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Reverse Mortgages:
Get the Facts Before Cashing In On Your Home's Equity

Whether seeking money to finance a home improvement, pay off a current mortgage, supplement their retirement income, or pay for healthcare expenses, many older Americans are turning to "reverse" mortgages. They allow older homeowners to convert part of the equity in their homes into cash without having to sell their homes or take on additional monthly bills.

In a "regular" mortgage, you make monthly payments to the lender. But in a "reverse" mortgage, you receive money from the lender and generally don't have to pay it back for as long as you live in your home. Instead, the loan must be repaid when you die, sell your home, or no longer live there as your principal residence. Reverse mortgages can help homeowners who are house-rich but cash-poor stay in their homes and still meet their financial obligations.

To qualify for most reverse mortgages, you must be at least 62 and live in your home. The proceeds of a reverse mortgage (without other features, like an annuity) are generally tax-free, and many reverse mortgages have no income restrictions.

Three Types of Reverse Mortgages

The three basic types of reverse mortgage are: **single-purpose** reverse mortgages, which are offered by some state and local government agencies and nonprofit organizations; **federally-insured** reverse mortgages, which are known as Home Equity Conversion Mortgages (HECMs), and are backed by the U. S. Department of Housing and Urban Development (HUD); and **proprietary** reverse mortgages, which are private loans that are backed by the companies that develop them.

Single-purpose reverse mortgages generally have very low costs. But they are not available everywhere, and they only can be used for one purpose specified by the government or nonprofit lender, for example, to pay for home repairs, improvements, or property taxes. In most cases, you can qualify for these loans only if your income is low or moderate.

HECMs and proprietary reverse mortgages tend to be more costly than other home loans. The up-front costs can be high, so they are generally most expensive if you stay in your home for just a short time. They are widely available, have no income or medical requirements, and can be used for any purpose.

Before applying for a HECM, you must meet with a counselor from an independent government-approved housing counseling agency. The counselor must explain the loan's costs, financial implications, and alternatives. For example, counselors should tell you about government or nonprofit programs for which you may qualify, and any single-purpose or proprietary reverse mortgages available in your area.

In a "reverse" mortgage, you receive money from the lender and generally don't have to pay it back for as long as you live in your home.

The amount of money you can borrow with a HECM or proprietary reverse mortgage depends on several factors, including your age, the type of reverse mortgage you select, the appraised value of your home, current interest rates, and where you live. In general, the older you are, the more valuable your home, and the less you owe on it, the more money you can get.

The HECM gives you choices in how the loan is paid to you. You can select fixed monthly cash advances for a specific period or for as long as you live in your home. Or you can opt for a line of credit, which allows you to draw on the loan proceeds at any time in amounts that you choose. You also can get a combination of monthly payments plus a line of credit.

HECMs generally provide larger loan advances at a lower total cost compared with proprietary loans. But owners of higher-valued homes may get bigger loan advances from a proprietary reverse mortgage. That is, if you have a higher appraised value without a large mortgage, then you may likely qualify for greater funds. Location (for example, your neighborhood) is only one part of the determination of appraised value.

Loan Features

Reverse mortgage loan advances are not taxable, and generally do not affect Social Security or Medicare benefits. You retain the title to your home and do not have to make monthly repayments. The loan must be repaid when the last surviving borrower dies, sells the home, or no longer lives in the home as a principal residence. In the HECM program, a borrower can live in a nursing home or other medical facility for up to 12 months before the loan becomes due and payable.

As you consider a reverse mortgage, be aware that:

- Lenders generally charge origination fees and other closing costs for a reverse mortgage. Lenders also may charge servicing fees during the term of the mortgage. The lender generally sets these fees and costs.

- The amount you owe on a reverse mortgage generally grows over time. Interest is charged on the outstanding balance and added to the amount you owe each month. That means your total debt increases over time as loan funds are advanced to you and interest accrues on the loan.

- Reverse mortgages may have fixed or variable rates. Most have variable rates that are tied to a financial index and will likely change according to market conditions.

- Reverse mortgages can use up all or some of the equity in your home, leaving fewer assets for you and your heirs. A "nonrecourse" clause, found in most reverse mortgages, prevents either you or your estate from owing more than the value of your home when the loan is repaid.

- Because you retain title to your home, you remain responsible for property taxes, insurance, utilities, fuel, maintenance, and other expenses. So, for example, if you don't pay property taxes or maintain homeowner's insurance, you risk the loan becoming due and payable.

- Interest on reverse mortgages is not deductible on income tax returns until the loan is paid off in part or whole.

Getting a Good Deal

If you are considering a reverse mortgage, shop around to compare your options and the offered terms. Learn as much as you can about reverse mortgages before you talk to a counselor or lender. It will help you ask more informed questions, which could lead to a better deal.

- If you want to make a home repair or improvement or need help paying your property taxes, you may want to find out if you qualify for any low-cost **single-purpose loans** that may be available in your area. Area Agencies on Aging (AAAs) generally know about these programs. To find the nearest agency, visit www.eldercare.gov or call toll-free, 1-800-677-1116. Ask the AAA for information about available "loan programs for home repairs or improvements," or "property tax deferral" or "property tax postponement" programs.

- If you are interested in a federally-insured HECM, know that all HECM lenders must follow HUD rules, and that many of the loan costs including the interest rate will be the same no matter which lender you select. Still, some costs including the origination fee, other closing costs, and servicing fees may vary among lenders.

- If you live in a higher-valued home, you may be able to borrow more from a proprietary reverse mortgage. But it generally will cost more. The best way to see key differences between a HECM and a proprietary loan is with a detailed side-by-side comparison of future costs and benefits. Many HECM counselors and lenders can provide you with this important information.

- No matter which type of reverse mortgage you are considering, be certain you understand all the conditions that could make the loan due and payable. Ask a counselor or lender to explain the Total Annual Loan Cost (TALC) rates, which show the projected annual average cost of a reverse mortgage, including all itemized costs.

Be a Savvy Consumer

Be cautious if anyone tries to sell you something, like an annuity, and suggests that a reverse mortgage would be an easy way to pay for it. If you don't fully understand what they're selling, or you're not sure you need what they're selling, be even more skeptical.

Keep in mind that your total cost would be the cost of what they're selling **plus** the cost of the reverse mortgage. If you think you need what they're selling, shop around before you buy.

No matter why you decide to take a reverse mortgage, you generally have at least three business days after signing the loan documents to cancel it for any reason without penalty. Remember that you must cancel in writing. The lender must return any money you have paid so far for the financing.

Reporting Possible Fraud

If you suspect that anyone is violating the law, let the counselor, lender, or loan servicer know. Then, file a complaint with:

- your state Attorney General's office or state banking regulatory agency, and
- the Federal Trade Commission (FTC). You can do that online at ftc.gov or by phone, toll-free, at 1-877-FTC-HELP (1-877-382-4357).

Whether a reverse mortgage is right for you is a big question. Consider all your options. You may qualify for less costly alternatives. Contact the following organizations for more information:

Reverse Mortgage Education Project

AARP Foundation
601 E Street, NW
Washington, DC 20049
1-800-209-8085
www.aarp.org/revmort/list

U. S. Department of Housing and Urban Development (HUD)
451 7th Street, SW
Washington, DC 20410
1-888-466-3487
www.hud.gov/offices/hsg/sfh/hecm/rmtopten.cfm

Federal Trade Commission
Consumer Response Center
600 Pennsylvania Avenue, NW
Washington, DC 20580
ftc.gov/credit — Click on "Mortgages & Your Home" 1-877-FTC-HELP (1-877-382-4357)

The FTC works for the consumer to prevent fraudulent, deceptive, and unfair business practices in the marketplace and to provide information to help consumers spot, stop, and avoid them. To file a complaint or to get free information on consumer issues, visit ftc.gov or call toll-free, 1-877-FTC-HELP (1-877-382-4357); TTY: 1-866-653-4261. The FTC enters Internet, telemarketing, identity theft, and other fraud-related complaints into Consumer Sentinel, a secure, online database available to hundreds of civil and criminal law enforcement agencies in the U.S. and abroad.

Federal Trade Commission
Bureau of Consumer Protection
Office of Consumer and Business Education