What You Need to Know Before Considering a Reverse Mortgage

The John Marshall Law School
Fair Housing Legal Support Center & Clinic
A reverse mortgage may allow senior homeowners to “age in place” and stay in their homes longer.

Reverse mortgage proceeds can provide cash:
- for long-term, out-of-pocket expenses not covered by other insurance
- to pay off an existing for-purchase mortgage, thus reducing monthly expenses
- as an alternate supplemental income source in retirement

A HECM reverse mortgage is a “non-recourse” loan, meaning the amount owed cannot exceed the market value of the house at the time the loan becomes due.

A reverse mortgage may be appropriate for seniors whose children are in a better economic situation than their parents and have little or no expectation of receiving money from their parents’ estate.

A reverse mortgage has no escrow provisions. Homeowners must budget for the annual property taxes and hazard insurance.

A non-HECM reverse mortgage loan may lack insurance to protect the borrower against default by the lender.

A reverse mortgage loan is an expensive way to borrow money. Homeowners should make sure they consider all options available to them.

The counseling required to receive a HECM reverse mortgage may not, by itself, protect borrowers from making poor choices related to choice of lenders and payment options.

Surviving spouses who were not age-qualified at the time a reverse mortgage was taken out and were not borrowers may be in jeopardy of losing their homes if the loan balance cannot be repaid from other assets upon the death of the borrowing spouse.

While reverse mortgage loans are neither good nor bad, they are legally intricate and financially complex. Potential borrowers need be sure they understand how a reverse mortgage will affect them, as well as learn about other available alternatives that might fit their specific financial situation.

To find a HUD-certified reverse mortgage counselor in your area, call the HUD Counselor Locater at 800.569.4287 or go to www.hud.gov.
In its simplest form a reverse mortgage is a means by which homeowners aged 62 or older can convert some of the equity in their home into cash. The proceeds of a reverse mortgage are a loan that must be repaid when the borrower(s) no longer live in the home. No repayment is due as long as the homeowners continue to live in the home, pay the property taxes when they are due, keep hazard insurance on the home, and maintain the property.

The proceeds of a reverse mortgage loan can be taken in one of five basic ways:

1. A lump sum of cash
2. Payments for as long as the borrower lives in the house
3. Payments for a specific term of years
4. A line of credit from which the borrower can take cash as needed
5. A combination of monthly payments and a line of credit

Currently, the only requirements for homeowners to qualify for a HECM reverse mortgage are:

- Borrowers are at least 62 years of age
- There is sufficient equity in the property to pay off any liens against the property, including any existing for-purchase mortgage loans

Borrowers should be aware that there is no escrow account for property taxes and insurance with a reverse mortgage and borrowers must budget carefully to make sure they can pay these expenses when they are due. Borrowers also must receive counseling from a HUD-certified reverse mortgage counselor before they can be approved for a HECM reverse mortgage.

The mortgage loan that most people are familiar with is a loan to purchase a home. For purposes of illustration this might be considered a “forward mortgage.” As the note is paid off, the debt decreases and the homeowner’s equity in the property increases until the debt is extinguished and the homeowner owns all the equity. This is a “falling debt, rising equity” situation. A reverse mortgage works in just the opposite way. Over the life of the loan, the loan debt increases and the homeowner’s equity in the property decreases. This is a “rising debt, falling equity” situation.
There are four key components used to determine how much equity a homeowner can convert to cash through a reverse mortgage:

1. The appraised value of the home—the higher the value, the greater the loan
2. The age of the borrower(s)—in general, older borrowers can borrow more
3. The interest rate of the loan—the lower the rate, the greater the loan
4. The manner in which the proceeds are taken

The actual calculation is complex and potential borrowers should make sure they have been thoroughly counseled on all the variables and available options. A HECM reverse mortgage is insured by the Federal Housing Administration (FHA) with insurance premiums paid by the borrower. One of a HECM’s key features is that the loan balance owed will not exceed the market value of the home when the loan is due.

A HECM reverse mortgage is insured by the FHA. This protects the borrower in the event that the lender fails to make scheduled payments to the borrower. The insurance also protects the lender in the event that the market value of the property is insufficient to pay the loan balance when the loan becomes due. The premiums are added to the loan balance and can affect the total amount of equity the borrower can convert into cash. The calculation of the mortgage premium is complex and depends on several variables.

No. As in a for-purchase mortgage loan, a reverse mortgage borrower retains title to the home. When the loan becomes due (when the youngest borrower no longer lives in the home), the home may have to be sold to pay the debt if there are insufficient estate assets to do so. Since a HECM reverse mortgage is a non-recourse loan, the amount that must be repaid cannot be more than the market value of the home at the time the loan is due.
A HECM reverse mortgage can provide financial relief for senior homeowners who have limited savings or few financial assets other than the equity in their home. The proceeds from a reverse mortgage loan can be used to supplement income, pay medical bills, or make needed repairs to the home. However, if home equity is converted to cash at the minimum qualifying age and for less critical expenditures, homeowners can be left with no financial reserves for their later years.

Yes, under some specific circumstances. Normally, the balance of a reverse mortgage loan is due only when the borrower sells the house, no longer lives in the house, or dies. However, if the borrower rents out the property, fails to pay property taxes, does not insure the house, or lets the property fall into disrepair, the lender can foreclose and the loan will become due in full.

In September 2013, the FHA reduced the total amount of equity available to be converted through a HECM reverse mortgage. They also reduced the total amount that could be paid out in the first year of the loan. These changes were made to strengthen the FHA insurance program and protect its viability. For consumers, the major effect of these two changes was a dramatic increase in the complexity of a HECM loan. It is now all the more important for potential borrowers to thoroughly understand the many variables associated with these financial products before they consider taking out a HECM reverse mortgage.
The John Marshall Law School Fair Housing Legal Support Center & Clinic

The John Marshall Law School Fair Housing Legal Support Center was established in 1992. The Center educates and trains the public on fair housing law and provides legal assistance to those private and public organizations and persons seeking to eliminate discriminatory housing practices.

The Clinic is devoted exclusively to fair housing training and enforcement. Its unique nature allows it to assist persons in receiving and retaining the housing of their choice, thereby building and strengthening neighborhoods and communities.

The John Marshall Law School
Fair Housing Legal Support Center & Clinic
315 S. Plymouth Court
Chicago, Illinois 60604

Phone: 312.987.2397 | Fax: 312.427.9438
Email: fairhousingcenter@jmls.edu

www.jmls.edu/fairhousing