The Truth About Reverse Mortgages

The Need for Home Equity Conversion Mortgages (HECM)

Over half of homeowners in their 60's and beyond have little or no savings, and a large number still have mortgages on their homes. More and more of this group are continuing to work to pay the bills, but, even for these folks, there will be a time when they have to stop working. Social Security alone is not enough. Many people are going to need more money to have a comfortable lifestyle, and some just to survive.

Reverse Mortgages were established to help these people stay in their homes while using some of the equity to make their lives better.

The idea behind a reverse mortgage is relatively simple. Figure out how much money you can give a homeowner today, so that when the interest is added to it each month, the loan is not larger than the projected value of the property in the future, when a person the homeowner's age may die.

The amount you receive is determined by applying government provided factors to the appraised value of the home at the time the loan is made. These factors increase according to your age. Currently, at age 62 you would receive 52% of the home value, and at 90 or older 75%.

The HECM Loan has FHA Insurance for two purposes: 1. guarantee homeowner's proceeds, and 2. so investors will buy the loans.

The FHA can't just insure any amount, so they limit the maximum amount a homeowner can receive to a percent of the home value or $625,500, whichever is less. For example: a 62-year-old with a home value of one million would receive 52% of $625,500, not 52% of the one million.

Jumbo Reverse Mortgages – Are Non-FHA insured loans designed for larger home values. Currently, they yield from 21% to 50% of the home value. For example, 62-year-old with a home value of $4,000,000, could get 21% of the home value or $840,000.

How have people been hurt by reverse mortgages?

1. Widows have lost their homes because they were taken off the title when their husband got a reverse mortgage.

2. Foreclosures were triggered due to unpaid taxes. These folks spent their money and did not make sure they had enough to pay the taxes and insurance going forward. This would have happened with any type of loan.

3. People were tricked into purchasing an annuity with their reverse mortgage money.

4. People were led to believe that the money never had to be paid back.

5. As with any type of mortgage, people take the loan, use the money, and then complain that there is not enough equity in their property when they go to sell. They forget that they had use of the money.

How many people have reverse mortgages?

From the year 2000 to the present, **947,593** homes have HECM Reverse Mortgages, and there have been about 33,000 taken out by homeowners already this year.

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The Facts – Home Equity Conversion Mortgage

Notes

1. The property title stays in your name. The bank does not own your home.

2. It is called a "Reverse Mortgage" because, during the life of the loan, money flows FROM the bank TO you, unlike traditional loans, with payments, where the money flows TO the bank FROM you every month.

3. There are no monthly loan payments required, but there is one payment due at the end of the loan.

4. A reverse mortgage comes due when the home is no longer your primary residence. For many this is due to their death, but there could be other reasons like selling and moving. Also, with a reverse mortgage, the loan could come due for non-payment of taxes, insurance, HOA dues if applicable, or not keeping the home livable.

5. Your heirs can have up to one year to sell the property and settle the loan. This is to prevent them from being forced to sell the property quickly and take a lower amount. Your heirs choose what they want – sell and keep the money, or pay off or refinance the loan and keep the property.

6. Non-Recourse Loan – The home alone stands for the debt.

7. No Prepayment Penalty -You may sell and move or refinance at any time without any prepayment penalty.

8. There are no restrictions on what you can do with the money.

9. Ways to receive your money – All of most at one time. Monthly payments for life or a period of years. A line of credit to take the money when and if you need it. Or a combination of these.

10. Loan Interest Rates –The majority of HECM reverse mortgages are Open-End loans, meaning money does not need to be taken up front. It's available during the life of the loan. These have variable interest rates, which are based on the LIBOR Index plus a Margin and are in line with traditional mortgages. Some reverse mortgages are Closed-End loans, where you take all money at the beginning, and no more after that. These loans have a fixed interest rate that is usually higher than traditional loans with monthly payments.

11. Qualification – At least one of the homeowners must be 62 or over, and must demonstrate that he/she is able to pay the taxes, insurance, HOA dues, and maintain the home in livable condition. This is shown with a credit check and simple financial qualification. The homes are limited to Single Family Residences, 2, 3, or 4 unit homes, and HUD-approved condominiums and manufactured homes that meet FHA requirements are also eligible.

12. The reverse mortgage has no effect on Social Security or Medicare, and since it is money from a loan, it's not taxable.

The Costs Involved with a Reverse Mortgage

Notes

The first thing to know about the costs is that normally the homeowner doesn't pay them out of their pocket. They are simply added to the loan, because a reverse mortgage is made to help people by putting money in their bank account, not take money out.

There are costs involved, of course, just as there are with any loan – the escrow fee, title insurance, filing fees, appraisal cost, sometimes origination fee, and other normal fees as with any loan.

Sometimes the largest cost is the FHA Insurance Fee. This happens if the homeowner needs to use over 60% of the amount available during the first year. Then 2.5% of the home value (with the $625,500 limit) is added to the costs. However, the fee is quite low when less than 60% is used. It is only ½ of a percent or 0.5%.

The cost of a loan is determined by adding the up-front costs to all the interest paid for the entire time of the loan. This is how the APR is calculated. APR is what is used to comparing loan costs.

Is the reverse mortgage an expensive loan? –

It can be an expensive loan if two things happen together.

1. If you need to use more than 60% of the money in the first year,

And

2. You only have the loan for a short period of time - like 2 or 3 years.

If you use a reverse mortgage the way it was intended to be used, the costs are spread over the time of the loan, and are comparable to traditional mortgages.

The Wonderful Reverse Mortgage Line of Credit

The line of credit is money you haven't borrowed, but you have access to it if you need or want it in the future, and it is not dependent on your home value.

Growth Factor – The amount in your line of credit grows at 1.25% more that the current interest rate of your loan. As example: if your loan was 3%, you had $100,000 in your line of credit, and you didn't need it for 10 years, it would grow at 4.25% compounded - you would have $152,844 available in 10 years.

Uses for the line of credit – Social Security maximization, building retirement funds for larger distributions, protection against downturns in the stock market, home modifications for access, home care, and unexpected expenses are just a few ways homeowners have used the reverse mortgage line of credit.