Reverse Mortgage Guide

If you’re 62 or older – and want money to pay off your mortgage, supplement your income, or pay for healthcare expenses – you may consider a reverse mortgage. It allows you to convert part of the equity in your home into cash without having to sell your home or pay additional monthly bills. But take your time: a reverse mortgage can be complicated and might not be right for you. A reverse mortgage can use up the equity in your home, which means fewer assets for you and your heirs. If you do decide to look for one, review the different types of reverse mortgages, and comparison shop before you decide on a particular company.

Read on to learn more about how reverse mortgages work, qualifying for a reverse mortgage, getting the best deal for you, and how to report any fraud you might see.

How do Reverse Mortgages Work?

When you have a **regular** mortgage, you pay the lender every month to buy your home over time. In a **reverse** mortgage, you get a loan in which the lender pays *you*. Reverse mortgages take part of the equity in your home and convert it into payments to you – a kind of advance payment on your home equity. The money you get usually is tax-free. Generally, you don’t have to pay back the money for as long as you live in your home. When you die, sell your home, or move out, you, your spouse, or your estate would repay the loan. Sometimes that means selling the home to get money to repay the loan.

There are three kinds of reverse mortgages: single-purpose reverse mortgages – offered by some state and local government agencies, as well as non-profits; proprietary reverse mortgages – private loans; and federally-insured reverse mortgages, also known as Home Equity Conversion Mortgages (HECMs).

If you get a reverse mortgage of any kind, you get a loan in which you borrow against the equity in your home. You keep the title to your home. Instead of paying monthly mortgage payments, though, you get an advance on part of your home equity. The money you get usually is not taxable, and it generally won't affect your Social Security or Medicare benefits. When the last surviving borrower dies, sells the home, or no longer lives in the home as a principal residence, the loan has to be repaid. In certain situations, a non-borrowing spouse may be able to remain in the home. Here are some things to consider about reverse mortgages:

- **There are fees and other costs**. Reverse mortgage lenders generally charge an origination fee and other closing costs, as well as servicing fees over the life of the mortgage. Some also charge mortgage insurance premiums (for federally-insured HECMs).
- **You owe more over time**. As you get money through your reverse mortgage, interest is added onto the balance you owe each month. That means the amount you owe grows as the interest on your loan adds up over time.
- **Interest rates may change over time**. Most reverse mortgages have variable rates, which are tied to a financial index and change with the market. Variable-rate loans tend to give you

more options on how you get your money through the reverse mortgage. Some reverse mortgages – mostly HECMs – offer fixed rates, but they tend to require you to take your loan as a lump sum at closing. Often, the total amount you can borrow is less than you could get with a variable rate loan.

- **Interest is not tax-deductible each year**. Interest on reverse mortgages is not deductible on income tax returns – until the loan is paid off, either partially or in full.
- **You have to pay for other costs related to your home**. In a reverse mortgage, you keep the title to your home. That means you are responsible for property taxes, insurance, utilities, fuel, maintenance, and other expenses. And, if you don't pay your property taxes, keep homeowner's insurance, or maintain your home, the lender might require you to repay your loan. A financial assessment is required when you apply for the mortgage. As a result, your lender may require a "set-aside" amount to pay your taxes and insurance during the loan. The "set-aside" reduces the amount of funds you can get in payments. You are still responsible for maintaining your home.
- **What happens to your spouse?** With HECM loans, if you signed the loan paperwork and your spouse didn't, in certain situations, your spouse may continue to live in the home even after you die if he or she pays taxes and insurance, and continues to maintain the property. But your spouse will stop getting money from the HECM since he or she wasn't part of the loan agreement.
- **What can you leave to your heirs?** Reverse mortgages can use up the equity in your home, which means fewer assets for you and your heirs. Most reverse mortgages have something called a "non-recourse" clause. This means that you, or your

estate, can’t owe more than the value of your home when the loan becomes due and the home is sold. With a HECM, generally, if you or your heirs want to pay off the loan and keep the home rather than sell it, you would not have to pay more than the appraised value of the home.

Types of Reverse Mortgages

As you consider whether a reverse mortgage is right for you, also consider which of the three types of reverse mortgage might best suit your needs.

Single-purpose reverse mortgages are the least expensive option. They’re offered by some state and local government agencies, as well as non-profit organizations, but they’re not available everywhere. These loans may be used for only one purpose, which the lender specifies. For example, the lender might say the loan may be used only to pay for home repairs, improvements, or property taxes. Most homeowners with a low or moderate income can qualify for these loans.

Proprietary reverse mortgages are private loans that are backed by the companies that develop them. If you own a higher-valued home, you may get a bigger loan advance from a proprietary reverse mortgage. So if your home has a higher appraised value and you have a small mortgage, you might qualify for more funds.

Home Equity Conversion Mortgages (HECMs) are federally-insured reverse mortgages and are backed by the U. S. Department of Housing and Urban Development (HUD). HECM loans can be used for any purpose.

HECMs and proprietary reverse mortgages may be more expensive than traditional home loans, and the upfront costs can be high. That's important to consider, especially if you plan to stay in your home for just a short time or borrow a small amount. How much you can borrow with a HECM or proprietary reverse mortgage depends on several factors:

- your age
- the type of reverse mortgage you select
- the appraised value of your home
- current interest rates, and
- a financial assessment of your willingness and ability to pay property taxes and homeowner's insurance.

In general, the older you are, the more equity you have in your home, and the less you owe on it, the more money you can get.

Before applying for a HECM, you must meet with a counselor from an independent government-approved housing counseling agency. Some lenders offering proprietary reverse mortgages also require counseling.

The counselor is required to explain the loan's costs and financial implications. The counselor also must explain the possible alternatives to a HECM – like government and non-profit programs, or a single-purpose or proprietary reverse mortgage. The counselor also should be able to help you compare the costs of different types of reverse mortgages and tell you how different payment options, fees, and other costs affect the total cost of the loan over time. You can visit HUD for a list of counselors, or call the agency at 1-800-569-4287. Counseling agencies usually charge a fee for their services, often around $125. This fee can be paid from the loan proceeds, and you cannot be turned away if you can't afford the fee.

With a HECM, there generally is no specific income requirement. However, lenders must conduct a financial assessment when deciding whether to approve and close your loan. They're evaluating your willingness and ability to meet your obligations and the mortgage requirements. Based on the results, the lender could require funds to be set aside from the loan proceeds to pay things like property taxes, homeowner's insurance, and flood insurance (if applicable). If this is not required, you still could agree that your lender will pay these items. If you have a "set-aside" or you agree to have the lender make these payments, those amounts will be deducted from the amount you get in loan proceeds. You are still responsible for maintaining the property.

The HECM lets you choose among several payment options:

- a single disbursement option – this is only available with a fixed-rate loan, and typically offers less money than other HECM options.
- a "term" option – fixed monthly cash advances for a specific time.
- a "tenure" option – fixed monthly cash advances for as long as you live in your home.
- a line of credit – this lets you draw down the loan proceeds at any time, in amounts you choose, until you have used up the line of credit. This option limits the amount of interest imposed on your loan because you owe interest on the credit that you are using.
- a combination of monthly payments and a line of credit.

You may be able to change your payment option for a small fee.

HECMs generally give you bigger loan advances at a lower total cost than proprietary loans do. In the HECM program, a borrower generally can live in a nursing home or other medical facility for up to 12 consecutive months before the loan must be repaid. Taxes and insurance still must be paid on the loan, and your home must be maintained.

With HECMs, there is a limit on how much you can take out the first year. Your lender will calculate how much you can borrow, based on your age, the interest rate, the value of your home, and your financial assessment. This amount is called your “initial principal limit.”

Generally, you can take out up to 60 percent of your initial principal limit in the first year. There are exceptions, though.

Shopping for a Reverse Mortgage

If you’re considering a reverse mortgage, shop around. Decide which type of reverse mortgage might be right for you. That might depend on what you want to do with the money. Compare the options, terms, and fees from various lenders. Learn as much as you can about reverse mortgages before you talk to a counselor or lender. And ask lots of questions to make sure a reverse mortgage could work for you – and that you’re getting the right kind for you.

Here are some things to consider:

- **Do you want a reverse mortgage to pay for home repairs or property taxes?** If so, find out if you qualify for any low-cost single purpose loans in your area. Staff at your local Area Agency on Aging may know about the programs in your area. Find the nearest agency on aging at eldercare.gov, or call 1-800-677-1116. Ask about “loan or grant programs for home repairs or improvements," or "property tax deferral" or "property tax postponement" programs, and how to apply.

- **Do you live in a higher-valued home?** You might be able to borrow more money with a proprietary reverse mortgage. But the more you borrow, the higher the fees you'll pay. You also might consider a HECM loan. A HECM counselor or a lender can help you compare these types of loans side by side, to see what you'll get – and what it costs.
- **Compare fees and costs**. This bears repeating: shop around and compare the costs of the loans available to you. While the mortgage insurance premium is usually the same from lender to lender, most loan costs – including origination fees, interest rates, closing costs, and servicing fees – vary among lenders.
- **Understand total costs and loan repayment**. Ask a counselor or lender to explain the Total Annual Loan Cost (TALC) rates: they show the projected annual average cost of a reverse mortgage, including all the itemized costs. And, no matter what type of reverse mortgage you're considering, understand all the reasons why your loan might have to be repaid before you were planning on it.

Be Wary of Sales Pitches for a Reverse Mortgage

Is a reverse mortgage right for you? Only you can decide what works for your situation. A counselor from an independent government-approved housing counseling agency can help. But a salesperson isn't likely to be the best guide for what works for you. This is especially true if he or she acts like a reverse mortgage is a solution for all your problems, pushes you to take out a loan, or has ideas on how you can spend the money from a reverse mortgage.

For example, some sellers may try to sell you things like home improvement services – but then suggest a reverse mortgage as an easy way to pay for them. If you decide you need home improvements, and you think a reverse mortgage is the way to pay for them, shop around before deciding on a particular seller. Your home improvement costs include not only the price of the work being done – but also the costs and fees you'll pay to get the reverse mortgage.

Some reverse mortgage salespeople might suggest ways to invest the money from your reverse mortgage – even pressuring you to buy other financial products, like an annuity or long-term care insurance. Resist that pressure. If you buy those kinds of financial products, you could lose the money you get from your reverse mortgage. You don't have to buy any financial products, services or investment to get a reverse mortgage. In fact, in some situations, it's illegal to require you to buy other products to get a reverse mortgage.

Some salespeople try to rush you through the process. Stop and check with a counselor or someone you trust before you sign anything. A reverse mortgage can be complicated and isn't something to rush into.

The bottom line: If you don't understand the cost or features of a reverse mortgage, walk away. If you feel pressure or urgency to complete the deal – walk away. Do some research and find a counselor or company you feel comfortable with.

Your Right to Cancel

With most reverse mortgages, you have at least three business days after closing to cancel the deal for any reason, without penalty. This is known as your right of "rescission." To cancel, you must notify the lender in writing. Send your letter by certified mail, and ask for a return receipt. That will let you document what the lender got, and when. Keep copies of your correspondence and any enclosures. After you cancel, the lender has 20 days to return any money you've paid for the financing.