Tapping Home Equity: Reverse Mortgages

Bill Rives, Ph.D., CLU®, ChFC®, RHU®
Department of Finance
Fisher College of Business
The Ohio State University

Agenda

- What is a reverse mortgage?
- Borrower requirements
- Property requirements
- Payment plans
- Reverse mortgage costs
- Some cheap advice

What is a Reverse Mortgage?

- **A reverse mortgage is a <u>loan</u>**
  - You use a portion of your home's equity as collateral
  - The loan does not have to be repaid until the last surviving homeowner moves out of the residence – thus you cannot outlive a reverse mortgage
  - At this point, the estate has roughly 6 months to repay the balance on the loan (usually by selling the home)
  - Equity in excess of the loan balance belongs to the estate
  - The estate is not personally liable if the home sells for less than the loan balance (the lender assumes this risk)

Borrower Requirements

- **FHA Home Equity Conversion Mortgage (HECM)**
- **To be eligible:**
  - All homeowners must be at least 62 years old; each must have his/her name on the title
  - You must own the property "free and clear"
  - You must occupy the property as your principal residence
  - All taxes must be current (no delinquent taxes)
  - You must attend a HUD consumer information session
  - There usually are no income or credit score requirements

Property Requirements

- **Qualifying properties:**
  - Single-family home (built on site)
  - 2-4 unit residence with one unit occupied by the borrower
  - HUD-approved condominium project
  - HUD-approved manufactured home
- **Homes must meet FHA property standards and flood requirements**
  - Hazard and flood insurance premiums may be verified
  - Minimum insurance coverages must be maintained

Payment Plans

- **You can select from 5 payment plans:**
  - **Tenure**

    Equal monthly payments as long as an owner lives in the residence
  - **Term**

    Equal monthly payments for a fixed time period
  - **Line of credit**

    Periodic (installment) payments withdrawn at borrower's discretion
  - **Modified tenure**

    Combination of a line of credit and tenure payments
  - **Modified term**

    Combination of a line of credit and payments for a fixed time period

Reverse Mortgage Costs

- **There are 5 categories of loan fees:**
  - FHA mortgage insurance premium (initial and annual) to support loan guarantees
  - Third-party charges (e.g., appraisal, title search)
  - Loan origination fee (2% of the first $200,000 of property value, plus 1% of the value in excess of $200,000, up to the FHA lending limit, not to exceed a fee of $6,000)
  - Servicing fees (annual cost of maintaining the loan)
  - Interest charges (fixed rates 3% to 4%, variable rates are available in some markets)

Some Cheap Advice

- **Points to consider:**
  - Reverse mortgage fees are high, due largely to insurance costs that support loan guarantees
  - Because the loan balance grows over time, the remaining equity for estate / inheritance can decrease over time
  - A reverse mortgage may affect eligibility for Medicaid and other need-based government assistance
  - A reverse mortgage is a complex transaction; you need a professional counselor to advise you
- **Use a Home Equity Line of Credit (HELOC)?**

THANK YOU!!

Dr. Bill Rives

rives_4@fisher.osu.edu

(614) 326-0613