Reverse Mortgage Loans

Borrowing Against Your Home

AARP®

AARP does not endorse any reverse mortgage lender or product, but wants you to have the information you need to make an informed decision about these loans and other, less costly, alternatives.

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*An online version of this booklet is available at www.aarp.org/revmort.

Reverse Mortgage Loans: Borrowing Against Your Home

October 2010 Update

Since the publication of this booklet in 2008, there have been a number of important changes in the reverse mortgage world. The following is a summary of these issues, as they affect the content of this book as of October 2010. Page numbers are provided to help you find the areas of the book that are affected by these changes.

Property eligibility: Though legislation to allow HECM loans on cooperatives was passed, the enabling regulations have not been finalized, so as of this time (October 2010), cooperatives are still not eligible. (page 8)

Home value limits: The nationwide home value limit of $417,000 on HECM loans was raised to $625,500 and will continue at that level until at least December 2011. This increase made HECMs more attractive for borrowers with higher value homes, and is one reason for the disappearance of proprietary loans. (pages 9, 26, 32)

Loan amounts: HUD reduced the percentages of home value that can be borrowed, as of October 1, 2009. For example, prior to October 2009, a 62-year-old homeowner could borrow about 62% of their home value in a HECM loan. After the 2009 change, they could get about 56%. Similar changes were put in place at all age levels. On October 4, 2010, another set of changes went into effect, with more complicated results. In general, loan limits were reduced by another 1-5 percent. However, for some borrowers with low interest rates, loan amounts increased compared to 2009. These changes affect estimated loan amounts throughout this book, such as the tables on page 10 and 11, and examples on pages 9 and 15.

Origination fee: Limits on origination fees have not changed, but the willingness of lenders to reduce or even eliminate origination fees has changed dramatically. Since April 2010, some lenders are waiving or reducing origination fees on many of their loans. Be aware that some lenders offer the lower origination fee in exchange for a higher interest rate, and some offer lower origination fees only on lump-sum loans, so make sure you get the details. (page 13)

Servicing fees: As with origination fees, lenders have recently begun reducing or eliminating monthly servicing fees on many loans. When comparison shopping for a lender, it pays to ask about a $0 service fee, as this can increase available loan proceeds by several thousand dollars. As with origination fees, lower service fees may be offset by higher interest rates in some cases. (page 14)

Mortgage insurance premiums: Beginning October 4, 2010, the annual mortgage insurance premium on all HECM loans increased from 0.5% per year to 1.25% per year. (pages 13, 14, 15, 16)

Creditline growth rate: Because of the increase in the annual mortgage insurance premium, the creditline growth rate will now be the interest rate + 1.25%. (page 10)

Fixed interest rates: Fixed rates became much more widely available beginning in early 2009, and many lenders are offering moderately low fixed rates at this time. It is still the case that lenders typically require a 100% lump sum draw as a condition of offering the fixed rate option —that is, the borrower must take all available loan funds at closing. (page 27)

Adjustable interest rates: Rates that adjust only once a year stopped being widely available in September 2009. At the present time, adjustable-rate HECMs are all monthly adjustable, and nearly all are based on the LIBOR index, which is more volatile than the 10-year Treasury rate that has been historically used as the basis for HECM loans. (page 27)

HECM for Purchase: A new variation on the HECM program that began in 2009, the HECM for Purchase allows a borrower to use a HECM to purchase a new home, rather than borrowing against a home they already own. Loan-to-value percentages are the same as for regular HECMs. The borrower can use the HECM to pay for part of the purchase, and then would have to bring a downpayment equal to the remaining cost of the home. For example, a 62-year-old borrower who wanted to buy a $200,000 home could get about $112,000 from a HECM, and then would have to pay about $88,000 plus closing costs using their own funds. Borrowers must make their new homes their principal residence within 60 days of closing the loan.

HECM Saver: Another variation on the HECM went into effect on October 4, 2010. The HECM Saver product has a much lower upfront mortgage insurance premium (0.01% compared to 2%), but offers loan amounts that are 10-18% lower than the traditional HECM, which is now called the HECM Standard. This product is designed for people who want to borrow a smaller amount of money. Also, since the upfront costs are lower, it can be more appropriate for those who expect to move or sell the home within a few years.

Non-HECM reverse mortgages: Proprietary, or privately insured, reverse mortgages (those that are not FHA-insured HECM loans) nearly vanished from the marketplace during the recession. At this time, only a few products are available, mostly for very high-value homes. (pages 8, 20, 26)

Reverse mortgage counseling: All HECM counselors are now required to pass an exam and receive specialized education in order to be HUD-approved. A searchable list of agencies with approved HECM counselors can be found at: **https://entp.hud.gov/idapp/html/hecm_agency_look.cfm**. (page 25)

Preparing for counseling: As of September 2010, all HECM counselors are required to send a packet of information to each client, and allow time for the client to review it, before the counseling session can take place. This packet will include individualized loan estimates and other materials. "Emergency" or same-day counseling is only available in cases of financial or medical emergency. (page 25)

Selecting a lender: As noted above, there is now more variation among lenders with respect to loan costs. Be sure to ask about servicing fees, origination fees, and 3rd party costs. Some lenders are even offering to pay the initial mortgage insurance premium on the client's behalf. If you are considering an adjustable rate HECM, be sure to ask about the "margin"—this is the part of the rate that the lender actually controls.

Note that some lenders will offer reduced fees only on the fixed-rate products with the lump-sum draw requirement. Others will offer reduced fees on both fixed and adjustable-rate products. Don't let yourself be talked into borrowing more money than you need, just to get lower upfront fees—a lump-sum draw can cost you a lot more money in the long run! (page 28)

Reverse Mortgage Loans: Borrowing Against Your Home

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Part 1: Basic Questions

Here are five important questions to keep in mind when reading this booklet:

1) Do you really need a reverse mortgage?
2) Can you afford a reverse mortgage?
3) Can you afford to start using up your home equity now?
4) Do you have less costly options?
5) Do you fully understand how these loans work?

1) Do you really need a reverse mortgage? Why are you interested in these loans? What would you do with the money you would get from one? Are the needs you intend to meet really worth the high cost of these loans?

If you want to take that dream vacation, a reverse mortgage is a very expensive way to pay for it. Investing the money from these loans is an especially bad idea because the loan is highly likely to cost more than you could safely earn.

If anyone is trying to sell you something and recommending you use a reverse mortgage to pay for it, that's generally a good sign that you don't need it and shouldn't be buying it. Be especially wary if you don't fully understand what they are selling or aren't certain that you need it.

2) Can you afford a reverse mortgage? These loans are very expensive, and the amount you owe grows larger every month. The younger you are when you take out a reverse mortgage, the longer compound interest will grow and the more you will owe. On the other hand, due to high upfront costs, reverse mortgages can be especially costly if you sell and move just a few years after taking one out.

3) Can you afford to start using up your home equity now? The more you use now, the less you will have later when you may need it more, for example, to pay for future emergencies, health care needs, or everyday living expenses—especially if your current needs grow or your income does not keep pace with inflation. You may also need your equity to pay for future home repairs or a move to assisted living.

If you are not facing a financial emergency now, then consider postponing a reverse mortgage. Homeowners who decide to wait have "a reasonable expectation of securing a better product at a lower cost in the not-too-distant future," according to a report by the Fidelity Research Institute.

4) Do you have less costly options? Do you have other financial resources

that you could use instead of taking out a loan? If you don't, and if you could easily make the monthly repayments on a home equity loan or home equity line-of-credit, these alternatives are much less costly than a reverse mortgage.

Many state and local governments offer very low-cost loans for paying your property taxes or making home repairs. Have you checked at **www.aarp.org/quicklink** to see if you are eligible for federal, state, local and private programs that help pay for prescription drugs, utility bills, meals, health care and other needs?

Have you seriously looked into the costs and benefits of selling your home and moving to a less expensive one? You just might find that you may prefer living somewhere else with lower costs or more services.

5) Do you fully understand how these loans work? Reverse mortgages are quite different from any other loan, and the risks to borrowers are unique. Before considering one, you need to do your homework carefully and thoroughly. A reverse mortgage is a major financial decision, and you can't afford to find out too late that you misunderstood or were not aware of any important facts about these loans.

Read this entire booklet. Then, for more information and answers to your questions, request a reverse mortgage counseling session as described in Part 5 of this booklet. If the counselor doesn't know the answers to all of your specific questions, request counseling from a different counselor or agency.

Part 2: Introducing Reverse Mortgages

Until recently, there were two main ways to get cash from your home: you could sell your home, but then you would have to move; or you could borrow against your home, but then you would have to make monthly loan repayments.

Now there is a third way of getting money from your home that does not require you to leave it or to make regular loan repayments.

"Reverse" Mortgages

A "reverse" mortgage is a loan against your home that you do not have to pay back for as long as you live there. With a reverse mortgage, you can turn the value of your home into cash without having to move or to repay a loan each month.

The cash you get from a reverse mortgage can be paid to you as:

- a single lump sum of cash;
- a regular monthly cash advance;
- a "creditline" account that lets you decide when and how much of your available cash is paid to you; or
- a combination of these payment methods.

No matter how this loan is paid out to you, you typically don't have to pay anything back until you die, sell your home, or permanently move out of your home. To be eligible for most reverse mortgages, you must own your home and be 62 years of age or older.

Other Home Loans

To qualify for most home loans, the lender checks your income to see how much you can afford to pay back each month. But with a reverse mortgage, you don't have to make monthly repayments. So you don't need a minimum amount of income to qualify for a reverse mortgage. You could have no income, and still be able to get a reverse mortgage.

With most home loans, if you fail to make your monthly repayments, you could lose your home. But with a reverse mortgage, you don't have any monthly repayments to make, so you can't lose your home by failing to make them.

Reverse mortgages typically require no repayment for as long as you—or any co-owner(s) of yours—live in your home. So they differ from other home loans in these important ways:

- you don't need an income to qualify for a reverse mortgage; and
- you don't have to make monthly repayments on a reverse mortgage.

"Forward" Mortgages

You can see how a reverse mortgage works by comparing it to a "forward" mortgage—the kind you use to buy a home. Both types of mortgages create debt against your home and affect how

much equity or ownership value you have in your home. But they do so in opposite ways.

"Debt" is the amount of money you owe a lender. It includes cash advances made to you or for your benefit, plus interest. "Home equity" means the value of your home (what it would sell for) minus any debt against it. For example, if your home is worth $150,000 and you still owe $30,000 on your mortgage, your home equity is $120,000.

Falling Debt, Rising Equity

When you purchased your home, you probably made a small down payment and borrowed the rest of the money you needed to buy it. Then you paid back your "forward" mortgage loan every month over many years. During that time:

- your debt decreased; and
- your home equity increased.

As you made each repayment, the amount you owed (your debt or "loan balance") grew smaller. But your ownership value (your "equity") grew larger. If you eventually made a final mortgage payment, you then owed nothing, and your home equity equaled the value of your home. In short, your forward mortgage was a "falling debt, rising equity" type of deal.

Rising Debt, Falling Equity

Reverse mortgages have a different purpose than forward mortgages do. With a forward mortgage, you use your income to repay debt, and this builds up equity in your home. But with a reverse mortgage, you are taking the equity out in cash. So with a reverse mortgage:

- your debt increases; and
- your home equity decreases.

It's just the opposite, or reverse, of a forward mortgage. During a reverse mortgage, the lender sends you cash, and you make no repayments. So the amount you owe (your debt) gets larger as you get more cash, and more interest is added to your loan balance. As your debt grows, your equity shrinks, unless your home's value is growing at a high rate.

When a reverse mortgage becomes due and payable, you may owe a lot of money and your equity may be very small. If you have the loan for a long time, or if your home's value decreases, there may not be any equity left at the end of the loan.

In short, a reverse mortgage is a "rising debt, falling equity" type of deal. But that is exactly what informed reverse mortgage borrowers want: to "spend down" their home equity while they live in their homes, without having to make monthly loan repayments.

(To make certain you understand what "rising debt" and "falling equity" mean, read the Appendix at the end of this booklet.)

Exceptions

Reverse mortgages don't always have rising debt and falling equity. For example, if a home's value grows rapidly, your equity could increase over time. But most home values don't grow at consistently high rates, so the majority of reverse mortgages end up being "rising debt, falling equity" loans.

Common Features

Although there are different types of reverse mortgages, all of them are similar in certain ways. Here are the features that most have in common.

Homeownership

With a reverse mortgage, you remain the owner of your home just like when you had a forward mortgage. So you are still responsible for paying your property taxes and homeowner insurance and for making property repairs.

When the loan is over, you or your heirs must repay all of your cash advances plus interest (see "Debt Limit" below for more on repayment). Reputable lenders don't want your house; they want repayment.

Financing Fees

You can use the money you get from a reverse mortgage to pay the various fees that are charged on the loan. This is called "financing" the loan costs. The costs are added to your loan balance, and you pay them back plus interest when the loan is over.

Loan Amounts

The amount of money you can get depends most on the specific reverse mortgage plan or program you select. It also depends on the kind of cash advances you choose. Some reverse mortgages cost a lot more than others, and this reduces the amount of cash you can get from them. Within each loan program, the cash amounts you can get generally depend on your age and your home's value:

- the older you are, the more cash you can get; and
- the more your home is worth, the more cash you can get.

The specific dollar amount available to you may also depend on interest rates and closing costs on home loans in your area.

Debt Payoff

Reverse mortgages generally must be "first" mortgages; that is, they must be the primary debt against your home. So if you now owe any money on your property, you generally must do one of two things:

- pay off the old debt before you get a reverse mortgage; or
- pay off the old debt with the money you get from a reverse mortgage.

Most reverse mortgage borrowers pay off any prior debt with an initial lump sum advance from their reverse mortgage. In some cases, you may not have to pay off other debt against your home. This can occur if the prior lender agrees to be repaid after the reverse mortgage is repaid. Generally, the only lenders willing to consider "subordinating" their loans in this way are state or local government agencies.

Debt Limit

The debt you owe on a reverse mortgage equals all the loan advances you receive (including any used to finance loan costs or to pay off prior debt), plus all the interest that is added to your loan balance. If that amount is less than your home is worth when you pay back the loan, then you (or your estate) keep whatever amount is left over.

But if your rising loan balance ever grows to equal the value of your home, then your total debt is generally limited by the value of your home. Put another way, you generally cannot owe more than what your home is worth at the time you repay the loan.

This overall cap on your loan balance is called a "non-recourse" limit. It means that the lender, when seeking repayment of your loan, generally does not have legal recourse to anything other than your home's value and cannot seek repayment from your heirs. (See Part 3 for an exception to this limit on federally insured reverse mortgages.)

Repayment

All reverse mortgages become due and payable when the last surviving borrower dies, sells the home, or permanently moves out of the home. (Typically, a "permanent move" means that neither you nor any other co-borrower has lived in your home for one continuous year.) Reverse mortgage lenders can also require repayment at any time if you fail to:

- pay your property taxes or special assessments;
- maintain and repair your home; or
- keep your home insured.

These are fairly standard "conditions of default" on any mortgage. On a reverse mortgage, however, lenders generally have the option to pay for these expenses by reducing your loan advances, and using the difference to pay these obligations. This is only an option, however, if you have not already used up all of your available loan funds.

Other default conditions could include:

- your declaration of bankruptcy;
- your donation or abandonment of your home;
- your perpetration of fraud or misrepresentation; or
- eminent domain or condemnation proceedings involving your home.

A reverse mortgage may also include "acceleration" clauses that make it due and payable. Generally, these relate to changes that could affect the security of the loan for the lender. For example:

- renting out part or all of your home;
- adding a new owner to your home's title;
- changing your home's zoning classification; or
- taking out new debt against your home.

You must read the loan documents carefully to make certain you understand all the conditions that can cause your loan to become due and payable.

Canceling the Deal

After closing a reverse mortgage, you have three extra days to reconsider your decision. If for any reason you decide you do not want the loan, you can cancel it. But you must do this within three business days after closing. "Business day" includes Saturdays, but not Sundays or legal public holidays.

If you decide to use this "right of rescission," you must do so in writing, using the form provided by the lender at closing, or by letter, fax, or telegram. It must be hand delivered, mailed, faxed, or filed with a telegraph company before

midnight of the third business day. You cannot rescind orally by telephone or in person. It must be written.

Loan Types & Costs

The most well-known and widely available reverse mortgage is the Home Equity Conversion Mortgage (HECM). This loan is discussed in detail in Part 3. Other types of reverse mortgages and alternatives to these loans are discussed in Part 4.

Loan costs can vary by a lot from one type of reverse mortgage to another. Not all reverse mortgages include the same types of loan costs. As a result, the true, total cost of reverse mortgages can be difficult to understand and compare. That is why federal Truth-in-Lending law requires lenders to disclose a "Total Annual Loan Cost" for these loans.

Total Annual Loan Cost

The Total Annual Loan Cost (TALC) combines all of a reverse mortgage's costs into a single annual average rate. TALC disclosures can be useful when comparing one type of reverse mortgage to another. But they also show that the true, total cost of an individual reverse mortgage loan can vary by a lot and can end up being much more—or less—expensive than you might imagine.

TALC disclosures reveal that reverse mortgages generally are most costly when you live in your home only a few years after closing the loan.

Short-term TALC rates are very high because the start-up costs are usually a very large part of the total amount that you owe in the early years of the loan.

However, as your loan balance grows larger over time, the start-up costs become a smaller part of your debt. As these costs are spread out over more and more years, the TALC rate declines.

If the loan's growing balance catches up to the home's value, your debt is then generally limited by that value. This makes the true cost of the loan decrease at a faster rate. So the longer you live in your home, or the less its value grows, the less expensive your loan is likely to be.

Some shortcomings of the TALC disclosure and a more complete way to measure reverse mortgage costs and benefits are discussed in Part 3.

Part 3: The Home Equity Conversion Mortgage (HECM)

The HECM is the only reverse mortgage insured by the federal government. HECM loans are insured by the Federal Housing Administration (FHA), which is part of the U.S. Department of Housing and Urban Development (HUD). The FHA tells HECM lenders how much they can lend you, based on your age and home value. The HECM program limits your loan costs, and the FHA guarantees that lenders will meet their obligations.

HECMs Versus Other Reverses

HECM loans generally provide the largest loan advances of any reverse mortgage. HECMs also give you the most choices in how the loan is paid to you, and you can use the money for any purpose.

Although they can be costly, HECMs are generally less expensive than privately insured reverse mortgages. These other reverse mortgages may have smaller fees, but they generally have higher interest rates. On the whole, HECMs are likely to cost less in most cases. A notable exception may be the reverse mortgages now being developed by some credit unions.

The only reverse mortgages that always cost the least are the ones offered by state or local governments. These loans typically must be used for one specific purpose only; for example, to repair your home or to pay your property taxes. They also generally are available only to homeowners with low to moderate incomes. Part 4 of this booklet discusses reverse mortgages other than HECMs.

HECM Eligibility

HECM loans are available in all 50 states, the District of Columbia, and Puerto Rico. To be eligible for a HECM loan:

- You, and any other owners of your home, must be aged 62 or over, live in your home as a principal residence, and not be delinquent on any federal debt.
- Your home must be a single-family residence in a 1- to 4-unit dwelling, or part of a planned unit development (PUD) or a HUD-approved condominium. Some manufactured homes are eligible, but most mobile homes are not. Cooperatives are expected to become eligible by the end of 2008.
- Your home must meet HUD's minimum property standards, but you can use the HECM to pay for repairs that may be required.
- You must discuss the program with a counselor from a HUD-approved counseling agency; information on

HECM counseling appears in Part 5 of this booklet.

HECM Benefits

The HECM program provides the widest array of cash advance choices. You can take your entire loan as a:

- single lump sum of cash; or
- "creditline" account of a specific dollar amount that you control, that is, you decide when to make a cash withdrawal from this account, and how much cash to withdraw; or as a
- monthly cash advance for a specific period of time, or for as long as you live in your home.

In addition, you can choose any combination of these options, and change your cash advance choices at any future time.

Loan Amounts

The amount of cash you can get depends on your age, current interest rates, and your home's value. The older you are, the more cash you can get. If there is more than one owner, the age of the youngest is the one that counts. The lower the interest rate, the greater your loan amount will be.

In general, the greater your home's appraised value, the more money you can get. However, the value is subject to a limit of $417,000 in November of 2008, and this limit is subject to change every January. If your home is worth more than $417,000, you are still eligible for an HECM loan, but the amount of money you can get is based on $417,000, not on your home's actual value. For example, if your home is valued at $500,000, then the amount you can borrow is the same as it would be if your home were valued at $417,000.

(The $417,000 limit does not apply to parts of Hawaii, which have higher limits. But it does apply to the other 49 states plus the District of Columbia and Puerto Rico.)

Lump Sums & Creditlines

Table 1 shows how much you could get from a HECM if you take it all as a single lump sum of cash or as a creditline, if:

- the value of your home is $150,000, $250,000, or $350,000;
- the expected interest rate on the loan is 6%, 7%, or 8%;
- the age of the youngest borrower at closing is 65, 70, 75, 80, 85, or 90; and
- the servicing fee is $35, closing costs are $2,500, and the origination fee is the maximum allowed by HUD (see p. 13).

You can divide the amounts in Table 1 between a lump sum and a creditline. For example, a 75-year-old borrower living in a $250,000 home getting a HECM loan at 7% expected interest could select:

- a lump sum or creditline of $135,484; or
- any combination of lump sum and creditline that totals $135,484, for example, a lump sum of $30,000 and a creditline of $105,484.

For an estimate of HECM cash benefits based on your age, home value, and current interest rates, go to the online calculator at **www.aarp.org/revmort** (click on "Reverse Mortgage Calculator").

Creditline Growth

Perhaps the most attractive HECM feature is that its creditline grows larger over time. This means that the amount of cash available to you increases until you withdraw all of it.

For example, if the creditline equals $100,000 and you withdraw $20,000, you would have $80,000 left. But if your next withdrawal is one year later, you would then have more than $80,000 left because the $80,000 grows larger by the same total rate being charged on your loan balance. If that rate were to equal 6% per year, for example, your available creditline one year later would be $84,800 (6% x $80,000 = $4,800).

So a growing HECM creditline can give you a lot more total cash than a creditline that does not grow. The HECM creditline keeps growing larger every month for as long as you have any credit left; that is, until you withdraw all your remaining cash.* The calculator at

Table 1: HECM Lump Sum or Creditline

		Lump sum or creditline when expected rate is		
Home Value	Age	6%	7%	8%
$150,000	65	$74,325	$59,626	$47,530
	70	81,782	68,513	56,965
	75	89,638	78,084	67,672
	80	97,930	88,228	79,088
	85	106,260	98,400	90,820
	90	114,250	108,233	102,207
$250,000	65	$129,925	$105,026	$84,530
	70	142,182	119,713	100,165
	75	155,038	135,484	117,872
	80	168,530	152,128	136,688
	85	181,960	168,700	155,920
	90	194,650	184,533	174,407
$350,000	65	$186,025	$150,926	$122,030
	70	203,082	171,413	143,865
	75	220,938	193,384	168,572
	80	239,630	216,528	194,788
	85	258,160	239,500	221,520
	90	275,550	261,333	247,107

* The rate at which your creditline grows each month equals the current interest rate being charged on your loan plus one-half of one percentage point, divided by 12. So if the interest rate this month is 5.5%, your creditline would grow by 0.5% (5.5% + 0.5% = 6%/12 = 0.5%). If you had a creditline of $80,000 at the start of the month, it would equal $80,400 at the end (0.5% X $80,000 = $400).

www.aarp.org/revmort (click on "Reverse Mortgage Calculator") estimates how much cash would remain in a HECM versus a non-growing creditline.

HECM creditline growth means you should not even think about taking a large lump sum of cash from a HECM and putting it into savings or an investment. If you did that, you would be charged interest on the full amount of the HECM lump sum.

But if you leave the money in the creditline, not only would you avoid substantial interest charges. You would also end up with more available cash, as your creditline increases at a greater rate than a savings account or safe investments are likely to increase.

Plus a Monthly Advance

The HECM program lets you combine a lump sum, a creditline, or both with a monthly advance. A monthly loan advance does not increase or decrease in dollar amount over time. So it will buy less in the future as prices increase with inflation.

You can choose to have monthly HECM advances paid to you for:

- a specific number of years that you select (a "term" plan); or
- as long as you live in your home (a "tenure" plan).

A term plan gives you larger monthly advances than a tenure plan does. The shorter the term, the greater the advances can be. But the advances only run for a specific period of time. You do not have to repay the loan when the term ends, but you no longer receive monthly advances past the end of the term you select.

Table 2 shows some of the combinations that could be selected by a 75-year-old female borrower living in a $250,000 home with a loan at 7% expected interest

Table 2: HECM Monthly Advance Plus Lump Sums or Creditlines for a 75-Year-Old Borrower Living in a $250,000 Home*

Any combination of a lump sum and a creditline totaling...

	plus a monthly advance for...			
	tenure	15 years	10 years	5 years
0	$995	$1,248	$1,598	$2,697
$ 25,000	811	1,017	1,303	2,200
$ 50,000	627	787	1,008	1,702
$ 75,000	444	557	713	1,204
$100,000	260	326	418	706
$125,000	77	96	123	208
$135,484	0	0	0	0

*Based on a 7% expected interest rate and the loan costs used in Table 1.

and the same loan costs as assumed in Table 1.

For example, if this borrower selects a $25,000 lump sum and a $50,000 creditline, she also could get any one of the following: a monthly advance of $444 for as long as she lives in her home, $557 each month for 15 years, $713 each month for 10 years, or $1,204 monthly for 5 years. Table 2 makes two things clear:

- if you take more money as a lump sum or creditline, the monthly advances are smaller; and
- if you select a shorter term of monthly advances, the amount of each advance is greater.

Monthly Advances Only

Table 2 also shows that you get the largest possible monthly advance if you do not take a lump sum or a creditline. But putting all of your loan funds into a monthly advance reduces your financial flexibility, especially if you have little in savings. Remember, monthly advances are fixed, so their purchasing power decreases with inflation.

Adding a growing creditline to a monthly advance not only gives you a hedge against rising prices. It also provides readily available cash for unexpected expenses. So if you are interested in a monthly advance, it's a good idea to consider adding a creditline as well.

On the other hand, for a $20 fee, you could change your payment plan at any time. For example, you could add a creditline to a monthly advance, although this would reduce the amount of the monthly advance. You could also convert part or all of a creditline into a monthly advance.

HECM Repayment

As with most reverse mortgages, you must repay a HECM loan in full when the last surviving borrower dies or sells the home. It also may become due and payable if:

- you allow the property to deteriorate, except for reasonable wear and tear, and you fail to correct the problem; or
- all borrowers permanently move to a new principal residence; or
- due to physical or mental illness, the last surviving borrower fails to live in the home for 12 months in a row; or
- you fail to pay property taxes or hazard insurance, or violate any other borrower obligation.

Debt Limit

If your rising HECM loan balance ever grows to equal the value of your home, then your total debt is limited by the value of your home if the home is sold to repay the loan. But if the home is not sold and the loan is repaid with other funds, then you or your estate would owe the full loan balance—even if it is greater than your home's value. Your heirs would not have any personal liability for repaying the loan.

HECM Costs

Almost all the costs of a HECM can be "financed," that is, they can be paid from the proceeds of the loan. Financing the costs reduces the net loan amount available to you, but it also reduces your cash, out-of-pocket cost. The itemized costs

of a HECM loan include an origination fee, third-party closing costs, a mortgage insurance premium, a servicing fee, and interest.

Origination Fee

An origination fee pays a lender for preparing your paperwork and processing your loan, also known as "originating" a loan. If your home is worth less than $125,000, a lender can charge up to $2,500 for this fee. If it is worth more than $125,000, the fee is limited to 2% of the first $200,000 of your home's value plus 1% of any amount over $200,000, up to an absolute limit of $6,000. On a $250,000 home, for example, the origination fee limit would be $4,500 (2% x $200,000 = $4,000 plus 1% of $50,000 = $500). Origination fees vary from one lender to another, so it can pay to shop around. The amount of this fee may also be negotiable with a lender.

Third-Party Closing Costs

A "closing" is a meeting at which legal documents are signed to "close the deal" on setting up a mortgage. The date of closing is the day on which a mortgage begins. Closing a mortgage requires a variety of services by third parties other than the originating lender. These services include an appraisal, title search and insurance, surveys, inspections, recording fees, mortgage taxes, credit checks, and others.

Third-party closing costs on a HECM loan vary with the value of the home and from one state or area to another. However, all the HECM lenders in a given area are likely to charge about the same closing costs on any specific loan. The total of all these costs generally ranges from about $2,000 to $3,000, although they are substantially higher in some areas.

A lender may require a cash application fee to pay for an appraisal and minimal credit check. Some will refund this fee to you. Others will apply it to your origination fee or third-party closing costs.

Mortgage Insurance Premium (MIP)

HECM insurance is financed by an MIP charged on all HECM loans. The cost, which may be financed with the loan, is charged in two parts:

- 2% of your home's value (or 2% of HUD's home value limit, whichever is less) is charged "upfront" at closing; and
- 0.5% is added to the interest rate charged on your rising loan balance.

HECM insurance guarantees that you will receive your promised loan advances, and not have to repay the loan for as long as you live in your home, no matter:

- how long you live there;
- what happens to your home's value; and
- what happens to the lender from whom you got your loan.

The MIP also guarantees that your total debt can never be greater than the value of your home if it is sold to repay the loan. It makes it possible for you to keep getting your monthly loan advances or growing creditline as promised even if:

- you live much longer than others your age;

- your home's value grows very little, not at all, or declines; or
- your loan balance catches up to and then is limited by the value of your home.

As a government program, HECM insurance does not generate a profit. The premiums paid by all borrowers are used to continue making loan advances to and limit the amount owed by the borrowers who live the longest and whose home values grow the least or decline.

The MIP is a substantial cost. The upfront portion on a $250,000 home, for example, would be $5,000. The cost of the 0.5% added to the interest rate depends on how much money you borrow, when you borrow it, and the interest rate on the loan. For a 75-year-old borrower living in a $250,000 home, who borrows one-half of the maximum loan amount at closing at an expected rate of 7%, the cost during her remaining life expectancy (12 years) would be about $7,900.

Servicing Fee

"Servicing" a loan means everything lenders or their agents do after closing it, including making or changing loan advances at your request, transferring insurance premiums to FHA, sending account statements, paying property taxes and insurance from the loan at your request, and monitoring your compliance with your obligations under the loan agreement.

FHA limits the servicing fee to $30 per month if the loan has an annually adjustable interest rate, and to $35 if the rate is monthly adjustable (see below). But the amount of this fee can vary from lender to lender within these limits. So it can pay to shop around.

To finance this fee with the loan, a lender is required to "set aside" a prescribed dollar amount* and deduct it from your available loan funds. But this total amount is not added to your loan balance. Instead, the monthly fee is added to your loan balance each month.

The total amount actually paid in servicing costs depends on the amount of the monthly charge plus how long it is paid. For a 75-year-old borrower who pays $35 per month for her remaining life expectancy (12 years), that cost would be $5,040.

On traditional "forward" mortgages, the cost of servicing is added to the interest rate. So you may not have seen this fee before—but you've paid it.

Total Non-Interest Costs

If you've been keeping track of all the upfront and ongoing costs described for a 75-year-old borrower in a $250,000 home, you know that the total (not including interest) could be about $25,000. For the youngest borrowers (aged 62) in higher-valued homes ($417,000 or more) in the areas with higher third-party closing costs ($4,000), the total of all non-interest costs could be over $45,000.

*The amount "set aside" for servicing is the "present value" of the monthly fee from closing until the borrower would reach age 100. Since few borrowers live to age 100, the total amount set aside overstates the actual amount likely to be charged on most loans over the life of the loan.

Interest Charges and Total Costs

The largest single cost of any reverse mortgage is generally the interest that is charged on these loans. For example, a 75-year-old borrower living in a $250,000 home qualifies for a HECM creditline of about $135,484 at 7% expected interest. If this homeowner takes one-half of that amount ($67,742) as a lump sum at closing, she would immediately owe that $67,742 plus about $12,000 in upfront costs, for a total of $89,742.

The remaining life expectancy of a 75-year-old borrower assumed in the HECM program is 12 years. If this borrower lives in her home that long, the total amount of interest added to her loan balance at 7% interest would be $111,056 if the interest rate does not change over the life of the loan. So after 12 years, at age 87, she would owe the initial $67,742 she borrowed plus $12,000 in upfront costs, $7,933 in monthly mortgage insurance premiums (MIPs), $5,040 in servicing fees, and $111,056 in interest charges for a total of $203,771 (see Table 3).

Table 3: HECM Loan Costs at Life Expectancy for a 75-Year-Old Borrower in a $250,000 Home

Total Amount Borrowed	**$67,742**
Loan Costs	
Upfront Costs	$12,000
Total Monthly MIPs	$7,933
Total Monthly Servicing Fees	$5,040
Total Monthly Interest Charges	$111,056
Total Loan Costs	$136,029
Total Amount Owed (Loan Balance)	**$203,771**

Table 4 (see page 16) shows how the costs summarized in Table 3 would be added to the loan balance year by year, making the total amount owed increase over time. The figures in both tables assume that the loan's 7% interest rate would not change. But any increases or decreases in that rate would increase or decrease the amount of interest and MIP owed on the loan. Information on interest rate choices is discussed in Part 5 of this booklet.

Tables 3 and 4 also assume that the borrower makes no creditline withdrawals after taking a $67,742 lump sum advance at closing. If she does take creditline draws after closing, the total amount of interest charges and MIPs would be greater than the amounts shown in these tables.

Total Cost Disclosures

As discussed in Part 2, the true, total cost of a reverse mortgage depends on factors in addition to its various costs. The Total Annual Loan Cost (TALC) of a reverse mortgage also depends upon:

- how long you live in your home; and
- what happens to its value during that time.

In general, the TALC rate is greatest when the loan is repaid within a few years after closing when the upfront costs are still a

large part of the total amount owed. On the other hand, TALC rates are lowest when you live longer than others your age, or when your home's value grows little, or declines. But TALC disclosures also do not address two key considerations for reverse mortgage borrowers:

- the total amount of cash you get from the loan; and
- the amount of equity you get to keep at the end of the loan.

Model Specifications

In 2000, under a grant from the U.S. Department of Housing and Urban Development, the AARP Foundation's Reverse Mortgage Education Project invited reverse mortgage counselors and lenders to develop a more complete and individually customized standard for measuring reverse mortgage costs and benefits. The result of this joint effort was a set of model specifications for analyzing and comparing reverse mortgages. The specifications are based on a simple way of looking at these loans. All reverse mortgages turn your home equity into three things:

- loan advances paid to you;
- loan costs paid to the lender and others; and
- leftover equity, if any, paid to you or your heirs at the end of the loan.

Because reverse mortgages turn home equity into only these three things, you

Table 4: Rising Loan Costs for a 75-Year-Old HECM Borrower Living in a $250,000 Home

At end of year	Upfront Fees	Servicing Fees	Monthly MIPs	Interest Charges	Total Costs
0	$12,000				$ 12,000
1	$12,000	$ 420	$ 414	$ 5,794	$ 18,628
2	$12,000	840	862	12,068	25,770
3	$12,000	1,260	1,347	18,860	33,467
4	$12,000	1,680	1,872	26,210	41,762
5	$12,000	2,100	2,440	34,161	50,701
6	$12,000	2,520	3,054	42,759	60,333
7	$12,000	2,940	3,718	52,055	70,713
8	$12,000	3,360	4,436	62,103	81,899
9	$12,000	3,780	5,212	72,962	93,954
10	$12,000	4,200	6,050	84,694	106,944
11	$12,000	4,620	6,955	97,368	120,943
12	$12,000	5,040	7,933	111,056	136,029

can analyze any reverse mortgage by asking three simple questions:

- How much would I get?
- How much would I pay?
- How much would be left at the end of the loan?

At the end of a reverse mortgage, all of your home's value will have been turned into one of these three things: loan advances, loan costs, or leftover equity.

AARP's model specifications provide a set of rules for estimating how much of your home's value will have been turned into each of these three things at various future times. They also estimate a total annual average loan cost for each of these future times.

The specifications permit all of these estimates to be based on the creditline advances and a future interest rate that you select. You can also choose the rate at which you expect your home's value will grow. By varying these factors, you can see how much effect each can have on a loan's total cash advances, total cost, and leftover equity. You need to keep in mind, however, that all of these figures are estimates. The actual figures will depend on:

- the actual creditline advances you select during the loan;
- the actual interest rates charged on the loan; and
- the actual changes in your home's value during the loan.

Information on obtaining loan analyses and comparisons produced by the model specifications is discussed in Part 5 of this booklet. For a copy of the model specifications, go to **www.aarp.org/revmort**, click on "Basics," and then on "Total Costs and Model Specifications." Scroll down to "AARP Resources" for a link to the specifications.

Other Choices

TALC disclosures and other measures estimate the total cost of a HECM. But only you can determine how much it would be worth to you. And that might depend on other choices that may be available to you.

Part 4 of this booklet discusses other reverse mortgages that may be available to you. It also explores various alternatives to reverse mortgages for you to consider.

Part 4: Other Choices

A Home Equity Conversion Mortgage (HECM) may be a reasonable choice for you, either now, or at some future time. But until you compare it to your other options, you cannot make an informed decision about it. This section discusses other types of reverse mortgages, and alternatives to reverse mortgages. Seriously considering all your options will help you see more clearly why you prefer some to others. It is also likely to lead you to the decision that best serves your needs.

Other Reverse Mortgages

Deferred Payment Loans (DPLs)

Many local and some state government agencies offer DPLs for repairing or improving your home. This type of public sector reverse mortgage provides a one-time, lump sum advance. No repayment is required for as long as you live in your home.

DPLs aren't available everywhere, and they can be difficult to find, in part because they go by a variety of names and descriptions. Contact your city or county housing department, area agency or county office on aging, or the nearest community action or community development agency. Also contact your state housing finance agency. If these agencies don't offer DPLs, they may know where to find them, or they may offer other low-cost home repair loans with easily affordable monthly payments.

Eligibility criteria vary from program to program. Most are limited to homeowners with low or moderate incomes. Many place a limit on a home's value, or lend only in defined areas. Some have a minimum borrower age or a disability requirement.

DPLs can be used only for the specific types of repairs or improvements that each program allows. This may limit you to projects that replace or repair basic items such as your roof, wiring, heating, plumbing, floors, stairs, or porches. Many programs will cover improvements in accessibility or energy efficiency. Such modifications may include the installation of ramps, rails, grab bars, storm windows, insulation, or weather-stripping. (Search for "fixing homes" at **www.aarp.org**.)

You may be able to combine a DPL with a HECM loan. To do this, the DPL lender must agree to be repaid after the HECM is repaid. The best thing about DPLs is their very low cost. Generally they have no origination fee, no insurance premium, minimal (if any) closing costs, and very low (or no) interest. If interest is charged, it is often done on a "fixed" basis, that is, the rate never changes. Many DPL

programs also charge “simple” rather than “compound” interest. This means that interest is not charged on any of the interest that has been previously added to the loan balance.

Some DPL programs even forgive part or all of the loan if you live in your home for a certain period of time. In other words, you may end up paying nothing back ever. If you can find and qualify for a “forgivable” DPL, you would most likely have more equity left at the end of the loan than you had at the beginning. In any case, a DPL is one of the best bargains you will find.

Even so, you still must be careful dealing with home improvement contractors. Ask the DPL program for help in finding a reliable contractor and developing a sound contract.

Property Tax Deferral (PTD)

Some state and local government agencies offer “property tax deferral” (PTD) loans. This type of public sector reverse mortgage generally provides annual loan advances that can be used only to pay your property taxes. No repayment is required for as long as you live in your home.

According to a 2007 AARP study, some type of PTD program is available in parts or all of the following states: Arizona, California, Colorado, Florida, Georgia, Idaho, Illinois, Iowa, Maine, Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, North Dakota, Oregon, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, Wisconsin, Wyoming, and the District of Columbia.

In some states, PTD is available on a uniform, statewide basis. In many others, it is not available in all areas, or is not the same in all the areas where it is available. Eligibility criteria vary considerably. Most programs have a minimum age of 65 and are limited to homeowners with low or moderate incomes.

If you live in a state listed above, contact the local government agency to which you pay your property taxes. This agency can tell you if the program is available in your area, and what you must do to qualify. It also can give you details on how the program works.

The amount of the annual PTD loan advance is generally limited by the amount of your property tax bill for that year. Some programs limit the annual advance to some part of the tax bill, or to a specific amount.

In the most restrictive programs, the loan can only be used to pay for special assessments.

The total amount you can borrow over the life of a PTD loan is limited in most programs. In other words, you may become ineligible for additional annual loan advances at some point in the future.

PTD programs generally do not permit these loans to be “subordinate” to other loans. So you cannot have a PTD loan and another reverse mortgage at the same time.

Like deferred payment loans, PTD loans

generally charge no origination fee, no insurance premium, and minimal, if any, closing costs. The interest rate is usually fixed, but it varies from program to program. In some cases, interest is charged on a simple basis, that is, no "interest on interest."

Other Public Loans

State housing finance agencies in Connecticut and Montana offer specialized reverse mortgage loans. The Connecticut plan is limited to persons who are no longer able to function on their own.

These plans provide limited lump sum advances, plus monthly advances that stop after a fixed period of time. But the loan does not have to be repaid for as long as you live in your home. The cost of these plans is very low, but the benefits are limited as well.

For more information on the Connecticut plan, call 1-860-571-3502. For information on the Montana program call 1-800-761-6264 or 1-406-841-2840.

Proprietary Reverse Mortgages

"Proprietary" reverse mortgages can provide larger loan amounts than the HECM program, but they are generally the most expensive type of reverse mortgage. Private companies develop and back these loans, and decide which lenders may offer them. By contrast, HECMs are backed by the U. S. Government and may be offered by any lender approved by the Federal Housing Administration.

If you live in a home worth a lot more than HUD's home value limit for the HECM program (currently $417,000), you may qualify for a larger loan amount from a proprietary plan than from a HECM. For example, in order to get a greater loan amount from a leading proprietary plan than from a HECM, a 75-year-old consumer would need to own a home worth more than about $850,000. A 62-year-couple, on the other hand, would need to own a home worth more than about $1.1 million to get a larger loan amount from the proprietary plan.

But even if you could get a larger loan amount from a proprietary plan, it might not actually provide you with more in total loan advances than a HECM would provide. As explained earlier, the amount of funds remaining available in a HECM creditline grows larger every month, and may do so at a rate that is greater than the one at which proprietary creditlines grow.

Proprietary creditline funds generally do not grow at all or do so at a fixed rate. But that fixed rate may be less than the rate at which HECM creditlines grow. So an initially smaller HECM creditline may provide more total cash over time than an initially larger creditline that grows at a lower rate.

Compared with HECMs, proprietary reverse mortgages typically offer lower upfront and monthly fees but charge much greater interest rates—as much as three percentage points (3%) greater. So the lower fees on a proprietary plan can be offset by its much higher interest rate, resulting in greater total costs for the proprietary plan.

A new type of proprietary reverse mortgage now being developed by some

credit unions, however, may provide a clearly lower-cost alternative to HECMs. These plans would provide smaller loan amounts than a HECM, but would charge much smaller fees.

The best way to compare a proprietary plan with a HECM is to use a side-by-side comparison produced by software that meets the model specifications for analyzing reverse mortgages discussed in Part 3 of this booklet. Information on obtaining these revealing comparisons is presented in Part 5.

Alternatives to Reverse Mortgages

Selling and Moving

Many homeowners become interested in reverse mortgages as a way to remain living in their present homes. Selling the home and moving elsewhere are generally not very appealing to most reverse mortgage shoppers.

The single best way to evaluate a reverse mortgage, however, is to compare it to what may be your only other viable option: selling your home and using the proceeds to buy or rent a new home. Do you know:

- How much cash you could get by selling your home?
- What it would cost you to buy (and maintain) or rent a new home?
- How much money you could safely earn on any money left over after you buy a new home?

Have you recently looked into buying a less costly home, renting an apartment, or moving into assisted living or other alternative housing?

Until you have seen and considered other housing options, how do you know that none could be preferable to your current home? Or preferable to a reverse mortgage? For your own peace of mind, you should seriously look into what else might be available. (Search for "housing options" at **www.aarp.org**.)

Most likely you will come to one of two conclusions:

- you may find another housing option that is a lot more attractive than you thought; or
- you may confirm what you were fairly certain of all along: that where you live now is the best place for you to be.

No matter what you conclude, you will have a much better idea of the overall costs and benefits of staying versus moving. That will give you a better sense of what is important to you. And it will then be easier for you to evaluate the comparative costs and benefits of a reverse mortgage.

Public Benefits

Your home is probably the most important investment you have ever made. You've probably spent much of your adult life making monthly payments on a traditional "forward" mortgage. So cashing in on that long-term investment while continuing to live in your home can be an appealing idea.

But most people have also made another kind of long-term investment. They've

paid taxes all of their adult lives, and this has supported a variety of public programs. From time to time, most of us have benefited from some of these programs.

But you can't benefit from a program if you don't know it exists. That's why you should be aware of the major programs for which you may be eligible.

Supplemental Income

A substantial portion of all Americans aged 65 and over who are eligible for monthly cash benefits from SSI (Supplemental Security Income) are not getting them.

To qualify for this program, your liquid resources (cash and savings) must be less than $2,000 ($3,000 for a couple). Certain resources, such as home equity up to $500,000 ($750,000 in some states), a small burial fund, or one car usually do not count. Your monthly unearned income in 2008 could not exceed $657 ($976 for a couple). But the income limits are greater if you have earned income from a job, or if you live in one of the states providing a supplement to SSI.

If you qualify for SSI, you may be automatically eligible for other public benefits as well. For the latest information, call 1-800-772-1213. On the Internet, go to **www.ssa.gov** and search for "SSI."

Health Care Costs

Public benefit programs can also help pay for medical expenses. For the latest information, search for "Medicaid" and "Medicare prescripton drug coverage" at **www.aarp.org**. You can also call the Medicare Hotline at 1-800-633-4227. When you call, say "Medicaid" or "drug coverage" to get information about these programs.

Property Tax Relief

Most states have one or more property tax relief programs. For information on property tax relief in your state, contact the local agency to which you pay your property taxes, your state department of revenue or taxation, or your nearest area agency on aging.

Agencies on Aging

Your single best source for a wide variety of public benefit programs is your AAA (area agency on aging). Find your AAA by calling 1-800-677-1116 or search online at **www.eldercare.gov**.

This agency can help you find programs such as

- energy assistance
- household chore services
- home health care
- prescription drugs
- meal programs
- housing
- transportation, and many others.

Benefits QuickLINK

This one-stop online public benefits source helps you find low and no-cost programs that can pay for basic expenses, help you stay healthy, and assist older relatives. You fill out a questionnaire to find programs

for which you may be eligible. You get the contact information you need to learn more about—and apply for—these programs. To use this resource, go to **www.aarp.org/quicklink**.

Postpone or Combine

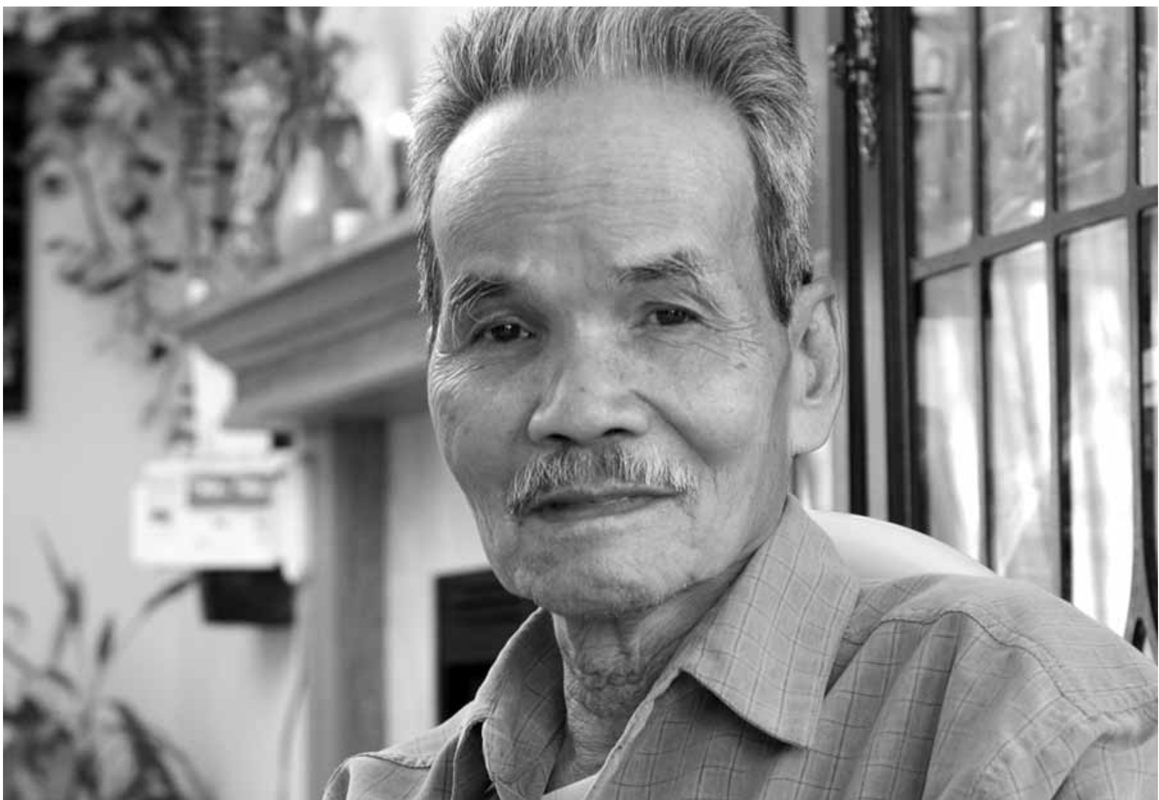
Public benefits can make it possible for you to postpone getting a reverse mortgage until a future time. In many cases, that may allow you to get larger future loan dvances because you will be older and your home's value is likely to be greater at that time. And the longer you wait, the less your equity will have been consumed by interest charges.

On the other hand, you can sign up for public benefits and take out a reverse mortgage. If you do, your need for loan advaces will be less than if you were not receiving public benefits. By taking smaller loan advances, you will have smaller interest charges and preserve more equity for future use.

Cautions

Just make certain you don't jeopardize any public benefits by getting more cash than you need from a reverse mortgage.

For example, loan proceeds remaining in a checking or savings account at the end of a calendar month are counted as liquid assets by SSI and similar programs. If your total liquid assets exceed SSI limits (currently $2,000 for a single person, $3,000 for a couple), you can lose your eligibility. So limit your loan proceeds to what you expect to spend in a given month (*Source: Reverse Mortgages: A Lawyer's Guide*, American Bar Association, 1997, pp. 35-36).



Part 5: Key Decisions

Homeowners seriously considering a reverse mortgage should ask themselves these key questions:

- **Who else should I involve in considering this loan?**
- **Which counselor should I choose?**
- **Have I given due consideration to all my choices?**
- **When would be the best time to take out a reverse mortgage?**
- **What interest rate should I select?**
- **Which lender should I choose?**
- **How should I use this loan?**

No one can answer these questions for you. Only you can decide what's right for you and your situation. But you need to consider these decisions carefully, because you will make them one way or another. And it's better to do so by thinking them through.

Sharing the Decisions

Who else should you involve in making your decisions about a reverse mortgage? You may have a trusted friend or advisor who knows your circumstances—or someone who is generally good at figuring things out or discussing them with you. You may even want to invite such people to your discussion with a HUD-approved counseling agency.

On the other hand, you should be cautious of anyone who seems eager for you to get a reverse mortgage. Be especially alert if that person just happens to have ideas about what you might do with your loan proceeds. Watch out in particular for anyone trying to sell you something, or to get your signature on an agreement to pay them for any purpose.

Remember, we call such people "con men" because they are very good at gaining our confidence and trust. It's sad but true that the stranger being so nice to you may be more interested in your equity than your well-being.

Your Heirs

You also need to think about the impact of a reverse mortgage on your heirs. A loan with "rising debt and falling equity" means there will be less equity left for your heirs. If you get a lot of cash over many years from the loan, there may be little if any left for them.

Many children of reverse mortgage borrowers are pleased that their parents are able to use their equity and remain living in their homes. Often it is a great relief to these children that their parents are able to take care of their own needs; many even encourage their parents to do so.

Whether or not you decide to discuss this matter with your children or other heirs depends on a variety of personal and family factors. You may value their advice or want to know what they think. Or you may think it best not to discuss it before making a decision, or not to tell them after you have closed a loan.

On the other hand, to avoid future misunderstanding, you may want to make a note of your decision in your will. Whatever you decide, the important thing is to give some thought to your heirs. A reverse mortgage can have a substantial impact on your estate. So you need to think through how you want this to become known to your heirs.

Selecting a Counselor

To be eligible for a federally insured HECM (Home Equity Conversion Mortgage), you must discuss the loan with a counselor employed by a nonprofit or public agency approved by HUD (the U. S. Department of Housing and Urban Development). This counseling can be very helpful. So it can be a good idea even if you are thinking about applying for some other type of reverse mortgage.

HECM counselors provide in-person counseling in their local areas, and counseling by telephone in other areas nationwide. For current information on requesting HECM counseling, go to **https://entp.hud.gov/idapp/html/hecm_agency_look.cfm**. This counseling generally takes at least one hour. When provided by telephone, it typically requires two or more calls.

Counseling agencies may charge a fee for HECM counseling, but they must tell you about it before the counseling occurs, and the fee amount must be based on your ability to pay. Agencies cannot turn you away because of your inability to pay, and they cannot refuse to counsel you if you fail to pay. The maximum allowable fee in 2008 is $125 or the actual cost of providing the counseling, whichever is less. If your counseling agency charges a fee, you can have it paid out of your loan proceeds just like other HECM fees, or you can pay it directly to the counseling agency.

Be Prepared

However you request counseling, prepare for it carefully. If you are interested in a HECM, make certain you are eligible by re-checking the eligibility criteria in Part 3. Use the calculator at **www.aarp.org/revmort** (click on "Reverse Mortgage Calculator") to see if you can get the amount of cash you need to pay off any current debt on your home, and for other purposes.

Before requesting counseling, thoroughly consider the questions in Part 1 of this booklet and the key decisions discussed in this section. Make a written list of your questions, concerns, and the additional information you need. Include questions about the alternatives discussed in Part 4.

HUD's HECM network counselors use loan analysis and comparison software that meets the model specifications discussed in Part 3. Ask your counselor to send you loan printouts in advance so you can review them before your counseling session, and have them in hand when your counselor explains them.

Considering Alternatives

Have you carefully considered the main alternatives to a HECM? Have you seriously looked into the other options discussed in Part 4? If not, you should do so before applying for a HECM. Even if you end up getting a HECM, combining it with another option may make more sense than not.

If you can qualify for a home equity loan and easily make the required monthly repayments, this option is generally less costly than a HECM or a proprietary reverse mortgage. But before applying for one of these loans, learn about the potential pitfalls in this market. Search for "home equity loans" and "predatory lenders" at **www.aarp.org**.

If you are considering a proprietary reverse mortgage, you must proceed with caution. Unlike HECMs, these loans are not insured by the federal government.If your home is worth more than $850,000 ($1.1 million for couples), you may be able to get larger loan advances than you could get from a HECM. But you may also pay more, and you need to understand how much more these loans may cost.

The best way to compare the costs and benefits of a proprietary plan versus a HECM is to get the side-by-side loan comparisons produced by software that meets AARP's model specifications discussed in Part 3. You can get these comparisons from counselors who belong to HUD's national HECM counseling network, who can be found at **www.hecmresources.org/hecmresources/requests.cfm**.

You can also get these comparisons from some lenders. For the latest information on lenders who can provide these comparisons, go to **www.aarp.org/revmort** and click on "Key Decisions," and then on "Selecting a Lender."

Selecting a Time

When would be the best time to take out a reverse mortgage: now or later? In the future, you may be eligible for larger cash advances because you will be older and your home is likely to be worth more. If your home's value is greater than HUD's home value limit (currently $417,000), that limit is subject to change each January. On the other hand, if interest rates rise, you may not be able get greater loan advances in the future.

Look at Table 1 in Part 3 or use the calculator at **www.aarp.org/revmort** (click on "Reverse Mortgage Calculator") to see how much difference an older age or greater home value could make. The table also shows you how much difference a higher interest rate could make.

Remember, one month after you take out a reverse mortgage your debt will begin growing. Look at Table 4 in Part 3 to see how fast that debt can grow. The longer you postpone taking out a reverse mortgage, the more interest charges you will avoid and the more equity you will most likely have if and when you do decide to become a reverse mortgage borrower.

Selecting an Interest Rate

If you are considering a HECM, you can select an interest rate that is subject to

change once a month or once a year, or one that remains the same (a "fixed" rate) for the life of the loan.

Fixed Interest Rates

Fixed rate loans are attractive to most consumers, but fixed rate HECMs may be no bargain for most borrowers, as the interest rate on some of these loans has exceeded 15%.

The only way homeowners could get a realistic fixed rate from these lenders was if they agreed to take 100% of their available loan amount in a single lump sum at closing. But this meant they would be charged interest on the full amount of the largest possible loan advance, and most HECM borrowers have no need for such a large advance. So if they were to agree to a 100% lump sum, they would be paying substantial unnecessary interest charges and—by completely exhausting their loan amounts—losing the creditline growth to which they would otherwise be entitled.

On the other hand, if a borrower needs such a large loan amount, for example, to pay off the current mortgage on a home, a fixed rate HECM of this type would be worth considering.

Adjustable Interest Rates

HECM lenders must offer an interest rate that is subject to change once a year. These "annually-adjustable" HECMs can increase or decrease by the same amount as any increase or decrease in a HUD-approved interest rate index identified in the loan documents. But this rate cannot change by more than 2 percentage points up or down per year, nor by more than 5 total points over the life of the loan,

HECM lenders may also offer a "monthly-adjustable" rate that may increase or decrease each month by the same rate as any increase or decrease in a HUD-approved interest rate index identified in the loan documents. Although HUD does not require any interest rate caps on these rates, some lenders may provide them.

The index rate indices approved by HUD are the 1-month and 1-year U. S. Constant Maturity Treasury (CMT) rate and the 1-month and 1-year London Interbank Offered Rate (LIBOR), an international index widely used for adjustable rate mortgages in the U. S.

Monthly Versus Annually Adjustable

Monthly adjustable rates are generally lower than annually adjustable rates when based on the same rate index. Lower rates mean larger HECM loan amounts, less growth in the amount you owe, and less growth in your available creditline funds. When interest rates fall, monthly adjustable rates drop sooner and more often than annually adjustable rates. They can also decrease by more than 2 percentage points per year and by more than 5 percentage points over the life of the loan.

The main advantage of annually adjustable HECMs are that when interest rates rise, they increase later and less frequently than monthly adjustable rates. In addition, they cannot increase by more

than 2 percentage points in any year, and by no more than 5 percentage points over the life of the loan.

To date, most HECM borrowers have selected monthly adjustable rates, no doubt because they prefer the greater loan amounts and the lower initial rate charged on the loan. Some may also believe that rates are unlikely to increase by more than the caps on annually adjustable rates.

Borrowers selecting an annually adjustable rate are generally concerned that rising rates might exceed the annual rate's caps for extended periods. Without the protection of these caps, they fear, their loans balances will grow faster, so there will be a lot less equity for them or their heirs when the loan is over.

Selecting a Lender

The most complete lists of HECM lenders can be found online at **www.hud.gov/ll/code/llslcrit.cfm**. Enter your city or select your state, place a checkmark in the "HECM" box, and click the "SUBMIT" button.

But which lender should you use to get a HECM loan? You need to consider cost, origination services, loan servicing, and a lender's professional commitment to meeting consumer needs.

Cost

HECM loan costs can vary by a lot from lender to lender, so it pays to shop around before deciding on a lender. Letting lenders know that you are shopping around may also help you get a better deal.

The only HECM costs that lenders do not control are the upfront and monthly mortgage insurance premiums. So you need to find out how much each lender you are considering would charge you for the origination fee, all third-party closing costs, the monthly servicing fee, and—most importantly—the interest rate. Some lenders may say that their interest rate is based on a specific rate index plus a "margin." If they do, ask what the actual interest rate would currently be.

When comparing the cost of loan fees versus interest, keep in mind that the interest rate will apply to your total and growing loan balance for as long as the loan lasts. Ask lenders and your HECM counselor to show you what the impact of different available combinations of loan fees and interest rates would be on the amount you would owe in the future. If you are concerned about rising interest rates on an adjustable rate loan, ask them to show you how much more you would owe if the average rate on your loan would be higher than the rate initially charged on the loan.

Origination Services

The level of service a lender provides may be more difficult to assess than cost is, but service can be important. You will want your loan officer to be knowledgeable, experienced, and respectful.

After reading this booklet, you will be better able to gauge how well a lender knows reverse mortgages. How long a lender has been offering HECMs and in how many places may be particularly important if your loan runs into any

unexpected snags. An experienced lender has already encountered most of the issues that can cause problems, and is most likely to have a good working relationship with the nearest HUD office.

You will also want a loan officer who respects your knowledge and preferences and helps you reach your own decisions. Pressure sales tactics are a sure sign that a lender is more concerned about selling you a loan than meeting your needs.

Loan Servicing

At loan closing, most lenders transfer their loans to another office or company specializing in servicing the loan from that point forward. Ask each lender you are considering: "Who will service my loan after it closes?"

Request a sample of the account statements the servicer would send you. Make certain you fully understand all the information on these statements. In particular, if you are considering a HECM creditline, find out how the servicer would keep you informed about the growing amount of credit a HECM provides (see Part 3).

Professional Commitment

A commitment to meeting consumer needs can be seen in a lender's professional relationships and consumer information.

For example, members of the National Reverse Mortgage Lenders Association (NRMLA) have developed "best practices" for their industry. For more information, go to **www.reversemortgage.org**. If you don't want to be contacted by a NRMLA lender, however, be sure to state that preference if you request any NRMLA publications.

Lenders committed to the highest standard of consumer information can provide loan analyses and comparisons that meet AARP's model specifications as discussed in Part 3. For the latest information on lenders who can provide this type of consumer information, go to **www.aarp.org/revmort**. But please note that AARP does not endorse any reverse mortgage product or lender.

Spending Your Equity

How much of your available loan amount would you take as a lump sum, as a creditline, or as a monthly advance? For what reasons would you take withdrawals from a HECM creditline?

You need to consider these questions carefully, especially if your home equity is one of your few financial assets. Very simply, the more equity you use now, the less will be left in the future. If you spend all your equity too soon, it may become financially difficult for you to remain living in your home.

For example, if you have to move due to disability or failing health, you would need to pay for the cost of moving, future living expenses, and possibly assisted living or other types of care. So the amount of equity remaining at the end of your loan could be vitally important to you.

Leftover Estimates

HECM counselors and lenders can estimate how much equity would be left at various future times based on assumptions about future interest rates, your loan advances, and about changes in your home's value.

These estimates generally assume that your home would be sold to repay the loan. So they deduct the estimated cost of selling your home from your remaining equity.

Then it's a simple calculation: If the estimated net sale proceeds are greater than your estimated debt, you (or your heirs) would get the difference in a lump sum of cash. If at any point your rising debt catches up to your home's value, then there would be no equity left.

Realistic Estimates

Unless your counselor or lender uses computer software based on AARP's model specifications discussed in Part 3, the leftover estimates they provide may have serious shortcomings.

Most reverse mortgage borrowers select a creditline. The amount of leftover equity at the end of a creditline loan depends primarily on the size and timing of the cash advances a borrower requests during the loan.

Computer software based on the model specifications lets you enter the creditline draws that you expect to make. This gives you a more accurate estimate of the equity that would remain if your loan were to end at various points in the future. Other loan software may not permit you to see how your expected creditline draws would affect your remaining equity.

Other loan software may also assume that the initial interest rate charged on your loan will never change. But that may be unlikely after a time of relatively low interest rates over the past several years. So this assumption may overestimate your future leftover equity.

Software based on the model specifications lets you select the interest rate used to estimate your leftover equity. So you can choose a higher rate than the one that is initially charged on your loan.

By varying these factors, you can see how much effect each can have on your leftover equity. You should remember, however, that all of these figures are estimates. The actual figures will depend on:

- the actual creditline advances you select during the loan;
- the actual interest rates charged on the loan; and
- the actual changes in your home's value during the loan.

Creditline Growth

Most HECM borrowers put all of their available cash into a creditline. So it's important to be able to see how creditline withdrawals affect the growing amount of credit available from a HECM.

The calculator at **www.aarp.org/revmort** (click on "Reverse Mortgage Calculator") can show you the effect of various creditline withdrawal patterns

on a year-by-year basis. To see them, run the calculator and then on the "Loan Calculator Estimates" page click on the "Creditline" button toward the bottom of the page, and follow the instructions.

Computer software based on AARP's model specifications discussed in Part 3 can also show the effect of different creditline withdrawals on your future loan balance, total amount owed, and total annual average loan cost.

If you take a HECM creditline, keep an eye on its growth. Being aware of how much cash remains in your creditline and the rate at which it is growing will help you make decisions about making cash withdrawals.

Remember, you can control the amount of credit that remains in your account. The less cash you take out now, the more will remain for later. It doesn't make much sense to set up a creditline and then not use it. But you should also avoid using too much too soon if you can.

For example, if you spend all the cash in your creditline, will you still be able to pay your property taxes and homeowner's insurance? If you fail to make these payments, and there is no cash left in your creditline, a HECM lender can foreclose on your loan. Just like with a forward mortgage, if you do not pay your property taxes and insurance, you could lose your home.

So be certain to leave enough cash in your creditline to pay your taxes and insurance if you do not have other funds available for this purpose.

Investing

Investing the money you get from a reverse mortgage is not wise. It is extremely unlikely that you could safely earn more from an investment than the loan would cost. Besides, the funds you do not spend from a HECM creditline grow larger at a greater rate than you could safely earn.

Careful Spending

Be wary of anyone who wants to sell you something, and suggests a reverse mortgage as a way to pay for it. Be especially wary if

- you do not fully understand what they are selling; or
- you are not certain that you need what they are selling.

Remember that the total cost to you equals the cost of what they are selling plus the cost of the reverse mortgage. If you conclude that you do need what they are selling, be sure to shop around before making a decision. You are under no obligation to buy goods or services from the party that suggested you borrow against your home to pay for them.

For example, if an insurance agent tries to sell you an annuity by way of reverse mortgage financing, be sure to check out all the cautions about these types of arrangements on the "Spending Your Equity" page at **www.aarp.org/revmort**.

Refinancing

After you get a reverse mortgage, sometime in the future you may be able to increase the loan funds available to you

by refinancing the loan. Large increases in your home's value, increases in HUD's home value limit (currently $417,000), or lower interest rates could make this possible.

When you refinance a HECM, lenders are required to show you the total cost of refinancing, and compare it to the increase in available loan funds that a refinance would provide.

This comparison makes it easy for you to see the total costs that would be added to the amount you owe versus the additional loan funds that would become available to you. If you need help understanding the comparison, HECM counselors can explain it to you.

Glossary

acceleration clause
the part of a contract that defines when a loan may be declared due and payable

adjustable rate
an interest rate that changes, based on changes in a published market-rate index

appraisal
an estimate of a home's market value

appreciation
an increase in a home's value

Area Agency on Aging (AAA)
a local or regional nonprofit organization providing information on services and programs for older adults

cap
a limitation on the amount by which an adjustable interest rate may change during a specified time period

closing
a meeting at which legal documents are signed to "close the deal" on a mortgage; the time at which a mortgage begins

CMT rate
the Constant Maturity Treasury rate, used as an interest rate index in the HECM program

condemnation
a court action adjudging a property to be unfit for use, or converting a private property to public use under the right of eminent domain

creditline
a credit account that permits a borrower to control the timing and amount of the loan advances; also known as a "line-of-credit"

current interest rate
the interest rate currently being charged on a loan

deferred payment loans (DPLs)
reverse mortgages providing lump sums for repairing or improving homes, usually offered by state or local governments

depreciation
a decrease in the value of a home

eminent domain
the right of a government to take private property for public use, for example, to build a highway

expected interest rate
in the HECM program, the interest rate used to determine a borrower's loan advances

Fannie Mae
a private company that buys and sells mortgages; a government-sponsored entity that operates under the general oversight of the federal government

Federal Housing Administration (FHA)
the part of HUD (the U.S. Department of Housing and Urban Development) that insures HECM loans

federally insured reverse mortgage
a Home Equity Conversion Mortgage (HECM) (see below)

home equity
the value of a home, minus any debt against it

home equity conversion
turning home equity into cash without having to leave your home or make regular loan repayments

Home Equity Conversion Mortgage (HECM)
the only reverse mortgage program insured by the Federal Housing Administration (see Part 3)

home value limit
in the HECM program, the largest home value that can be used to determine a borrower's loan advance amounts

initial interest rate
the interest rate that is first charged on a loan beginning at closing

leftover equity
the net proceeds from selling a home, minus the total amount of debt owed against it

LIBOR
the London Interbank Offered Rate, used as an interest rate index in the HECM program

loan advances
payments made to a borrower, or to another party on behalf of a borrower

loan balance
the amount owed, including principal and interest; generally capped (limited) in a reverse mortgage by a non-recourse limit

lump sum
a single loan advance at closing

margin
in the HECM program, the amount added to an interest rate index to determine the initial, current, and expected interest rates

maturity
when a loan becomes due and payable

model specifications
a detailed set of rules for analyzing and comparing reverse mortgages (see Part 3)

mortgage
a legal document making a home available to a lender to satisfy a debt

non-recourse mortgage
a home loan in which a lender generally may look only to the value of the home for repayment

origination
the overall administrative process of setting up a mortgage, including the preparation of documents

property tax deferral (PTD)
reverse mortgages providing annual loan advances for paying property taxes, usually offered by state or local governments

proprietary reverse mortgage
a reverse mortgage product owned by a private company

reverse mortgage
a non-recourse loan against home equity providing cash advances to a borrower and requiring no repayment until a future time

right of rescission
a borrower's right to cancel a home loan within three business days of closing

servicing
performing administrative functions on a loan after closing

Supplemental Security Income (SSI)
a federal program providing monthly cash benefits to low-income persons aged 65+, blind, or disabled

tenure advances
fixed monthly loan advances for as long as a borrower lives in a home

term advances
fixed monthly loan advances for a specific period of time

Total Annual Loan Cost (TALC) rate
the projected annual average cost of a reverse mortgage including all itemized costs

More Information Online

To get the latest information on reverse mortgages, visit AARP's website at **www.aarp.org/revmort**. There you will find more details and more up-to-date coverage of the topics presented in this booklet.

Appendix:
Rising Debt and Falling Equity

The purpose and operation of a reverse mortgage are different from those of a standard "forward" mortgage. The purpose of a forward mortgage is to purchase a home; the purpose of a reverse mortgage is to generate cash.

In a forward mortgage, your home equity increases over time. Your loan balance (the amount you owe) decreases as you make monthly repayments to the lender. Meanwhile the value of your home is usually increasing. Forward mortgages are "falling debt, rising equity" transactions (see Table A-1).

In a reverse mortgage, your home equity generally decreases over time. Your loan balance rises as loan advances are made to you by the lender, interest is added to the outstanding loan balance, and you make no repayments to the lender. Unless the home appreciates (grows in value) at more than a moderate rate, the loan balance starts "catching up" to the home. Reverse mortgages are typically "rising debt, falling equity" transactions (see Table A-1).

A simplified example of a reverse mortgage is presented in Table A-2. The purpose of this table is to show the "rising debt, falling equity" characteristics of reverse mortgages in general. To simplify the example, the table does not include all the closing costs and fees that are generally charged by a mortgage company or bank. It also does not include the costs of selling a home, which typically reduce the amount of equity remaining at the end of the loan.

In the example, you can see that the $1,000 monthly loan advances in column A are added to the monthly interest at 0.5% in column B to equal the loan balance (amount owed) in column C. Over time, the loan balance grows larger. You can also see that the loan balance is subtracted from the home's value (assumed to be growing at 4% per year) in column D to produce the amount of remaining home equity in column D-C.

Table A-1:
Comparison of Typical "Forward" and Reverse Mortgages

Item	"Forward" Mortgage	Reverse Mortgage
Purpose of loan	to purchase a home	to generate income
Before closing, borrower has...	no equity in the home	a lot of equity in the home
At closing, borrower	owes a lot, and has little equity	owes very little, and has a lot of equity
During the loan, borrower...	makes monthly payments to the lender loan balance goes down equity grows	receives payments from the lender loan balance rises equity declines
At end of loan, borrower...	owes nothing has substantial equity	owes substantial amount has much less, little, or no equity
Type of Transaction	Falling Debt-Rising Equity	Rising Debt-Falling Equity

Table A-2: Simplified* Reverse Mortgage Example

Assumptions:

Monthly Loan Advance	$1,000
Monthly Interest Rate	0.5%
Original Home Value	$200,000
Appreciation Rate	4% per year

	A	B	C	D	(D-C)
End of Year	Principal Advances	Interest@ 0.5%/mo.	Loan Balance	Home Value	Home Equity
1	$12,000	$397	$12,397	$208,000	$195,602
2	24,000	1,559	25,559	216,320	190,760
3	36,000	3,532	39,532	224,872	185,339
4	48,000	6,368	54,368	233,971	179,602
5	60,000	10,118	70,118	243,330	173,211
6	72,000	14,840	86,840	253,063	166,222
7	84,000	20,594	104,594	263,186	158,591
8	96,000	27,442	123,442	273,713	150,270
9	108,000	35,453	143,453	284,662	141,208
10	120,000	44,698	164,698	296,048	131,349

*Illustrative example only; does not include loan closing costs and fees, or home selling costs. For complete cost example, see Part 3, Tables 3 and 4.

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For more information, go to AARP.org **Reverse Mortgage section** at **www.aarp.org/revmort**.

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