The Reverse Mortgage Advantage

The Tax-Free, House-Rich Way to Retire Wealthy!

WARREN BOROSON

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Preface

Reverse mortgages are a fairly new wrinkle, and dramatic changes are sure to come in the years ahead. For instance, other lenders will probably arrive on the scene to offer such mortgages to people whose houses are above-average in value, not just average in value or extremely high in value. After all, it is not just ordinary people who may be house-rich and cash-poor; very wealthy people may be exceedingly house-rich and somewhat cash-poor. As someone has said, reverse mortgages are a work in progress. One recent important change: The Department of Housing and Urban Development now allows counselors from the National Foundation of Credit Counselors and Money Management International to provide guidance about its Home Equity Conversion Mortgage.

But reverse mortgages are certainly an idea whose time has come, despite all the myths and misinformation that have been circulating out there—myths and misinformation that, I hope, this book will help in some small measure to dispel.

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Introduction

A Most Peculiar Mortgage

If you are somewhat nervous about the whole idea of a reverse mortgage—where you borrow against your free-and-clear ownership of your home—welcome to the club!

Almost anybody would be nervous.

Besides which, a good many scary and misleading stories have been circulating about reverse mortgages (see Chapter 3). Perhaps the most common and the most nasty: A bank will take over your house, and you will wind up out on the street or perhaps living with your disgruntled children.

Not that reverse mortgages are always the best step for any older homeowner in pursuit of cash. There are reasonable alternatives, such as a home-equity loan, moving to a smaller residence in a less expensive community, or buying an income (immediate) annuity (see Chapter 5). Still, much of the time, when you add up the pros and the cons, the reverse mortgage manages to land in the winner's circle.

It is, after all, a most peculiar mortgage.

It isn't simply the opposite of a "forward" mortgage, not just a mortgage where a bank pays you instead of your paying the bank.

It is a mortgage where you can't ever be left holding the bag. Even if you get a reverse mortgage at 62 and live to 104, and the monthly payments you receive total $1 million while your house is worth only $300,000, you won't owe the bank any more than $300,000. Neither will your children or any other heirs you may have.

A very peculiar mortgage, as I said.

Yes, reverse mortgages have drawbacks. They are not a primrose path to Easy Street.

Here are some of those drawbacks:

- If you have a very expensive house, you may have trouble getting a lot of money from a government-sponsored reverse mortgage. Such reverse mortgages are for the average American, not for the Bill Gateses of the world. (But there are other reverse mortgages for the Gateses, called cash accounts. A woman with an $18 million house got one. See Chapter 11.)
- Reverse mortgages are not cheap. They come with expensive "closing costs," the money you must fork over to get the mortgage. I know a former banker, in her 80s, who took one look at the closing costs of a reverse mortgage she was applying for and snorted, "Outrageous!" She was wrong. But even leaders in the reverse-mortgage world concede that nobody ever said they were cheap.

Why aren't reverse mortgages more popular? More and more people have been getting them, but many more people would benefit. Here are some of the reasons:

- They are relatively new, dating back only a few decades.
- They are sometimes hard to understand. There are a few varieties, for one thing, and they play by somewhat different rules.
- They can be intimidating, introducing people to strange words like HECM, LIBOR indexes, and tenure periods.
- There have always been scandals involving mortgages. At one time, for example, there were "shared appreciation" mortgages. You obtained a loan on your house, and when the house eventually was sold, the lender helped himself to a percentage of the house's appreciation. Some lenders hired appraisers who deliberately under-appraised the value of a house—so that the lenders grabbed a

higher percentage of the sales price than they were entitled to. Today, shared-appreciation mortgages are typically not administered. And most reverse mortgages are carefully monitored by the U.S. Department of Housing and Urban Development to prevent any hanky-panky.

Now let us look at some good things about reverse mortgages:

- A poll of people 55 and older by the AARP found that 89 percent wanted to stay where they were living as long as possible. One of the primary benefits of a reverse mortgage is that you can remain in your house. The chances of your leaving your house against your will are very slim. To lose your house, involuntarily, you would have to stop paying the property taxes or neglect your house something awful. And when that has seemed a possibility, lenders usually step in to prevent this.
- The second major benefit of a reverse mortgage is that you can readily access cash when you need it.
- There's a good chance that your heirs will still inherit some money, even if you borrow against your house to the hilt. It's rare for houses in America to lose their value over any long time period. So, if you live in your house for any decent length of time after getting a reverse mortgage, its value is likely to appreciate—beyond the amount that you borrowed plus any interest you owe.
- Today's reverse mortgages are much simpler and more attractive than they were in the past. Today, certain expenses have limits on them. People applying for reverse mortgages must be given advice from counselors who are knowledgeable and objective. In short, it's a brand-new and far better ballgame, demonstrating why the number of reverse mortgages doubled from 2003 to 2004.
- In the early 1980s, I was writing about reverse mortgages and recall Jack Guttentag of the Wharton School, a mortgage expert, telling me what a good idea reverse mortgages were, if only they would cost less. Today they do cost less, and I will demonstrate the ways to further reduce costs (see Chapter 14).
- Finally, a reverse mortgage can make life much nicer and more comfortable for older Americans. Extra cash can mean that older

folks can more readily pay their bigger bills—their property taxes, home maintenance, and insurance. They can afford better health care and more comprehensive health insurance. They can buy newer and safer cars, dine out more often at better restaurants, take longer vacations and travel overseas, offer money for college to their grandchildren, and go to bed at night without fretting about unpaid bills.

Basically, a reverse mortgage can help older people live more comfortably and relax. The reaction I have heard again and again from people who have obtained reverse mortgages is that it was a godsend.

Thomas Scabareti, an authority on reverse mortgages, has summed it up nicely: "They are not a panacea. They are right for some people and not right for others. If you need additional income for a period of time, it's a good product. The terms are favorable, and there are great protections to let you age in place. For a lot of people, they work."

Even if you are persuaded that a reverse mortgage is just the ticket for you, or for a parent or relative, questions remain. What kind of payment do you want—a lump sum, monthly checks, a line of credit, or a combination? Which lender should you get a reverse mortgage from? And how can you keep the fees and other charges down?

In this book I have tried to provide sensible and easy-to-understand answers to these questions. As an old-timer myself, my goal is to share wisdom and tactics so that you can obtain the right reverse mortgage for your situation.

I've featured interviews with many esteemed authorities on reverse mortgages, including lenders, government officials, and people who have actually taken out reverse mortgages. (Some of the interviews with borrowers were conducted by Mia Paterno, Iris Rosendahl, Mary Linley, Bram Boroson, and Rebecca Boroson; editing was done by Matthew Boroson.)

In addition to providing practical information about reverse mortgages, I suggest how to spend the money you receive—and most importantly, how *not* to spend the money to avoid financial troubles (chapters 15 and 16). Advice is also offered to the adult children of borrowers, beginning with: Don't feel guilty if you want an inheritance (Chapter 18).

Finally, my credentials: As a former real estate agent, I have received numerous awards from prominent real estate organizations. I understand mortgages, having been a homeowner for more than 40 years. My writing includes articles on everything from the care and feeding of septic tanks (*Money* magazine) to how to bargain for a house (*New York Daily News* magazine). Books I've written on real estate include *How to Buy a House with Nothing (or Little) Down* (with Martin M. Shenkman), *How to Sell Your House in a Buyer's Market* (with Mr. Shenkman), *The Homebuyer's Inspection Guide* (with Ken Austin), *Save Thousands on Your Mortgage, Sell Your Own Home, Everything You Need to Know About Buying a House (in 60 Pages)*, and *Buying and Selling a House in a Changing Market.*

As you proceed through the reverse mortgage selection process, I would be pleased to hear from you, learn about your own experiences, and answer any questions you may have. Feel free to e-mail me at: WarrenBoroson@aol.com.

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Reverse Mortgages for Total Beginners

Here are several questions that people have asked about reverse mortgages, along with the answers.

Can you explain what a reverse mortgage is so that I can finally understand it?

I knew a violinist with the New York Philharmonic who had most of his financial assets in two rare violins: a Stradivarius and a Guarnieri. They were worth, together, over $1 million. But his portfolio, while noteworthy, was not diversified. If the market for rare violins sank, his worldly wealth would have been devastated.

His portfolio was also illiquid; if he needed cash, it's doubtful that he could quickly sell one of his violins for a reasonable price.

A house is like that. Valuable and illiquid. If you are willing to take a big loss, you could probably find a buyer in no time, but, even so, getting your hands on the money would still take months.

Assuming that the violinist needed cash, he might have obtained a loan, with his violins as collateral. He would receive money—and he would still own those violins, which he needs for his job.

That's what homeowners with reverse mortgages have done—obtained a loan secured by their houses. But they must eventually repay the loan, with interest.

Will I still own my house?

Absolutely!

"That's the No. 1 question people ask me," says Sarah Hulbert, senior vice president, national director, of Seattle Mortgage Company's Reverse Mortgage Division, "and for 14 years I've been giving the same answer. Of course you will."

This is the most pernicious myth about reverse mortgages—that a bank or the government will end up owning your home sweet home.

When Bill Agner, director of reverse mortgages for the Mortgage Network in Indianapolis, gives a talk, an unhappy listener will invariably say to him afterwards, "Yeah, you get a few bucks, and then they take your home."

Fortunately, people seem to be becoming better informed. These days, when Mike Gruley, president of First Financial Mortgage Corp. in Northville, Michigan, asks audiences how many people believe that banks will wind up owning the homes of borrowers with reverse mortgages, only 5 percent raise their hands. Not long ago, it was 80 percent.

Well, yes, it's possible that you can lose your house. In very unusual situations—if you don't pay the property taxes or keep up your homeowners insurance, or if you let your home deteriorate badly (we're not just talking about ordinary wear and tear).

But Gruley notes that lenders will be very cautious when it comes to evicting people from their houses; a lender needs the Department of Housing and Urban Development's permission to do so. "And HUD is unlikely to kick an old widow out of her house," he says. The publicity would give the entire reverse-mortgage industry, still in its infancy, a hurt that would not heal quickly.

In fact, no one I have interviewed knows of anyone who has obtained a reverse mortgage and wound up being evicted. If a borrower does fall behind on property taxes or insurance, lenders may pay the bills themselves—by lowering the amount being loaned to the homeowner.

Who can get a reverse mortgage?

Someone 62 or older with a house that is his or her main residence and who has received counseling and has a certificate to prove it.

Who should get one?

One ideal candidate is someone who is "house-rich and cash-poor." Like the man with the two violins. And anyone with a continual need for money, not just a colossal need right now. "Continual" is the key word. Other ideal candidates are people who *want* cash—to live a more comfortable life. They are not the same as people who *need* cash.

Where do you get a reverse mortgage?

The big three: the Department of Housing and Urban Development is behind the Home Equity Conversion Mortgage (HECM); Fannie Mae has its Home Keeper; and Financial Freedom has its Cash Account.

For a free list of reverse mortgage lenders and certified loan-counseling agencies, contact HUD at 888-466-3487. For information about lenders that offer Fannie Mae Home Keeper reverse mortgages, call 800-732-6643. For information about Financial Freedom Cash Accounts, call 888-REVERSE. Also, the National Reverse Mortgage Association Act at 1-866-264-4466.

How much can I get?

That depends on your age, the value of the house, and the level of interest rates. The older you are, the more valuable the house, and the lower interest rates are, the more you can borrow. In 2006, the maximum lending limits were:

HECM = $200,160 (mostly rural areas) to $362,790 (urban)

Fannie Mae Home Keeper = $417,200

Financial Freedom Cash Account = No set limit

Who should not get one?

First off, someone thinking of living in a house for only a few years—such as a person planning to move to a warmer climate soon. Reason: those closing costs may not have been worth it.

This example has been calculated by the National Center for Home Equity Conversion: A 75-year-old widow gets a $150,000 reverse mortgage, folding the $6,500 closing costs into the loan. She then begins receiving a monthly income of $562. Two years later, she moves to a nursing home. Over two years, the monthly income she received was $13,488. Considering the closing costs and the interest she owed, her effective interest rate was almost 50 percent. But if she had lived in the house for 12 years, receiving $80,928, the effective interest rate would have dropped to 10.8 percent.

Why the age of 62?

Perhaps because most Americans retire at age 62. Also, as Sarah Hulbert points out, people under 62 have such long life expectancies that the size of the loan available to them might not be significant.

Why have reverse mortgages not become more popular?

In many cases, widows are the ideal borrowers, but they tend not to be knowledgeable about finance and therefore are full of trepidation because their late husbands handled all the finances. With a widow, says Agner, "We try to bring in other family members to help her."

Another reason is that older people tend to be dubious about debt. They remember the Depression, when banks foreclosed on houses right and left. And not long ago these same homeowners celebrated when their mortgages were finally paid up. (In the old days, there were actually mortgage-burning parties.) No wonder that people in their 60s or older become anxious at the thought of obtaining a new mortgage.

Baby boomers, people born right after World War II, are more open to the idea. They are the credit card generation, and debt has never daunted them.

Not only that, but Joseph DeMarkey, vice president of the Bank of New York Mortgage in Milford, Massachusetts, believes they are not so intent on leaving a large estate. Whereas many older people want to leave their houses to their children.

John Curtis, Wells Fargo home mortgage area manager in the Minneapolis area, reports that the children may be living in $500,000 houses and making $500,000 a year, but their parents want these kids to inherit the family homestead. He asks these parents: "Did your own mom and dad leave you anything?" "Nope." He winds up advising them to take care of themselves. (*Minneapolis Star Tribune*, Sept. 7, 2002)

Still another reason that reverse mortgages are not more popular is that the subject is complicated. You have a variety of choices, and there are darned few easy answers. One counselor, Stephen Pepe of the Community Service Network in Stoneham, Massachusetts, tells me that many of his clients ask him, "If your parents applied for a loan, what would you tell them?" His sensible answer: it depends on their situation.

Do people use the money frivolously?

In places where house prices have soared, an increasing number of people do use their extra money for luxuries, like trips down the Amazon or to buy expensive Ferraris. In Seattle, reports Sarah Tyndal, a counselor with Pierce County Community Service, people with reverse mortgages have bought season tickets to Seattle Mariners baseball games for their whole family. But in less fortunate areas like Michigan, says Mike Gruley of First Financial Mortgage, perhaps one or two out of a hundred do.

In any case, frivolity is in the eye of the beholder. If someone is wealthy, why not take a little flier? I occasionally meet elderly people who are well heeled but timid about spending a dime. I tell them: Enjoy a night at the opera! Take some friends to the Four Seasons restaurant! Live it up a little!

Joseph DeMarkey recalls a borrower in the Northeast intent on becoming a snowbird. He used a lump sum reverse mortgage to buy a second home in Florida. Other borrowers have told him that they plan to take around-the-world cruises.

Sarah Hulbert says that most people use the money from reverse mortgages to pay off their existing mortgages and pressing bills, and in general to subsidize their retirement. But in one case, a mother was well-to-do, and so was her son. He didn't need money. So she obtained a reverse mortgage and, at his suggestion, went on an around-the-world cruise—for a full year. "She was 85 years old at the time, and she told me that the trip was fantastic."

John Curtis of Wells Fargo Home Mortgage closed a reverse mortgage for a 90-year-old man who wanted to buy a new car. According to Curtis, "He said, 'I want to get a PT Cruiser.' He wanted to do it because he had a girlfriend." Then there was the 90-year-old man in New Jersey who bought a Ferrari because, he explained, his 50-year-old girlfriend thought he looked good in it.