



THE FHA REVERSE MORTGAGE PROGRAM: A MAJOR OPPORTUNITY TO HELP AMERICA'S SENIORS

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Updated June 12, 2009

I. The FHA Home Equity Conversion Mortgage Program

The Home Equity Conversion Mortgage (HECM) is the nation's oldest and most popular reverse mortgage product, accounting for virtually all reverse mortgages made in the U.S. The HECM is insured by the Federal Housing Administration (FHA), an arm of the U.S. Department of Housing and Urban Development (HUD).

The HECM has been available since 1989 to homeowners 62 or older. Eligible property types include owner-occupied 1- to 4-family homes, manufactured homes, condominiums and townhouses. HUD is currently implementing regulations that would allow HECMs on cooperative units.

The amount of funds that a homeowner is eligible to receive from a reverse mortgage depends upon: (1) the person's age (or age of the youngest borrower in the case of a couple); (2) the value of the home; (3) current interest rates; and (4) the FHA lending limit, which was raised in 2008 to \$417,000 nationwide. For the balance of 2009, Congress raised the loan limit to \$625,500.

Borrowers can choose to receive the proceeds as (1) a upfront lump sum payment, (2) fixed monthly payments (for a set period; or, for as long as the borrower occupies the home), (3) a line of credit, or (4) a combination of these.

As a safeguard, all prospective borrowers must receive counseling from a HUD-approved, nonprofit housing counseling agency before they can apply for a reverse mortgage. Upon completion of the counseling session, the borrower and counselor must sign the certificate before it's presented to the lender.

The fee that a lender charges is limited by HUD rules. The origination fee is equal to 2% on the initial \$200,000 of maximum claim amount (lesser of the home value or county lending limit) and 1% on the balance thereafter with a cap of \$6,000. The full origination fee, as well as other closing costs, may be financed as part of the HECM. This means a senior incurs very little out-of-pocket expense to get a reverse mortgage.

Borrowers must also pay an FHA insurance premium, equal to 2 percent of the loan amount upfront, plus an annual premium thereafter equal to 0.5 percent of the loan amount. The MIP guarantees that if the company managing the borrower's account – commonly called the loan "servicer" – goes out of business, the government will step in and make sure the client has continued access to loan funds. Furthermore, the MIP guarantees that the borrower will never owe more than the value of the home when the property is sold to pay back the HECM.

Interest rates can be fixed or adjusted either monthly or annually (the borrower chooses) and based on an index called the 1-year U.S. Treasury Constant Maturity Rate published weekly by the Federal Reserve. Both the monthly and annually adjusted rates have lifetime caps.

More recently, HUD added the 1-month and 1-year London Interbank Offered Rate (“LIBOR”) as acceptable indices for calculating the interest rate on federally-insured reverse mortgages.

The monthly or annual adjustments don’t alter the monthly payments that borrowers can receive (if they have chosen the monthly payment option). Instead, the adjustment affects the total interest that is charged on the loan, which is added to the loan balance while the loan is outstanding and is paid when the loan becomes due.

A borrower is not required to make any mortgage payments to the lender during while the loan is outstanding. The HECM becomes repayable, in full, when the sole remaining borrower dies or no longer occupies the home as his or her principal residence (e.g., through a sale of the home or a permanent move out). The repayment obligation is equal to the sum of the total funds advanced to the borrower, plus interest and any closing costs and other charges financed as part of the loan.

Typically, the home is sold to pay back the reverse mortgage, but the heirs or estate have the option to keep the home and use other funds to retire the debt. If the home sells for more than the amount owed, the excess equity is retained by the borrower or the heirs/estate. If the home sells for less than the amount owed, FHA absorbs the shortfall, thus guaranteeing that the borrower never owes more than value of the home. If, however, the family chooses to keep the home, FHA requires the entire balance to be repaid, even if the amount exceeds the home’s value.

About 1,600 FHA-approved lenders are currently involved in the origination and/or purchase of HECMs. Most of these are correspondents who sell the loans to one of a small number of major lenders who fulfill a role in the industry as “seller/servicers.”

II. Why HECM is an important program

Today over 34 million Americans are over age 65.¹ This is expected to double in the next 30 years to almost 70 million.² By 2030, 20 percent of Americans will be over age 65.³ Almost four out of five seniors own their own homes, meaning that there are about 27 million senior homeowners today, and that number will rise in the future. Seniors of all races have the highest rates of homeownership.⁴

In addition, senior homeowners have a lower median income than any other demographic group (\$23,311 for seniors, and \$43,581 for all homeowners nationwide), yet seniors have the *highest* median home equity (\$80,000 for seniors, compared to \$57,000 for all homeowners and only \$19,000 for homeowners under age 35).⁵ This indicates that conversion of home equity into income could significantly increase the relatively low incomes of senior homeowners.

¹ U.S. Bureau of the Census, Current Population Reports.

² Ibid.

³ Ibid.

⁴ “Housing Our Elders: A Report Card on the Housing Conditions and Needs of Older Americans,” HUD, November 1999.

⁵ The State of the Nation’s Housing 2000, Harvard University Joint Center for Housing Studies.

This is obviously important from a public policy perspective. Seniors are a large and growing segment of the population. As seniors age, their incomes do not generally increase, while their needs do. Homes need repairs and accessibility improvements, chronic illnesses require ongoing treatment and expensive prescription drugs, cars wear out and must be replaced with more expensive ones, and people with declining mobility may need more daily help with household tasks. Seniors who cannot afford these growing expenses either forego them—thereby, sacrificing quality of life, independence, and even their health—turn to families, who are often hard pressed to help; take out expensive home equity loans, which must be repaid on a current basis; seek government assistance; or sell their homes in order to access their home equity. Studies by AARP have shown that seniors will sacrifice considerable quality of life in order to remain in their homes for as long as possible.⁶

Reverse mortgages offer an ideal way to avoid these dire consequences while maintaining seniors' desired independence in their own homes. Seniors do not have to repay the loans until they die or move out of the home. They can never owe the lender more than the home is worth when the loan is due. They can use the money in almost unlimited ways, and with payment plans that can be tailored to suit their needs and financial goals. Reverse mortgages can also save the federal government money through reduced demand for health care and other benefits. Proceeds from reverse mortgages can be used to:

- pay for home repairs, cost-saving energy improvements, and improvements to accessibility that can prevent injuries;
- pay for ongoing in-home health care, so the senior can avoid expensive government-paid hospitalization or nursing home care;
- pay for one or more new or used cars, or a wheelchair-accessible van;
- pay for expensive prescription drugs that may not be covered by any government or private insurance plan;
- pay for motorized wheelchairs and other life-enhancing equipment that Medicare or private insurance may not pay for;
- many other uses that can help seniors maintain their dignity, avoid asking hard-pressed children for help, and enjoy life.

In addition to helping seniors who wish to stay in their present homes, FHA implemented a new program called HECM for Purchase, which allows qualified borrowers to use a reverse mortgage to purchase a new home that better suits their needs.

III. HUD's Responsibility

The advantages for seniors, their families, and the government of a robust reverse mortgage program are clear. The HECM is the dominant reverse mortgage product in the market and

⁶ Fixing to Stay, AARP, May 2000.

HUD can help promote the program to make reverse mortgages widely available to as many seniors as possible. Congress has clearly expressed great interest in the program, particularly its potential to help seniors afford long-term care, thereby helping to reduce the millions of dollars in eventual federal expenditures for seniors' health care needs.

The Centers for Medicare and Medicaid Services, a federal agency within the Department of Health and Human Services, and the Robert Wood Johnson Foundation funded a study by the National Council on Aging (NCOA) that explores the potential of encouraging seniors to utilize their home equity to cover their long-term care needs. In 2000, the nation spent \$123 billion a year on long-term care for those age 65 and older, with the amount likely to double in the next 30 years. Nearly half of those expenses were paid out of pocket by individuals and only three percent were paid by private insurance; government health programs pay the rest.

NCOA's report—titled *Use Your Home to Stay at Home: Expanding the Use of Reverse Mortgages to Pay for Long Term Care*—showed that reverse mortgages can help an estimated 13.2 million elderly homeowners pay for long-term care, allowing many to remain independent in their homes longer. Of the 13.2 million eligible households, an estimated 9.8 million currently have an impairment that can make it hard to live at home.

In total, these households could access as much as \$695 billion in home equity through reverse mortgages. For individuals, the extra cash could go a long way to help with family caregiving and other long-term care expenses. For example, a borrower aged 75 years old with a home worth \$100,000 could receive a reverse mortgage that could pay a family caregiver \$500 a month for almost 12 years; \$1,120 a month in adult day care services for almost five years; or \$2,160 a month in home care—daily care for at least four hours—for 2.5 years.

But, despite the huge potential market, and the clear public policy advantages of the HECM program, the program remains under-utilized. Since the program's inception, almost 530,000 HECM loans have been originated⁷. HUD has, on occasion, touted the potential for the program, but the updating and modernizing of the program that is required has not been allowed to take place

IV. Proposals for Action to Improve the FHA HECM Program

The nation's reverse mortgage lenders have worked tirelessly since 1989 to make the HECM program widely available and understood. Over the past couple years, NRMLA has worked closely with HUD officials and Congress to make substantial improvements, which include the following:

1.) Approve \$798 million credit subsidy in HUD's 2010 budget.

The Department of Housing and Urban Development has requested \$798 million in its proposed 2010 budget to support the HECM program. If these funds are not approved, HUD may have to increase FHA insurance premiums charged to seniors, or restrict

⁷ HUD Statistics Through April 2009

eligibility to the program. In these challenging economic times, it's difficult to justify increasing upfront costs to seniors or restricting access to reverse mortgages for those seniors who need funds the most to cover retirement expenses.

2.) Implement a permanent lifting of the cap on the number of HECM loans that FHA is authorized to insure.

Without legislation, the FHA can only insure 275,000 HECM loans. Right now, the cap is under suspension, but a more permanent solution is needed.

3.) Make the HECM single national loan limit of \$625,500 permanent

The economic stimulus plan approved by Congress this past spring raised the single national loan limit for HECMs from \$417,000 to \$625,500, with the stipulation that the new limit would expire on December 31, 2009.

The \$625,500 loan limit should be made permanent. While we understand the intent of the economic stimulus law is to provide short-term solutions to help jumpstart the economy, the higher loan limit is already having a dramatic positive impact on elderly households. Many seniors who previously could not qualify for a reverse mortgage because they didn't have enough equity are now able to pay off existing mortgages and avoid foreclosure, or refinance existing HECMs and obtain additional funds to help pay for critical retirement needs that enable them to stay in their homes.

4.) Increased Funding for Counseling

As a reminder, all prospective borrowers must receive counseling from a HUD-approved, nonprofit housing counseling agency before they can apply for a reverse mortgage. Historically, counseling was funded by a combination of a direct appropriation (roughly \$3-4 million annually), financial contributions from lenders to counseling agencies, and, more recently, a new provision implemented by HUD that allows borrowers to pay for the counseling. (For a sense of magnitude, counselors conducted approximately 130,000 counseling sessions in FY'08 at a cost of \$125 each, for a total of \$16,250,000).

With the passage of the Housing and Economic Recovery Act last year, lenders are now prohibited from helping to pay for counseling.

When borrower-paid counseling was first discussed, the thinking was that the counseling fees could be paid from borrowers' loan proceeds, once loans were closed and disbursed. However, it can take several months between the time a homeowner is counseled and when the loan actually closes. A number of counseling agencies said that they could not afford to wait the few months between providing counseling and loan closing to get paid and so began charging prospective borrowers upfront. This caused a hardship for some consumers and deterred others from seeking HECMs.

Counseling agencies are also supposed to provide counseling at no cost to clients who demonstrate “hardship,” but it has been left up to each individual agency to determine its policy for doing this. Appropriated funds are now generally being used to pay agencies for hardship cases, as well as to pay for those sessions that do not result in a loan. But current appropriations still fall short of the need.

A solution we’ve discussed with congressional staff is to seek an appropriation that would be sufficient to cover the full amount of counseling, so agencies can be paid at the time of counseling for all sessions. Borrower payments, from funds disbursed at closing, could then be paid into a fund to replenish part of the appropriation. In subsequent years, appropriations could be sought to pay for the hardship cases and fall-out cases, and payments from borrowers would cover those sessions that do result in loans.

V. Conclusion

A healthy, active HECM program could be a key component for helping seniors take control over their financial situation. Reverse mortgages are a promising way to unlock billions of dollars in home equity, providing financial security, independence, and great improvement in the quality of life for thousands of senior homeowners and their families. Wider acceptance of reverse mortgages can mean reducing the need for costly increases in federal spending on health care and other benefits for seniors in the future. Because the FHA HECM program is the primary source of reverse mortgages, Congress and HUD should work more closely with the reverse mortgage industry to make needed program changes and devote greater effort to managing and promoting the program. This will result in more senior homeowners enjoying the benefits of this outstanding program. NRMLA and all its member lenders stand ready to assist Congress and HUD in this vitally important effort.