

## The Advantages of a Reverse Mortgage

For many seniors, the family home is their second biggest asset, next to the value of a retirement income stream. However, short of selling your house, there are only a few ways to get access to the value locked inside. Three of the main ways are by:

- Refinancing or taking out a first mortgage
- Using a home equity line of credit
- Using a reverse mortgage

You've probably heard about reverse mortgages, but aren't completely sure how they work and if they make sense for your situation. So, first some background, and then a summary of the advantages of reverse mortgages. Then next month we'll look at the disadvantages of these popular vehicles.

### What *are* reverse mortgages?

According to *Consumers Union* ([www.consumersunion.org/finance/revconwc899.htm](http://www.consumersunion.org/finance/revconwc899.htm)), the publisher of *Consumer Reports*:

A reverse mortgage is a popular but complex home loan just for senior homeowners. If you qualify for a reverse mortgage, you will not have to make monthly payments on the loan. Instead, the lender pays you. Typically, the reverse mortgage is repaid from your home's equity when you sell the home, move out permanently, or die. You, or those who will inherit from you, can keep any sales proceeds from your home in excess of what you owe the lender. To qualify for a reverse mortgage, you must be a homeowner who is at least 62 years old. The mortgage on your home must be fully or nearly paid off.

A reverse mortgage allows you to receive a loan against your home. This can be in the form of a lump sum, regular monthly checks, or a line of credit. The money is repaid with interest when the borrower sells the house, moves (or goes into a nursing home), or dies.

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### **How much can you borrow?**

The amount you can borrow depends on your age, the current interest rate, and the appraised value of your home or FHA's mortgage limits for your area, whichever is less. Generally, the more valuable your home is, the older you are, the lower the interest, the more you can borrow. For example, based on a loan with an interest rate of approximately 9 percent, and a home qualifying for \$100,000, a 65-year-old could borrow up to 22 percent of the home's value; a 75-year-old could borrow up to 41 percent of the home's value; and an 85-year-old could borrow up to 58 percent of the home's value. The percentages do not include closing costs because these charges can vary (U.S. Department of Housing and Urban Development, [www.hud.gov/offices/hsg/sfh/hecm/hecmabou.cfm](http://www.hud.gov/offices/hsg/sfh/hecm/hecmabou.cfm)).

### **What are some advantages of a reverse mortgage?**

A reverse mortgage can help meet your cash flow needs. The additional monthly payment should run for the remainder of your life, since payments are based on the life expectancy of the owner(s). You are better able to maintain your financial independence and an adequate standard of living. And, with a reverse mortgage, you are able to remain in your home, keep ownership, and increase your monthly income stream.

You are getting, in effect, your own money back. The payments you are receiving consist of the money you paid into the house and any increase in your home's value over the years. This means the money you receive from a reverse mortgage is tax-free.

Reverse mortgages are complicated products and are not right for everyone, so if you're considering one, first talk with a trained and qualified advisor such as those at HUD-approved agencies, who give advice free or at low cost.

### **The Cautions of a Reverse Mortgage**

Given the limited experience most people have with reverse mortgages, it's important to understand the cautions associated with these loans.

In many ways, reverse mortgages “look” like annuities. You get regular payments as long as you follow the lender’s rules. But these mortgages are still loans—not “free” money. Reverse mortgages:

- Are complex and carry a variety of risks and responsibilities
- Have many expenses and charges
- Reduce the value of your estate because they are loans and must be repaid
- May impact your Medicaid-paid long-term care eligibility

### **Complexity**

Reverse mortgages are so complex that, according to the National Reverse Mortgage Lenders Association (NRMLA), you are *required* by law to meet with a reverse mortgage counselor before obtaining the loan to review:

- Options other than a reverse mortgage including housing, social services, health and financial alternatives
- Other home equity conversion options such as property tax deferral programs
- The financial implications of a reverse mortgage
- The tax consequences affecting your eligibility for state or federal programs and the effect on your estate or heirs

### **Costs**

The costs of a reverse mortgage are similar to a new home loan or a home refinance: origination and appraisal fees, an up-front mortgage insurance premium (for the FHA Home Equity Conversion Mortgage – HECM), and standard closing costs such as a credit report, title insurance and various fees. You are also charged interest on the outstanding loan balance and a monthly servicing fee. Adding closing costs and other fees to the initial loan will increase your total loan amount.

Remember, too, that the amount you owe on a reverse mortgage increases each time you receive your monthly payment (or access your line of credit).

In addition, you are responsible for your home’s taxes, insurance, repairs, and maintenance. These things are essential to maintaining the lender’s investment in your reverse mortgage and failure to pay them could result in you being forced to repay the loan. And the only means to repay the loan before you die may be to sell your home.

## **Effect on Your Estate**

A reverse mortgage must be repaid when you no longer use your home as your permanent, primary residence – for example, if you sell it, move into an assisted living or other long-term care facility, or die. That means you, your estate or your heirs must pay back the loan, using either private funds or by selling the home. (The total amount that must be repaid cannot exceed your home's appraised value.)

## **Medicaid Dilemma**

Payments you receive from a reverse mortgage may push you over Medicaid's limits for receiving assistance with long-term care expenses. A reverse mortgage may also reduce your ability to qualify for Supplemental Social Security benefits or benefits specific to your state.

## **Bottom Line**

If your other financial resources are limited, a reverse mortgage may be a viable solution. Talk with your family, a qualified financial advisor and then a certified housing counselor to see if a reverse mortgage is right for you. For help with reverse home mortgage counseling, call the U.S. Department of Housing and Urban Development's (HUD) Housing Counseling Clearinghouse at 1-888-466-3487.

## **For more information:**

- [www.reversemortgage.org/](http://www.reversemortgage.org/) is provided by the National Reverse Mortgage Lenders Association (NRMLA). NRMLA also offers free consumer guides at [www.reversemortgage.org/ConsumerGuides/tabid/251/Default.aspx](http://www.reversemortgage.org/ConsumerGuides/tabid/251/Default.aspx) or by calling 1-866-264-4466.
- [www.aarp.org](http://www.aarp.org): AARP has numerous articles and information on reverse mortgages.
- [www.reverse.org](http://www.reverse.org) is the website for the nonprofit National Center for Home Equity Conversion.
- [www.seniorjournal.com/ReverseMortgage.htm](http://www.seniorjournal.com/ReverseMortgage.htm): *Senior Journal*, an online magazine, offers information and links related to reverse mortgages
- [www.hud.gov/groups/seniors.cfm](http://www.hud.gov/groups/seniors.cfm): the "Information for Senior Citizens" section of HUD's website has links to information about reverse mortgages and HUD-approved housing counselors.

