristics change, we can expect that the reasons for using reverse mortgages also change; this is explored next.

[33] AARP Public Policy Institute, 2007.
[34] Ibid.
[35] HUD, 2009b.
[36] HUD, 2008a.

Why choose a reverse mortgage?

Although reverse mortgages provide an innovative way to access seniors' most valuable asset, only a small percentage of older households have taken advantage of this opportunity. According to an AARP study using HUD and U.S. Census Bureau data, in 2006, about 1 percent of the 30.8 million eligible households held reverse mortgages, with 0.9 percent being federally insured reverse mortgages.[37] The low rate of lending and the lack of knowledge regarding why consumers do and do not choose reverse mortgages led AARP to conduct a survey of reverse mortgage shoppers in 2006 and national opinion surveys regarding reverse mortgages in 1999 and 2007.[38]

The 2006 AARP survey investigated why borrowers applied for and how they used reverse mortgages. Table 2 presents results from the AARP survey on the reasons borrowers and non-borrowers explored reverse mortgages, and the main ways in which borrowers spent those funds. For those who explored reverse mortgages, those who decided to borrow and those who did not, the primary reasons for seeking this loan included paying off an existing mortgage on the home, improving their quality of life, paying everyday expenses, and making home repairs or improvements. Among those who actually took out reverse mortgages, 19 percent used the loan to pay off an existing mortgage, 18 percent made home repairs or improvements, 14 percent improved their quality of life, and 10 percent used proceeds for everyday expenses.

[37] AARP Public Policy Institute, 2007.
[38] Ibid.

Table 2: Reasons for Looking into Reverse Mortgages and Main Uses by Borrowers

	A Reason for Looking into a Reverse Mortgage		Main Reason for Looking (n = 946)	Main Use by Borrowers (n = 946)
	Borrowers (n = 946)	Non-borrowers (n = 563)		
Pay off mortgage	40%	40%	19%	19%
Home repairs/ improvements	47%	43%	14%	18%
Improve quality of life	73%	68%	18%	14%
Everyday expenses	50%*	40%	9%	10%
Emergencies/ unexpected	78%*	66%	13%	9%
Pay off non-mortgage debt	28%	27%	6%	7%
Health or disability	28%*	21%	7%	5%
Property taxes or insurance	29%*	21%	4%	5%
Financial help to family	15%	13%	2%	2%
Investments, annuities, or long-term care insurance	13%	17%	2%	1%
Household chores	18%	19%	1%	1%

* Statistically significant difference at the 0.05 level between borrowers and non-borrowers.

Notes: For the first two columns ("a" reason), multiple responses were allowed per respondent. For the last two columns ("main" reason), only one response was allowed per respondent.

Borrowers went through counseling and obtained reverse mortgages, while non-borrowers went through counseling and ultimately decided not to take out a reverse mortgage.

Source: AARP Public Policy Institute, 2007.

We surveyed selected HECM lenders and counselors in Wisconsin, California, Maryland, and Florida to obtain the industry's perspective on these loans, including how borrowers use them. Their responses supported the AARP conclusions and provided additional insight.[39] Both lenders and counselors gave many of the same reasons borrowers seek reverse mortgages. Some lenders and counselors stated that borrowers' use of loan proceeds to pay off mortgages and to finance increases in their daily expenses was due to cost of living increases that were presumably unanticipated. Lenders and counselors suggested that homeowners sought reverse mortgages: to provide the "security of being able to keep the home

[39] See Appendix C for survey questions and results.

and supplementing the income giving them peace of mind;" out of "desperation;" and because "people need more help now" (in reference to the current economy).

Not all borrowers choose reverse mortgages because of a pressing need. Rather, they may use the proceeds to buy a new home, make investments, or to assure access to funds for long-term care, lenders and counselors reported. The fact that most borrowers choose a line of credit payment option, allowing them to choose the time and amount of loan payments on a request basis, further suggests that most borrowers value the ability to meet future emergency expenses and provide a sense of security should they require additional income supplements.

To discover whether reverse mortgages are needs-driven or extras-driven, AARP disaggregated the findings by age, gender, income level, marital status, assets, home values, and health status. The individuals most likely to use their reverse mortgages to finance basic needs included those with lower incomes and fewer assets, who were 80 and older, had lower valued homes, who were widows or divorcees, or had poorer health status. Borrowers who were wealthier, younger, healthier, and married or never married were more likely to use their reverse mortgages for what the AARP report labels "extras." [40] The AARP findings and our interviews with lenders lead to the conclusion that borrowers seek and use the payments from reverse mortgages for a wide variety of reasons, which suggests that they face different risks in loan use and accumulation.

Why not choose a reverse mortgage?

There are many reasons eligible households who could benefit from the additional income do not choose to borrow against their home equity. Of course, not all eligible households need the additional income a reverse mortgage would provide, and homeowners may prefer to retain their equity in their homes. Some people who would benefit may not be aware that reverse mortgages exist. Mistrust of reverse mortgages may also contribute to underuse. Based on national surveys in 1999 and 2007, AARP reported an increase from 51 percent to 71 percent in the share of respondents who indicated that they had heard of reverse mortgages.[41] The Harris polling organization also conducted a national survey in 2007 and found that about 64 percent of respondents had heard of reverse mortgages, in contrast to home equity loans (78 percent), adjustable-rate forward mortgages (74 percent), and forward fixed-rate mortgages (72 percent). Among those who had heard of reverse mortgages, only 15 percent said they were very knowledge-able and 34 percent said they were somewhat knowledgeable of how reverse mortgages work. Even fewer had a favorable impression of reverse mortgages. Only 5 percent of respondents who had heard of reverse mortgages had a very favorable impression, 20 percent were somewhat favorable, and 18 percent were very unfavorable. Attitudes toward fixed-rate forward mortgages were much more

[40] AARP Public Policy Institute, 2007.
[41] Ibid.

favorable; 40 percent of respondents had a very favorable impression of this type of loan.[42]

A reluctance to reduce home equity is likely a major factor contributing to the lack of reverse mortgage use. After the time and investment needed to obtain a home, many individuals may have psychological and cultural reasons for not wanting to use their home to secure a reverse mortgage.

In 2007, AARP surveyed individuals who showed interest in a HECM, completed counseling, and *then* decided against obtaining a loan. Of the homeowners who completed the counseling process, 75 percent obtained a HECM, while 25 percent decided against it. Table 3 shows the results from the AARP survey regarding why counseling clients did NOT apply for reverse mortgages. In this survey respondents were able to give multiple reasons. It is important to emphasize that this is a fairly small group of "non-borrowers." [43]

Table 3: Reasons Counseling Clients Did Not Apply for Reverse Mortgages

Reasons for Not Applying	A Reason (n=346)	Main Reason (n=340)
The costs of the reverse mortgage were too high.	63%	30%
You decided that reverse mortgage was not necessary given your/the homeowner's financial situation.	54%	10%
You decided that a reverse mortgage would make more sense in the future than it would now.	43%	9%
You found another way to meet your or the homeowner's financial needs.	56%	9%
You like knowing that you or the homeowner owns the home completely, free of any mortgages.	57%	6%
The amount of money you would have received was too small.	28%	5%
You are still considering whether to apply for a reverse mortgage.	31%	5%
The process of taking out a reverse mortgage was too long or too complicated.	20%	4%
You want your children or other loved ones to inherit the home, or you want the home to remain in the family when you or the homeowner dies.	40%	4%
You are concerned that a reverse mortgage will put you or the homeowner in too much debt.	31%	3%
The costs of the home repairs required to get the reverse mortgage were too expensive.	13%	1%

Source: AARP Public Policy Institute, 2007.

[42] Harris Interactive, 2007.
[43] AARP Public Policy Institute, 2007.

The most common reason for not applying for a HECM was the perceived high cost of obtaining a reverse mortgage. Other reasons included finding alternative financial solutions and postponing the decision to take out a reverse mortgage.[44]

The results of the survey imply that the relatively high costs of reverse mortgages are a major barrier when making the final decision on whether to obtain one. The results of the Harris survey show that many seniors may be unaware of the HECM program and its insurance protection aspects or are simply distrustful of the program even if aware. Responses to the AARP survey imply that even those who had investigated the option of a reverse mortgage and later sought other loan alternatives may not have fully understood the costs and benefits of reverse mortgages.

The AARP results suggest several key insights for increasing the attractiveness of reverse mortgages for those who would benefit by accessing their home equity. First, consumer awareness of the product needs to be increased. Second, resistance to reducing home equity after retirement may need to be reduced. Finally, because the costs and complexity of obtaining a reverse mortgage present a major barrier to the willingness to participate in a reverse mortgage and to market growth, counseling to both inform and protect borrowers is a key requirement. Counseling should be structured to allow the borrower to fully digest potential costs they may incur but also the protections provided. The perceived risks and costs associated with reverse mortgages are also related to uncertainty about the future values of housing and other savings. This uncertainty has a significant impact on the actions with regard to reverse mortgages of borrowers, lenders, and the government. We discuss the effect of declining housing prices next, and other risks and costs later in the report.

The effect of the recession and housing price declines

HECM originations continue to expand at a record pace, and HECMs are assuming a growing share of the reverse mortgage market. According to the National Reverse Mortgage Lenders Association, the FHA insured a record 11,261 reverse mortgages in March 2009 and 57,856 loans since October 1, 2008, when the current federal fiscal year began.[45] This compares with 9,663 loans endorsed in March 2008 (or 55,218 year to date for fiscal year 2008).[46] These statistics also coincide with e-mail responses to our survey from private lenders, the majority of whom say they have originated more loans and received more inquiries at the end of 2008 and beginning of 2009, compared to the beginning of 2008.

---

[44] AARP Public Policy Institute, 2007.
[45] NRMLA, 2009.
[46] Ibid.

There are three economic conditions that are relevant to understanding the continuing growth in HECM originations: (1) depreciating home values, (2) low interest rates, and (3) weak-performing investment portfolios. The recent decline in home values would be a disincentive to taking out a HECM because the associated costs have not changed while the amount the homeowner is able to borrow is less. However, interest rates for HECMs are now relatively low, increasing the share of value that can be borrowed, and borrowers' other investments have underperformed, increasing the relative value of accessing home equity. These incentives are more than offsetting the disincentive of a lower maximum claim amount.

The long-run prospects for new originations are favorable for growth in HECM origination numbers. Lenders responding to our survey reported that since the recession began, owners of homes worth $1 million and more are asking about reverse mortgages, which they note is an entirely new phenomenon. This is most likely a consequence of an increasing need to stave off foreclosure and offset diminishing investment assets even among those in higher valued homes.

Decreases in home value do not increase a borrower's net liability because HECMs are non-recourse loans, under which a borrower can never owe more than the value of the property at the time the loan is repaid. However, decreasing home values increase the likelihood that a loan balance will exceed the value of the property. Thus, HUD may incur a large negative net liability in the short term as a result of falling house prices. In the longer term, (realized) liability may not rise if borrowers are less likely to sell their homes (terminate the loan) until housing values recover. It is important, though, to assess the magnitude of the effect of HUD's short-term liability and to examine the interaction between economic factors that would increase (or decrease) that liability and borrowers' decisions.

What Are the Costs and Risks of Reverse Mortgages?

One of the main drawbacks to reverse mortgages is that borrowers do not fully understand the risks and costs of this relatively new financial tool. This section outlines the risks involved with various types of reverse mortgages and compares the costs of reverse mortgages to other means of accessing home equity. We distinguish risks to government, lenders, and consumers. Further disaggregation by age, race, and income is shown in Appendix B.

Costs of reverse mortgages to homeowners

Although reverse mortgages provide elderly homeowners a tool for accessing home equity, they are not without costs to homeowners. Reverse mortgages require significant upfront costs, including origination fees, closing costs, mortgage premium insurance, and servicing fees. Fees may be financed as part of the reverse mortgage, thereby reducing initial out-of-pocket expenses. Loan values compound over the life of the loan and must be repaid when due.[47] These fees reduce the equity share that is paid to the borrower and more rapidly reduce the equity that remains when the loan is paid off. As a result of the high initial costs and the requirement they be paid back upon the home sale, reverse mortgages may not be a good option for homeowners who require a modest income supplement for only a short amount of time.

Comparing HECMs and home equity lines of credit

The decision to take out a reverse mortgage not only requires an evaluation of the risks involved to the borrower but also a comparison to other forms of tapping home equity for cash income. Table 4 compares the costs and requirements between a HECM loan and a home equity line of credit.

[47] NRMLA, 2006.

Table 4: Home Equity Conversion Mortgage vs.
Home Equity Line Of Credit and Which Has the Advantage

	Home Equity Conversion Mortgage (HECM)	Home Equity Line Of Credit (HELOC)	Advantage
Amount Available to Borrow	Based on age, interest rate, appraised value, or available equity. Generally 40-80% of equity.	Not age-based. Up to 70-100% of available equity, depending on income.	HELOC
Closing Costs	Usually $10,000-$20,000.	Usually $400-$1,500.	HELOC
Loan Term	Payable only when homeowner dies, sells, or permanently moves out.	Due at end of 10 years, after which loan needs to be repaid or refinanced.	HECM
Required Payment	No loan payments required until loan terminates.	Minimally required payment each month of interest accrued on loan balance during prior month.	HECM
Qualifications	Minimum 62 years of age. Income and credit score not considered.	Requires monthly payments. Lenders concerned about borrower's ability to pay gauged by credit scores, income, and savings.	HECM
Interest Rate	Adjustable. Determined by adding a "margin" to specified index rate such as the one-year U.S. Treasury. Deductible at loan termination. Tend to be lower rates than HELOC. Capped at 10% monthly.	Adjustable. Determined by adding a "margin" to specified index rate such as the one-year U.S. Treasury. Tax deductible. No cap.	HECM, however closing costs are typically financed, which accrues interest.
Unused Line of Credit	Interest accrues only on amounts drawn. Grows at same rate as borrower is paying on used loan balance.	Interest accrues on amounts drawn.	HECM

Source: CRS, 2008.

The advantage of the line of credit is clear from the table, requiring significantly lower closing costs and allowing the borrower to access higher amounts of home equity. However, reverse mortgages appeal to homeowners who are "house rich and income poor" because they provide additional income with no monthly payments. Unlike a home equity line of credit, a reverse mortgage does not require a borrower to meet income, asset, or home value restrictions to qualify for the loan. An important distinction is that the reverse mortgage loan repayment is not required until the borrower dies or no longer uses the home as the primary residence while home equity loans must be paid back over the life of the loan. That no payment is required during the life of the loan makes reverse mortgages most attractive to those with few resources beyond their home equity.[48] Hence, the minimal qualifications of reverse mortgages make them a more viable option for low-income homeowners.

Borrowers must consider various risks when deciding how to access their home equity for cash income. Selling one's home allows homeowners to access all accumulated equity, though the owner must move and pay for other housing.[49] Obtaining an equity line of credit requires a sufficient income versus debt ratio to qualify for the loan and monthly repayment begins immediately after the loan is disbursed. If a borrower with a home equity line of credit misses a monthly payment, he or she faces foreclosure.[50] Reverse mortgages avoid these risks.

Reverse mortgage risk

During the lifetime of a reverse mortgage, the loan balance grows due to both principal advances to borrowers and the accrual of interest and other loan charges on those advances. The outstanding loan may rise above the property value, which is known as crossover risk. The crossover point is approached if property values appreciate at a lower rate than that rate at which the loan increases.[51]

HECM loans are non-recourse loans, so if crossover occurs, the homeowner may continue to live in the home without fear that other assets will be garnished then or when the house is sold. HUD assumes the risk that the mortgage balance will exceed the value of the property when the house is sold. Lenders have the option to assign an active HECM loan to HUD when the loan balance reaches 98 percent of the maximum claim amount, thus transferring the consequences of crossover to HUD.[52] From the lender's perspective, the assignment of an active loan to HUD is the equivalent of a loan termination without loss to the lender. This action makes no difference to the borrower.

What distinguishes a HECM from other reverse mortgage products is that the FHA insurance flows two ways, to the lender and the borrower. The HECM program protects lenders both from borrowers who outlast the expected maturity event and from a decline in property values. In addition, the HECM protects the borrower from lender default, continuing to provide term or tenure payments and protecting the loan from being foreclosed. FHA also provides this insurance at a lower interest rate than private programs.

While HECMs substantially reduce the risk of reverse mortgages to lenders, they are not insured against all risks. FHA insurance does not cover the lender from

---

[48] HUD, 2009d.
[49] Eschtruth, Sun, & Webb, 2006.
[50] HUD, 2009e.
[51] Szymanoski, 1994.
[52] Szymanoski et al., 2008.

natural disasters, earthquakes, or floods. Hurricane Katrina led to losses by some lenders in the South because HUD was not liable for homes destroyed by the hurricane.[53] In addition, if a lender fails to make a payment to the borrower, HUD can strip the loan from the lender, in which case the lender would lose the amount already advanced to the borrower.[54]

HECMs do not protect borrowers against the risk of outliving a non-annuitized line of credit. Thus a homeowner might live much longer than he or she might have expected, and exhaust the original lump-sum distribution or line of credit. In general, people are not good estimators of life expectancy. According to the Society of Actuaries, "61 percent of pre-retirees and 67 percent of retirees under-estimate life spans."[55] Hence, about 7 in 10 retirees looking into taking out a reverse mortgage are likely to live longer than they expect. Borrowers could hedge against outliving their drawdown in equity by choosing the tenure option.

The development of a secondary market

The HECM program was created to allow the reverse mortgage market to grow by creating a secondary market in which lenders could sell their loan, thus protecting them "against losses resulting from non-repayment in full of the loans, [and] thereby making private lenders more willing to offer these loans."[56] A competitive and flourishing secondary market for reverse mortgages broadens the lender distribution channels and expands the investor base, which reduces lender risk and may lower borrowing costs for lenders competing for low-risk assets. Standard & Poor's projects the reverse mortgage market is poised to grow the most among secondary markets in the short-term.[57]

Before 2006 Fannie Mae was almost the lone purchaser of HECM loans from originating lenders. According to HUD, "the liquidity that Fannie Mae brought to the HECM market was vital to the success of the program in its early years."[58] Ginnie Mae began its HECM mortgage-backed securities program in September 2007, which gave lenders a new option to securitize FHA reverse mortgages in the secondary market. According to Standard & Poor's, "the secondary markets will continue to add certain efficiencies to the process, reducing the costs associated with originating reverse mortgages."[59]

The principal limit factor is an adjustment to the maximum claim amount, which incorporates risk factors to the payment stream. By adjusting payments based on age, expected interest rates, expected property appreciation, etc., HUD can

---

[53] Lender's response in authors' survey.
[54] Szymanoski, 1994.
[55] MetLife, 2003.
[56] HUD, 2008a.
[57] Schneider, Dougherty, & Shaikh, 2008.
[58] HUD, 2008a.
[59] NRMLA, 2009.

mitigate its liabilities. The mortgage insurance premium is a risk pooling mechanism that covers losses in the event of crossover. The HECM program's mortgage insurance premium charge of 2 percent at origination and 0.5 percent monthly has been actuarially sound. In other words, HUD had largely broken even through 2007, with revenues slightly higher than losses.[60]

Because of the recent problems banks have had related to mortgage-backed securities with forward mortgages, and because HECMs are a safe, low-risk asset to have on a balance sheet, an evolving secondary market for reverse mortgages could spur private product innovation as well as lead to lenders competing to offer HECMs at lower interest rates and with lower closing costs.

[60] HUD, 2008a.

Safeguards for Consumers

The HECM program includes various protections for consumers seeking to close on reverse mortgages. Regulations ensure borrowers understand how the HECM works and guard against the possibility that unscrupulous lenders take advantage of seniors. These safeguards take two forms: HUD requires loan counseling for HECM applicants, and safeguards are built into the HECM program design.

Counseling

Consumers have less understanding of reverse mortgages, compared to forward mortgages, because they are not as familiar with this newer product. Counseling gives borrowers the opportunity to discuss with a qualified individual the appropriateness of a reverse mortgage given the borrowers' life circumstances.

Before they can receive FHA-insured HECM, borrowers must complete loan counseling with HUD-approved third-party counselors, who are "neither directly nor indirectly associated with the mortgage transaction."[61] To ensure that borrowers understand all potential consequences of a HECM agreement, counseling must include discussion of other housing and financial options; the social services and health care available to seniors; other choices for home-equity conversion; and the financial consequences of entering into a HECM agreement. HUD mandates that agencies serve a specific geographic region or location so they are familiar with applicable state and local laws, and other programs that could benefit consumers.[62] Under Section 225 of the National Housing Act, loan counselors are required to review a borrower's financial information, complete a budget analysis, and determine whether other alternatives to a HECM would better meet the borrower's needs.[63]

Consumer counseling can be provided in person or over the phone to better serve seniors who are unable to travel due to limited mobility and health conditions.[64] Telephone counseling can be completed with a local agency or with one of the AARP counselors.[65] The AARP counselors are permitted to serve all borrowers regardless of location; however local agencies may provide telephone counseling only to borrowers who cannot travel to the local agency.[66]

HUD does not permit HECM lenders to directly contact a counselor or counseling agency on behalf of the borrower.[67] Initially, counselors were not allowed

[61] Rodda et al., 2000; HUD, 2009e.
[62] HUD, 2004.
[63] HUD, 2009e.
[64] HUD, 2006.
[65] HUD, 2008b.
[66] HUD, 2006.
[67] HUD, 2009e.

to accept fees for their services.[68] As of 2007, FHA allows counseling agencies to charge a “reasonable and customary” fee ($125 per counseling session) for their services, as long as the fee does not create a “financial hardship” for the borrower.[69] Income and debt obligations determine whether a borrower must pay the counseling services fee. Counseling agencies are not allowed to deny services to borrowers unable to pay.[70]

Results from our survey of reverse mortgage lenders and counselors suggest that the counseling requirement may not adequately address all borrower risk.[71] While lenders and counselors stressed that they provide complete information to the borrowers with whom they work, many reported that they were uncertain that all borrowers received sufficient counseling. Others suggested that counseling may not be provided until the loan process is almost complete. One counselor reported that she was concerned that borrowers were receiving counseling only as a formality. She wrote that lenders were referring borrowers for counseling services when they already had a closing date for their loan and requesting that she complete the necessary paperwork to show counseling occurred.

Other borrower protections

Often consumers will be advised to consider taking a reverse mortgage by a third-party or an entity not approved to originate FHA loans. Examples of third-parties include estate-planning services and financial advisors. As a borrower protection, HECM rules permit third parties to receive compensation for services only under limited circumstances.[72] Third parties are eligible for compensation for providing educational information to borrowers (“Advisor” services) when “engaged independently by the homeowner.”[73] Examples of these services include:

- educating prospective borrowers about reverse mortgage lending,
- demonstrating how closing costs and payment options could vary under each product, and
- maintaining regular contact with the lender to keep the borrower apprised of the status of the loan application.[74]

These services may only supplement the counseling requirement. Third parties may not fill out or process loan applications or close loans.[75] Third parties are not permitted to collect fees for simply referring a borrower to a FHA-approved lender. To address concerns that borrowers were paying fees not necessary to

---

[68] Rodda et al., 2000.
[69] HUD, 2008b.
[70] Ibid.
[71] See Appendix C for survey responses from lenders and counselors.
[72] HUD, 2008b.
[73] Ibid.
[74] HUD, 2008b.
[75] Ibid.

obtain a HECM to third-parties, loan counselors are required to inform consumers they may not use proceeds from a HECM loan to pay third-party fees.[76]

The HECM design includes additional consumer protections. All HECM loan brokers are required to use the same software program when determining a borrower's eligibility for a loan, providing borrowers with standard estimates for loan eligibility and amount. This limits the necessity for "shopping around" for a loan, as differences in loan estimates are not likely to arise among different lenders. Borrowers are protected from high loan fees by the fee limits placed on lenders under HUD rules.[77] These limits were put in place after complaints were made that borrowers were being charged "exorbitant fees." HUD limited the maximum origination fee that can be financed to $6,000, effectively limiting the origination fee to this amount because borrowers often do not have money to otherwise pay the fee. Lenders surveyed by Abt Associates reported that this fee was generally lower than the origination fee charged for a forward mortgage.[78] Borrowers have the option to cancel a reverse mortgage within three days of the loan closing. They must notify the lender in writing and may cancel for any reason. The federal truth-in-lending law also protects reverse mortgage borrowers by requiring lenders to disclose the projected average annual cost of the loan.[79]

Marketing of reverse mortgages to improve program image

As mentioned, AARP has studied consumer awareness and confidence in reverse mortgages, conducting two national surveys in 1999 and 2007.[80] Results have shown that seniors are aware that reverse mortgages exist but do not have complete understanding of how the program works. In the 2007 study, survey respondents were questioned about their awareness of different mortgage products, both forward and reverse, and their understanding of how the product works. Respondents reported being the least familiar with reverse mortgages out of all mortgage products.

Various sources publish information about reverse mortgages. HUD and AARP maintain detailed websites listing HECM program information, available lenders and counselors, and alternatives to HECMs. In addition, the National Council on Aging has created a program, "Use Your Home to Stay at Home" that presents positive aspects of the HECM program, including how seniors can use reverse mortgages to remain in their homes and pay for long-term health care.[81] Lenders have also initiated their own direct market campaigns to address the lack of consumer awareness and knowledge of the HECM program. HUD allows

[76] Rodda et al., 2000.
[77] Rodda et al., 2000.
[78] Ibid.
[79] Stucki, 2005.
[80] AARP Foundation, 2008.
[81] Stucki, 2005.

lender marketing, as long as lenders present a fair picture of all costs involved in taking a HECM loan.[82]

A potential pitfall of direct marketing is the opportunity provided for unscrupulous lenders to target uninformed senior citizens. AARP, state attorneys general and other state agencies have issued warnings and "scam alerts" to protect seniors from fraud related to reverse mortgages. AARP has detailed one scam in which a company sent unsolicited direct mailings to seniors requesting they return a card listing their age and phone number to receive information about "free money" for which they could be eligible. In turn, the company would sell this information to reverse mortgage vendors.[83] Although the potential for fraud in reverse mortgage marketing exists, there are few data on the frequency of fraud occurrence.

[82] Rodda et al., 2000.
[83] Kirchheimer, 2009.

Conclusions and Recommendations for GAO

More than 90 percent of reverse mortgage loans are in the form of HECMs. From their beginning in 1989 through 2007, HECM originations have made up a very small percentage of the mortgage market, amounting to about 500,000 loans.[84] While the 1990s produced a few hundred HECMs loans annually, the 21st century has been a marked contrast.

The 21st century has also shown a change in borrower characteristics. HECMs may no longer be a product that is primarily for low-income homeowners. In fact, many lenders have noted that the HECM program is an increasingly popular option for homeowners with home equity above $1 million. Data show that on average borrowers have increasing home values. Perhaps the program's rapid growth is exposing an even greater policy question—whether retirees increasingly view housing equity as an income alternative as concerns grow about the adequacy of Social Security and private pension plan benefits.

The HECM program created a secondary market with which to protect borrowers and lenders from losses that can occur from lender default, borrower non-repayment, and loan balance exceeding property value. An evolving secondary market in the private sector could result in lower costs for borrowers, more fixed rate HECMs, and product innovations that could further expand the reverse mortgage market.

The recent shock to the housing market will undoubtedly increase HUD's short-term liabilities. It is important for GAO to assess and continue to monitor the losses HUD is likely to incur from defaulting lenders and falling property values during this recession. At the regulatory level, it will be interesting to follow the changes to the limits to the maximum claim amount (which has almost doubled since 2007) and to understand the policy implications of higher HECM loan limits.

Finally, anecdotal evidence shows that there is a potential for consumer fraud, predatory marketing, and insufficient counseling. However, the extent to which this occurs is unknown. Evidence may represent isolated incidences or indicate growing trends.

The recent changes in demographics of borrowers, the economy, and the growth of HECMs present a new reverse mortgage landscape that necessitates the collection of better data. This will allow a more clear understanding of who is taking out reverse mortgages, for what reason, and the problems borrowers may face when taking or repaying the loan. With more complete data, reverse mortgages can be compared to other retirement security options, to determine whether they are a

[84] NBER, 2008.

good alternative for the entire eligible population, or better provide a niche product for select individuals.

As the HECM program approaches the 20-year mark since its inception, more recent and more complete data on HECM terminations will enable studies of the extent to which borrowers outlive their home equity. Thus, it is important that borrowers (and policymakers) understand the differences between the line of credit option and tenure option and why more borrowers don't choose the tenure option. As borrowers' average age continues to fall and the average loan duration continues to rise, exhausting a line of credit is more likely. Because reverse mortgages exhibit an accumulating loan balance, HUD's liability may grow if the housing market does not recover in the near future. New data on repayment of loans will allow better analysis of the relative advantages of the various payment stream options, such as comparing the tenure and line of credit options. When collecting new data, the GAO may want to ask questions regarding how borrowers perceived the lending institution and whether any problems arose with scams or fraud.

Based on the current data and a review of the literature, we find that reverse mortgages represent a potential retirement security alternative for those who have little income, but considerable home equity. However, as HUD amends reverse mortgage requirements to make them more accessible to a larger share of the population, and the GAO may want to consider the implications for retirement income security. As other retirement income security alternatives are increasingly insufficient, reverse mortgages may become an increasingly viable alternative to ensuring seniors have a more stable financial future.

References

AARP Foundation. (2008). “Reverse Mortgage Loans: Borrowing Against Your Home.” Retrieved from http://assets.aarp.org/www.aarp.org_/articles/money/financial_pdfs/hmm_hires_nocrops.pdf on April 10, 2009.

AARP Public Policy Institute. (December 2007). “Reverse Mortgages: Niche Product or Mainstream Solution? Report on the 2006 AARP National Survey of Reverse Mortgage Shoppers.” Retrieved from http://assets.aarp.org/rgcenter/consume/2007_22_revmortgage.pdf on January 30, 2009.

Congressional Research Service. (April 2008). “Reverse Mortgages: Background and Issues.” Order Code RL33843, 1-29. Retrieved from http://aging.senate.gov/crs/aging14.pdf on January 30, 2009.

Coronado, J. L., Maki, D. & Weitzer, B. (2007). “Retiring on the House? Cross-Cohort Differences in Housing Wealth.” In B. Madrian, O. S. Mitchell, and B.J. Soldo (Eds.), *Redefining Retirement: How Will Boomers Fare?* New York: Oxford University Press.

Eschtruth, A., Sun, W., & Webb, A. (September 2006). “Will Reverse Mortgages Rescue the Baby Boomers?” Center for Retirement Research at Boston College. Issue Brief No. 54. Retrieved from http://crr.bc.edu/briefs/will_reverse_mortgages_rescue_the_baby_boomers_.html on February 2, 2009.

Harris Interactive. (2007). “Two Thirds of US Adults Believe Current Mortgage Product Advertising and Marketing Lacks Credibility.” Retrieved from http://www.harrisinteractive.com/harris_poll/index.asp?PID=786 on March 13, 2009.

Kirchheimer, S. (9 February 2009). “Scam Alert: Reverse Mortgage Seduction.” AARP Bulletin. Retrieved from http://bulletin.aarp.org/yourmoney/scamalert/articles/scam_alert_reverse_mortgage_seduction.html on April 13, 2009.

MetLife. (2003) “Finding from the 2003 National Survey of American Pre-Retirees.” MetLife Mature Market Institute. Retrieved from http://www.instituteforpr.org/files/uploads/MetLife_IQTest.pdf on April 13, 2009.

National Bureau of Economic Research. (2008). “Reverse Mortgages: A Closer Look at HECM Loans.” Retrieved from http://www.nber.org/programs/ag/rrc/08-Q2%20Bishop,%20Shan%20FINAL.pdf on April 19, 2009.

National Reverse Mortgage Lenders Association. (2009). “Annual HECM Production.” Retrieved from http://www.nrmlaonline.org/RMS/STATISTICS/DEFAULT.ASPX?article_id=601 on April 12, 2009.

National Reverse Mortgage Lenders Association. (2006). "Just the FAQs: Answers to Common Questions About Reverse Mortgages: From the National Reverse Mortgage Lenders Association." Retrieved from http://www.reversemortgage.org/Portals/4/Just%20the%20FAQs%20Revised%201-06.pdf on February 27, 2009.

Reverse Mortgage Daily. (3 September 2008). "Fannie Mae Discontinues Home Keeper Reverse Mortgage Product." Retrieved from http://reversemortgagedaily.com/2008/09/03/fannie-mae-discontinues-home-keeper-reverse-mortgage-product/ on January 30, 2009.

Rodda, D.T., Herbert, C., & Lam, H. (2000). "Evaluation Report of FHA's Home Equity Conversion Mortgage Insurance Demonstration." Cambridge MA: Abt Associates. Retrieved from http://www.abtassociates.com/reports/200030764246417.pdf on March 6, 2009.

Schneider, J., Dougherty, M., & Shaikh, W. (2008). "U.S. Reverse Mortgages, Moving Forward." Standard & Poor's, Ratings Direct. Retrieved from http://www2.standardandpoors.com/spf/pdf/media/leadership_actions_mortgages_051908.pdf on April 19, 2009.

Scholen, K., & Belling, B. (2006). "Home Equity Conversion Mortgage (HECM) Counseling." NeighborWorks Training Institute. Retrieved from http://www.hecmresources.org/resources/study-manual.pdf on February 12, 2009.

Stucki, B. (January 2005). "Use Your Home To Stay At Home: Expanding the Use of Reverse Mortgages for Long-Term Care: A Blueprint for Action." National Council On Aging. Retrieved from http://www.ncoa.org/Downloads/ReverseMortgageReportPublications.pdf on April 13, 2009.

Szymanoski, E.J. (1994). "Risk and the Home Equity Conversion Mortgage." *Journal of the American Real Estate and Urban Economics Association.* Vol. *22*: 347-366.

Szymanoski, E.J., Enriquez, J.C., & DiVenti, T.R. (2008). "Home Equity Conversion Mortgage Terminations: Information to Enhance the Developing Secondary Market." U.S. Department of Housing and Urban Development. Retrieved from http://www.huduser.org/ intercept.asp?loc=/periodicals/cityscpe/vol9num1/ch1.pdf on April 19, 2009.

U.S. Department of Housing and Urban Development. (5 January 2009a). "FHA Reverse Mortgages." Retrieved from http://www.hud.gov/offices/hsg/sfh/hecm/hecmabou.cfm on February 14, 2009.

U.S. Department of Housing and Urban Development. (27 February 2009b). "2009 HECM Mortgage FAQs." Retrieved from http://www.hud.gov/offices/hsg/sfh/hecm/faqs_origination.cfm on April 19, 2009.

U.S. Department of Housing and Urban Development. (26 March 2009c). "HECM For Purchase Frequently Asked Questions." Retrieved from http://www.hud.gov/offices/hsg/sfh/hecm/faqs_hecm.cfm#GEN on April 28, 2009.

U.S. Department of Housing and Urban Development. (28 January 2009d). "How HUD's Reverse Mortgage Program Works." Retrieved from http://www.hud.gov/buying/reverse.cfm on February 14, 2009.

U.S. Department of Housing and Urban Development. (8 January 2009e). "Top Ten Things To Know If You're Interested in a Reverse Mortgage." Retrieved from http://www.hud.gov/offices/hsg/sfh/hecm/rmtopten.cfm on February 14, 2009.

U.S. Department of Housing and Urban Development. (2008a). "A Turning Point in HUD's Home Equity Conversion Program." Retrieved from http://www.huduser.org/periodicals/ushmc/spring08/ch1.pdf on April 19, 2009.

U.S. Department of Housing and Urban Development. (6 May 2008b). "Home Equity Conversion Mortgage Program: Counseling Fee." Mortgagee Letter 2008-12. Retrieved from http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/ on March 29, 2009.

U.S. Department of Housing and Urban Development. (28 September 2006). "Home Equity Conversion Mortgage Program: Home Equity Conversion Mortgage Counseling Requirements." Mortgagee Letter 2006-25. Retrieved from http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/ on March 29, 2009.

U.S. Department of Housing and Urban Development. (30 December 2004). "Home Equity Conversion Mortgage Counseling Requirements Simplified." Mortgagee Letter 2004-48. Retrieved from http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/ on March 29, 2009.

Zedlewski, S., Cushing-Daniels, B., & Lewis, E. (September 2008). "How Much Could Mortgages Contribute to Retirement Incomes?" Urban Institute. Brief Series No. 23. Retrieved from http://www.urban.org/url.cfm?ID=411763 on January 31, 2009.

Appendix A: Comparison of Types of Reverse Mortgage Payment Options

	Advantages	Disadvantages
Term	Provides monthly payments for fixed period of time chosen by borrower. Can provide larger monthly payments than tenure plan. The shorter the term, the larger the payments will be. Repayment is not required for as long as the borrower lives in the home as a principal residence.	Payments stop on a specific date. If borrower exhausts all equity and later must relocate due to health reasons, borrower might be left with little or no funds for relocating and ongoing living expenses.
Tenure	Provides monthly payments to borrower as long as borrower lives in home as principal residence. Payments are fixed and do not change from month to month.	Payments are fixed and will buy less in the future than today due to inflation.
Modified Term/ Tenure	Combines either of these monthly payment plans with line of credit. Added flexibility in case of emergencies. Line of credit creates personal cash reserve for emergencies such as health care expenses.	Adding line of credit to monthly payment plan reduces monthly payment.
Line of Credit	Allows borrower to select the timing and amount of the loan on a request basis until the line of credit is exhausted. Attractive to borrowers who may not need monthly supplemental income, only help with unexpected expenses. Amount of cash remaining available to borrower in HECM credit line grows larger each month (one-year U.S. Treasury rate + 0.5% + lender's margin) until all funds are exhausted.	Cost of set up is expensive relative to the amount of cash received by the borrower if borrower does not access line of credit very often. Once borrower withdraws all available funds, borrower can no longer obtain additional cash advances from it.

Source: Scholen & Belling, 2006.

Appendix B: How do the Different Types of Reverse Mortgages Affect Various Population Groups?

The benefits of the various reverse mortgages programs differ according to the characteristics of the borrowers. These characteristics include age, race, and income.

Differences based on borrower age

Forty-one percent of households owned their homes free of debt as of 2006, and of those homeowners, those with higher incomes were more likely to fully own their homes. The question of homeownership is important to consider when evaluating who is eligible for reverse mortgages, and which population subgroups are more likely to be eligible. When elderly homeowners seek reverse mortgages, the home equity they are able to convert into a loan differs depending on the age of the borrower. “Homeowners age 62 to 69 can convert about half of their equity, while adults age 91 and older can consume about 76 percent of their equity.”[85] Due to reverse mortgages having high closing costs, they may be a more viable option for homeowners who plan to live in their homes for several years. This would indicate that younger borrowers would be more likely to benefit from a reverse mortgage, however, as younger borrowers are not able to convert as much home equity into liquid income, older borrowers actually benefit more from reverse mortgages. Individuals are more likely to own their homes debt-free as they grow older. According to a 2008 Urban Institute study, 26 percent of homeowners ages 55–71 own their homes debt-free, while 57 percent of homeowners ages 72–81 own their homes debt free. Homeownership begins to decline around age 82, most likely due to elderly homeowners selling their homes after the loss of a spouse or when circumstances no longer allow individuals to take care of themselves or keep up with home maintenance and chores.[86]

Differences based on race

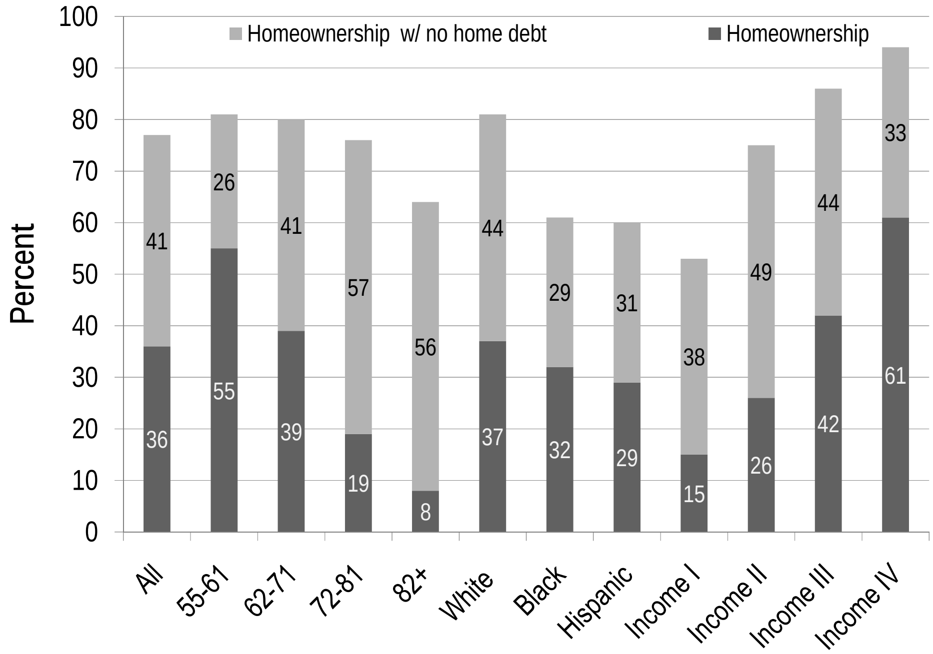
Of the homeowners who own their home debt-free, 44 percent are white, 29 percent are black, and 31 percent are Hispanic. Because whites have higher homeownership rates than Hispanics or blacks, they tend to benefit more from reverse mortgages than minority groups. [87]

[85] Zedlewski, Cushing-Daniels, & Lewis, 2008.
[86] Ibid.
[87] Ibid.

Differences based on income

Reverse mortgages are an alternative to traditional options to access home equity, such as loans or lines of credit. Often low-income homeowners will not qualify for traditional options. Reverse mortgages place income restrictions on home-owners and do not require repayment of the loan until the borrower dies or sells the home. Low-income homeowners, single elderly homeowners, and older homeowners have the potential for the largest gains in income from taking a reverse mortgage. However, these same groups tend to have the lowest homeownership rates.[88]

Figure 2: Homeownership Rates for Households Headed by Adults Age 55 and Older, 2006



Source: Zedlewski, Cushing-Daniels, & Lewis, 2008.

[88] Ibid.

Appendix C: HECM Survey of Lenders and Counselors

We sent the following questionnaire to reverse mortgage brokers and counselors in Wisconsin, Maryland, California, and Florida. We chose these states to provide a representation of different types of mortgage markets. Through this we gained an understanding of how the spring 2009 housing market has affected borrowers and the reverse mortgage industry. We received 11 questionnaire responses: three from California, four from Wisconsin, two from Florida, and two from Maryland.

The questions and responses we received are below. The responses are typed as originally written, which includes grammatical errors.

1.) Have you experienced a trend of continued annual growth in HECM originations within the last 10 year?

9 yes responses; 3 no

Positive Growth Comments:

CA - “They have become more popular every year. The growth of the HECM can also be attributed to the recognition it has gained in the industry. Five years ago, there were only four or five servicing companies, whereas today, there are more than a dozen. People (seniors, mortgage professionals and financial advisors) have become familiar with the product, more educated, and see it as a more easily obtainable and trustworthy option. A strong majority of seniors that I talk to today have at least heard of the program. I could not say that when I started in the industry in 2004.”

WI - “The economic crisis causing the loss in retirement dollars and the overall cost of living increase with food, gasoline and utilities is causing more seniors to seek the reverse mortgage so they can keep their home and supplement their income.”

WI – “started counseling in 1994, with economy the way it is and retirees losing money from the 401ks, a lot of them turning to reverse mortgages”

WI – “RMS have grown in popularity every year I have noticed an increase in growth rate since the subprime bubble popped. Is seems a number of brokers switched from forward to reverse mortgages.”

Negative Growth Comments:

FL - “We did experience a continued growth 2000 to 2005 but since the decline in property value in our area since 2006 I have seen a big decline in REM. People are still interested but do not qualify based on property values.”

MD – “Continued growth until 2008. Reduction in production for 2008 and YTD.”

CA – “I started in the reverse mortgage business in 2003; we communicated with and educated consumers to the merits of the product; at that time reverse mortgages were perceived very negatively. However with a strong media blitz we were able to go from doing zero to doing 300 in 2004, 400 in 2005, 700 in 2006, 600 in 2007, 300 in 2008 and we expect to do about 300 in 2009. We began to feel the adverse affects of a recession in late 2007 and strong impact in 2008 and that continues today since appraised values have tanked.”

2.) Do you expect the reverse mortgage market to continue to grow despite plummeting home values?

7 yes responses; 4 no

Market increase comments:

CA – “Yes, HUD raised limits, helps. Some interested.”

CA – “There are soon to be more senior homeowners than there ever has been as soon as the “baby boomers” have all hit 62, and it makes sense that as the number of the seniors increases so do the number of Reverse Mortgages.

I think senior homeowners are more aware than others of how home values fluctuate over time. Even though they may get a Reverse Mortgage today in a declining market, they understand that it isn’t a one shot deal. When eligible to, they can always refinance to take advantage of increases in home value, lending limits, significant age increases, etc… We have one or two homeowners who have refinanced their Reverse Mortgages more than 4 times with us. Our broker has been exclusively in the Reverse Mortgage industry since 1989.”

WI – “Home values have dropped however it does not appear to have much of an impact on the reverse mortgage market.”

WI – “Home values are not the main factor in deciding about getting a reverse mortgage. Seniors take out reverse mortgages to be able to stay in their homes. Without a RM, most would have to sell and move because they can’t afford to stay.”

Market decrease comments:

CA – “No, I believe we are pretty much stagnated until home values begin increasing.”

MD – “Industry will still grow but at a small rate.”

FL – “Not in the South Florida area. Our agency was counseling over 300 families a year that were interested in REM, but our request for REM counseling has dropped.”

FL – “Not is areas with average home values less than $100,000 and there was a refinance of at least 125% (of property value) within the past 2 years.”

3.) If it is the case that decrease home values make a HECM less attractive, do other factors still draw homeowners to take them out?

All yes responses

Comments:

MD – “Mostly because income decrease, uncertain job security, increasing in expenses etc… Another factor that draws senior homeowners’ attraction is that it is a good time to purchase a second home or investment property from reverse mortgage proceeds. Or as I mentioned earlier, use reverse mortgage to purchase a new home.”

FL – “Increase in living expenses and health care.”

FL – “Individual current debt to income.”

CA – “There are homeowners that do not need Reverse Mortgage benefits as income, more to free up the income that they already have. Simply paying off their liens and getting rid of the mortgage payments sometimes make a great impact. Seniors with incomes of $2000 or less that have a mortgage payment of usually (in California) more that $1000…. well we’re talking about half their pension or social security being taken up by those payments. I don’t think decreased home values make them less attractive to the consumer, it simply makes it more difficult for them to obtain them.”

WI – “Decreased home values can cause the homeowner to not quality for a reverse mortgage. The factors drawing the homeowner to take a reverse mortgage mainly are the security of being able to keep the home and supplementing the income giving them peace of mind.”

WI – “I have not seen decreased home values as a real issue in Wisconsin HECM. Increased cost of living, RE taxes, utilities, food, medical/drug costs make it more difficult for seniors to afford to stay in their homes.”

WI – “pay off current mortgage, liquid cash income, expensive rent for seniors in Madison, so better off to pay off mortgage and the amount in rent”

WI – “Loss of job, home repairs, increase in cost of living”

CA – “desperation”

MD – “With stock and pensions in trouble, people need more money to supplement their income. We can help less of the people that we could have helped a year or two ago but more people need help now.”

4.) Would you describe the “typical” reverse mortgage borrower as “house-rich, income-poor”?

All yes responses

Comments:

“I don’t like the terminology but it is true most of the time.”

“Equity rich. Many comment about how things cost more, but income is not increasing.”

“Not necessarily. There are some seniors seeking the reverse mortgage to payoff an existing mortgage to rid themselves of this payment. In some cases I would not consider them to be house rich but it is likely they are income poor.”

“The most common reason I see people using an RM is pay off an existing mortgage so they can free up the money they are using on payments.”

MD - “House-Rich, Cash Poor was the typical types however it is now changing. The reverse mortgage is now use for purchase new homes and it requires a good amount of down payments so senior with cash poor can’t afford to use the reverse mortgage for purchase options.”

5.) How would you describe the typical reverse mortgage borrower? Age, income

Comments:

CA - “75 with $2,000 per month income and debt payments equal to or exceeding income”

CA - “Most of our homeowners are 70-75 years of age and have incomes of between $1500 and $3000/month. Most are single, but we help a lot of couples too. Most of the single homeowners are female.”

MD - “The average borrower changes depending on the economy. Right now, most borrowers have a mortgage with payments that they need to pay off. They cannot afford the payments. As long as we can get enough money (home values are a factor) we can pay off the mortgage and they can stay in their home. The average age is about 73. Over the past few years, we have seen more couples, more unmarried men and younger borrowers. The typical borrower used to be a 76 woman. We also see many people that need to use their home equity for in home health care. This is more often with older borrowers.

Most borrowers have enough income to make ends meet but they do not have any money for unexpected expenses, such as health issues, losing a job (yes, many still work), home repairs etc… if we can get rid of their debt (mortgage payments and credit card debt) they are often fine. It works best if they are able to leave some money in their line of credit for a rainy day. But that is not always possible.”

FL – “House rich, cash poor.” “The borrowers we counsel, monthly expenses exceed their monthly income and the ones that have mortgages many have paid the home off once before and have refinanced into a forward mortgage mostly (liar loans. If you look at the income they were receiving when they obtained the loan they should have never received that mortgage. Now many are faced with upside down mortgages and facing foreclosure.”

FL – “Within the past five years: average age 65-75. I’m on a fixed income: I need to be able to use my mortgage payment elsewhere.”

WI – “The average borrower has their home paid for and the value of the home is approximately $150,000. They have experienced major medical problems or most recently lost their retirement dollars because of the stock market crash. They no longer have the financial cushion they once had.”

WI – “Homeowner 70+ years who definitely does not want to move out of their home. Wants to stay there until ‘they take me out feet first.’ Needs cash to pay off small mortgage to eliminate payments, or wants to draw a monthly amount to supplement their income. Wants to stop worrying about a tight monthly budget. Is not comfortable with monthly budget of social security alone.”

WI – “Most are medium to low-income, now that the lending limit is higher there are a few more higher income borrowers. Pay off credit card debt, outstanding mortgages, everyday living expenses in reserve, home repairs, peace of mind for a lot of people in case something breaks down they have something to fall back on, a way to stay in their home, home health care”

WI – “It varies widely, most are looking to either pay off a mortgage or do home repairs they could not otherwise do.”

MD – “The users are definitely younger than it used to be and lots of them are couples. They don’t like to be strapped with money and would prefer to enjoy their lives more. Therefore, most of younger borrowers are using reverse to pay off their existing mortgages.”

6.) Do you think the current economy will affect the type of homeowner that is borrowing?

Comments:

CA – “It has; only those who really need help are getting reverse mortgages; others are waiting for the appraised values to go up.”

CA – “Definitely. The past six months of shown us just what kind of situation the seniors were in. Some were utilizing option payments, paying interest only or less than interest, and that caught up to them in this market. Forward loans were also easier to get than they are now, so that option isn’t as viable for our homeowners anymore. As I said before, the cost of living is also escalating, so the need for RMs is growing…”

CA – “People with higher home values have been borrowing. All large banks used to have their own private programs – used to be higher value. Now only FHA program available with increase in limit.”

MD – “I think we will see more an more homeowners who thought that they had plenty of money for retirement but now find they need something more.”

MD – “As baby boomers are retiring in near future with high balance of mortgages, I predict there will be more demanding for fixed and lump sum product, and borrowers will get younger.”

WI – “few more homeowners with a higher income and higher priced homes. More people are compared about long term effects and what’s going to happen with economy and so more interest with annual adjustable than fixed rate because people are concerned with interest rates going up – even though lower with monthly adjustable.”

WI – “If the current economy stays as it is for awhile I predict an increase in the number of seniors turning to this product. Educating them is critical so they understand thoroughly how they will have to manage the money.”

WI – “Homeowners are seeing the income and savings they have from CDs, stocks, etc. dwindle away. It has made them worry more about running out of money in old age. I think more seniors will turn to reverse mortgages to supplement their income and stay in their home.”

WI – "I am concerned about two trends that have arisen in reverse mortgage lending. The first is a push from lenders to encourage existing RM borrowers to refinance now that the FHA Modernization bill has passed. Clients are being told that more money is available to them now that the lending limits have been raised. While this may be true in some cases, none of the clients I have met stand to gain any appreciable advantage from the changes to the RM loan.

The second and more troublesome trend is the increasingly aggressive marketing of reverse mortgages on the part of brokers. This is of concern because I am seeing some of the same language and tactics that were common during the sub-prime lending boom. For example clients are being told not to make their mortgage payments while waiting for the loan to process while some clients are being guaranteed that the loan will go through.

Most troubling is the number of clients that are referred by brokers with a closing date. I have been told repeatedly by brokers that the client is set to close on the loan, and they just need a certificate to finalize everything. By scheduling the counseling so late in the process, the brokers are seeking to reduce it to a formality. Even if the client has concerns after the counseling, they are likely to proceed with the loan because they already have invested a great deal of time and in some cases money into the process.

The common thought is that this doesn't really matter because the reverse mortgage doesn't require monthly payments, and once the homeowner has passed away or left the property, the status of the loan in of little concern.

This way of thinking is completely incorrect for a number of reasons. First the amount of equity that is taken to set up a reverse mortgage is substantial and should not be ignored. Secondly, homeownership is still, despite recent trends, the best way to build wealth and pass that wealth on to future generations. This is especially true among minorities and low-to-moderate income populations. Entering into a reverse mortgage without fully realizing the impacts on the ownership and equity of the property can undo years of wealth building and could lead to a wide scale loss of wealth in these communities. Lastly, the reverse mortgage does not insure homeownership they way it sometime portrayed. Homeowners can face foreclosure on a reverse mortgage by failing to pay their taxes, failure to maintain home-owner's insurance, or failure to maintain the physical condition of the property.

With the decline in home sales and refinancing, the reverse mortgage is looked at more than ever as a moneymaking loan and is attracting a growing number of lenders and brokers. In many cases these are the same players who helped to create the sub-prime loan crisis and some have continued to provide their clients with bad advice either through willful deceit or lack of knowledge. This is an issue that needs to be addressed sooner rather than later. The foreclosure crisis may be attracting most of the attention, but the reverse mortgage is the coming storm that we need to prepare for."

7.) What type of loan payment do most borrowers take? Annuity, line of credit, lump sum?

Comments:

CA – "It is a rare occasion when a homeowner takes a lump sum, usually only when the lump sum available is small because their debt payoff is high. Almost all take a line of credit."

CA – 70% credit line; 25% lifetime income; 5% lump sum

MD – "line of credit and lump sum to pay off existing mortgages"

WI – "the line of credit is by far the most popular"

WI - "line of credit"

WI – "Most are very conservative about drawing out a large sum of cash. Very few do this. They take a monthly draw of $500-$600 for a certain number of years to supplement income, plus a line of credit to draw upon for emergency cash or to pay RE taxes at end of year."

WI – "The line of credit is the most popular product because they can use the money as needed and the remaining dollar amount stays in the credit line and earns interest."

CA – "Up until last couple months line of credit. Now taking fixed rate."

FL – "Again this is influenced by socio-economics: at least 70% in less than 80% AMI take lump sum."

FL – "Many take lump sum. The reasons we hear a lot is many are looking to have home health aide assistance in the home, and increase income."

8.) Would you say people who take out a reverse mortgage are well educated about the risks and benefits of the product?

9 yes responses; 2 no

Positive Responses (borrowers are well educated)

CA – "We do a good job in educating our clients; I don't believe that is always that case, however."

WI – "I feel that the clients I work with are well educated after the counseling. Some come in knowing pretty much everything they need to some start out not knowing anything about the loan."

WI – "Many have already spoken with a lender, many times the lender explains the reverse mortgage program, receive a lot of information from lenders, send them a book"

WI – "In most situations the people have done a lot of research on the product themselves before they actually come in for counseling."

CA – "Yes, refer to counseling. Personally take a great deal of time to go over everything."

CA – "I believe that they are, especially as time goes on. We don't do a lot of business through the mail, we make "house calls" as we like to call it. We are noticing that we meet with homeowner more times (more than once) than we used to and often with children or advisors present. The more people in the game, so to speak, the more competition we have as well. A lot of homeowners shop and compare companies. As more homeowners get Reverse Mortgages, that's more homeowners that have friends that have Reverse Mortgages, and who better than a friend that's in the program to inform a senior about the pros and cons."

MD – "Most homeowners have looked into reverse mortgages for years before they actually get one. Most older (over 75) have family involved in the discussions."

Negative Responses (borrowers are *not* well educated)

FL – "Most of above mentioned population are influence and informed by commercials or mail-outs"

MD – "No they are mostly not. I do at least make sure that my borrowers are well educated of the program before ready to obtain it. However, I've seen and heard some borrowers were pushed to do reverse mortgages from some inexperience reverse mortgage originators without being completely educated of the program. That is a big concern."

9.) Do individuals looking to get a reverse mortgage typically receive consumer counseling before taking out the loan?

Comments:

FL – "All are required"

CA – "They always do if they end up doing a Reverse Mortgage, it is mandatory. Now that most, if not all, counseling agencies are charging for the counseling, I would say that not a lot get counseled and end up NOT getting the Reverse Mortgage. Only the more serious do…"

MD – "Everyone receives counseling from a non-profit before a loan even begins in process."

10.) How does the counseling process develop and unfold in the lender-borrower-counselor-government relationship?

Comments:

WI – "Not sure I understand the question. Counseling is usually done after the senior meets with a loan originator to explain product/options. Most counselors help senior understand their budget, answer questions about reverse mortgage as a second opinion about what I've told them. Also they verify what fees and costs are for the senior. For the most part, counselors do a good job."

WI – "Because this s HUD product the lender will seek a local housing counselor who can counsel the homeowner. There are some counselors who strictly do the counseling over the phone and then there are some who do both telephone and face to face. Face to face is the best as it gives the counselor the opportunity to build a relationship with them and the lenders. The homeowner has a stronger comfort level that they have made the right decision when they can sit down face to face with the counselor."

WI – "Mostly referred by lenders, not always aware counseling is required. Other agencies that are not lenders – aging office or other non-profits. Or through media coverage"

WI – "As a counselor I can have no relationship with the lender. I cannot schedule an appointment for a borrower with them and I cannot send the counseling certificate to them with the clients permission. I explain to client that my job is make sure thy have enough information to make the best decision possible about the loan, I don't care if they take the loan I care that they make the best decision for themselves and know why they made that decision. FHA often makes changes to RM features and counseling requirements it is the counselors responsibility to stay updated."

MD – "Typical cases, Borrower calls the lender or broker for initial information. In my case, I supply with lists of counseling agencies after my initial face to face interview with borrower. Borrower the call one of their preferred agency and make an appointment for counseling. Time to time, a borrower comes with the counseling certificate and ready to application Knowledge. These borrowers are increasing and they are shopping for better costs of obtaining the loan."

MD – "Counseling is required for all reverse mortgages. Only the HUD loan is really available now but even when there were private programs they always required counseling. As a lender we provide a list of approved counselors to our borrowers. They can then be counseled by phone or in person. Once they are counseled, they receive a certificate and we must have that certificate, signed by both the counselor and the borrower before we can even begin processing a reverse mortgage application."

FL – "Lenders always request the borrower contact the HUD agency first to obtain counseling prior to the ordering a application package. Many people are referred to us from the HUD website and the lender."

FL – "Indirectly by lenders: most borrowers are call us (from a list of agencies) after contacting a lender."

11.) From a public policy standpoint, what is most important to know about reverse mortgages?

Comments:

CA – "A reverse mortgage is a very important financial tool that can help seniors gain financial freedom and freedom from fear."

CA – "Unfortunately I don't think lawmakers have in-depth knowledge of the program. In some cases they have addressed the concerns of a few by making regulations that hurt the many. For instance, mandating that counseling be paid for out-of-pocket by the homeowner. Originally, the lenders were allowed to pay for counseling, which we honestly didn't mind doing. For a short time, it was allowed to be a financed cost of the loan. Now we're back to homeowners paying, I understand that this discourages any kind of pressuring or steering, but I don't believe that was a common occurrence. Whereas a lot of our seniors don't have $125 to front and most counseling agencies do not accept credit cards or checks, only money orders or debit cards. It made the process more difficult and more financially straining to a majority of consumers."

CA – "Reverse mortgages can be the best thing for seniors. FHA has their own software, which all lenders must use. This is beneficial to consumers, eliminating predatory aspect of loan."

FL – "It is a product that will allow many borrowers to maintain a comfortable lifestyle and the property will continue to grow in value."

MD – "Affiliate with NRMLA, National Reverse Mortgage Lenders Association or county running Agency in Aging."

MD – "There will be more need for the reverse mortgage but I think people will be less likely to choose to borrow on their home unless it is necessary. Many will do without first. There is much public policy concern about protecting the senior and this is often through the counseling. I think some of the weight to counseling is misdirected, I think that the loan officers should be licensed or certified specifically for this product. It is the lender that knows the specifics of the products, the current pricing and availability of options and specific requirements. They need to be sure to explain it and answer any questions fully and accurately. Also, I think there is some concern that folks from the forward mortgage market have been drifting into the reverse market and they may not have the senior's best interest at heart. I do not think the counselor can provide the detailed information that is necessary so the lender must be the one to explain the details. The counselor should be talking to the borrower to be sure they understand the basics and to look for trends of fraud or other misconduct. To work with a senior and often their family as well can take hours and hours of explanation and this is what the lender is paid to do. Most borrowers do not like talking to the counselor and only do so because they must. If a person is middle class, they feel like it make it seems like a charity program to have to talk to the counselor. They have often worked very hard all of their lives and do not want charity. They will talk to the counselor because they have to but they want someone more familiar with financial issues to talk to them about their specifics. A well trained loan officer can do that."

12.) Have you experienced, or do you foresee any issues with predatory lending/marketing?

Comments:

WI – "As with all loan products there are predatory lenders. What I have experienced in the past is that the homeowner through counseling can pretty much identify if they could be a victim. This is why it is so critical that the counseling takes place and actually a reverse mortgage may not be processed without the HUD required counseling. Seniors are always the target for predatory lenders, home improvement contractors, life insurance agents etc."

13.) What are your general thoughts about reverse mortgages?

Comments:

CA – "A reverse mortgage is a God send to many desperate seniors in trouble in so many ways. We literally save homes and change lives in a very positive manner with this product."

CA – "I think I can honestly say that I would encourage my own relatives to explore the program. The only cons I see are that the heirs inherit less. That is a con to the heir, not to the consumer, as a child of a parent only two years from turning 62, I'd rather see my father taken care of by the house that he worked to pay for, than to benefit from the equity myself at any point. I can understand the desire of seniors to leave their children with something, but in not in cases where their lifestyles are negatively impacted by that choice.

Other than that, I would say that program is going strong and will stay strong. The interesting part will be to see the evolution of the industry on my side of the fence. There are many more players on the field now and more and more regulations."

WI – "The reverse mortgage can be a useful tool for homeowners but it is not for everyone. It is expensive, it carries specific risks and it complicates passing the home on to heirs."

WI – "They are a good product but homeowner should consider other options that are available, should almost be used as a last resort. Do provide security. Have not had a case where children do not support reverse mortgages. Has not experiences issues with predatory lending."

WI – "A reverse mortgage is definitely a good product as it keeps the seniors in their home and gives them the financial stability they need and the reassurance they will be able to meet their needs. It is critical they understand how to manage finances because this is the equity in their home that is giving them the dollars they need and if poorly managed and the money is gone is a short period of time the other alternative is to sell the home or lose it to foreclosure."

WI – "They are an excellent product for seniors who want to stay in there homes as long as possible. It is a way, maybe the only way for them to afford to stay in their homes. I have worked with many seniors who were close to foreclosure or in serious financial trouble due to unpaid taxes, etc.

Many seniors live on social security from month to month and have less than $1,000 in their accounts at any time. NO back up cash in case of emergency.

They are also a good product for producers. It is very rewarding to help seniors. Some can even quit working! Usually they are very grateful and happy after the closing because their money worries are solved."