

REVERSAL OF FORTUNE

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Another day... another attempt at separating senior citizens from their money.

The air waves are being blanketed with advertisements for reverse mortgages. They are being sold as a cure-all for retirement financing, easy living, and in some cases a fantastic and astute means to finance other investments. The reality is that this could not be farther from the truth. Reverse mortgages can be to the advantage of senior homeowners who wish to remain in their residence, but are having difficulty keeping up with the mortgage payments, or have no other means of funding for unexpected expenses. Reverse mortgages are a vehicle whose use should be rare at best. Unfortunately they are being marketed like common aspirin, a cure all.

There are three options for older homeowners who wish to tap into the equity of their home.

1. Sell, and downsize
2. Take out a home equity loan.
3. Get a reverse mortgage.

A reverse mortgage is an interest-bearing loan secured by the equity in your home. To be eligible, the borrowers must own the home and be 62 years or older, however certain lenders are now offering them to people as young as 60. Similar to a home equity loan, the reverse mortgage allows one to convert their home equity to cash to use for whatever purpose the borrower wishes. Reverse mortgages, unlike other home loans do not require the borrower to make ANY INTEREST OR PRINCIPAL PAYMENTS THROUGHOUT THE LIFE OF THE LOAN. From that fact alone one can understand why unscrupulous financial advisors are salivating. The interest is added to the principal which is called rising debt. Unless the borrower opts for a fixed term the loan becomes due when the borrower dies, sells the home, or is out of the home for at least 12 months (nursing home or assisted living facility). When any of those events come to pass, you or your heirs must repay the loan, including all compounded interest in full. Usually what occurs is the house is sold, and the proceeds are used to repay the loan.

Like traditional mortgages and home loans interest will be charged. However, in the case of reverse mortgages, the interest is much higher. In addition, the fees and costs associated with reverse mortgages are often higher as well, sometimes as high as 8% of the total loan amount (think commission). Another point that is often missing from the Robert Wagner sales pitch is the fact that you are still the owner of the home and therefore are responsible for the property taxes, insurance and maintenance. If you are unable to meet these obligations, the lender will have the right to foreclose, leaving you with no place to live and no home equity to draw upon. If there is ever a point in time that you wish to downsize or move to assisted living facility for reasons other than costs, your loan will become due. With all the compounding interest, you might be quite surprised with how much money you owe, which can restrict options.

Deciding whether or not to tap into ones home equity through a reverse mortgage for retirement needs should be viewed as a last resort. Factors that determine whether or not one should check into the Last Chance Saloon depends on: your health, your spouse's health, your various income sources, the reasoning behind the loan, timing, estate and legacy planning and use of the loan's proceeds. The unfortunate reality is that reverse mortgages are being marketed and sold incorrectly with the usual pie-in-the-sky, Lifestyles of the Rich and Famous mentality. You DO NOT take out a reverse mortgage to fund vacations, boats, second homes, club memberships and other investments. Call it the double whammy; an unscrupulous financial advisor gets a hefty commission when selling a reverse mortgage and gets another fat check when convincing the senior to use the proceeds to fund another can't miss investment.

The original intent regarding the utilization of reverse mortgages was for aging, low-income homeowners to be able to keep their homes by providing a source of additional income to meet expenses. Crooked advisors are coming to the realization that retiring baby-boomers are sitting on immense pools of home equity capital that they are more than willing to drill for. Reverse mortgages are being marketed as way to enhance unaffordable and unrealistic retirement lifestyles. Home equity is an important building block of ones financial plan. Reverse mortgages can be a fantastic tool for helping seniors faced with losing their homes. For everybody else, it is the fast track to depleting the blood, sweat and tears you put into building home equity.

Tips When Considering Reverse Mortgages:

- **Weigh All Your Options:** Whether you need money to pay bills, or just want some extra cash, a reverse mortgage should ideally be a last, not a first, resort. Does it make more sense to sell your house and either downsize or rent while carefully investing the sale proceeds? Take out a home equity loan or line of credit? Can you consolidate credit card debts? Even if you are having trouble paying for your taxes or for home maintenance, there may be local government assistance programs that can help. Whatever your situation, ask your state agency on aging about less risky, or lower cost, ways to address your needs.
- **Understand the Risks, Costs and Fees:** Just because you won't be making any interest payments as long as you live in your home doesn't mean the interest rate doesn't matter. If you do decide to move, for whatever reason, you will have to pay back the loan plus compounded interest. The same is true if you have to leave your home, for whatever reason, for more than 12 months. Be sure to ask about all costs and fees, including any prepayment penalties.
- **Recognize the Full Impact of Your Decision:** While you typically do not have to pay taxes on the proceeds of a reverse mortgage, the income or lump sum you receive could impact your eligibility or your spouse's eligibility for various state and federal benefits, including Medicaid. In addition, depending on the laws of your state, a reverse mortgage may not enjoy the same home-equity protection that would otherwise apply if you have a health emergency and need to enter a nursing home and your spouse must liquidate assets to pay for that care. Finally, a reverse mortgage is generally not the right choice for those who want to leave their homes to their heirs.
- **Get Independent Advice:** Reverse mortgages are such complicated transactions that the federal government requires borrowers to meet with HUD-approved counselors before obtaining a federally guaranteed loan. (Most loans are federally guaranteed, but increasingly lenders are offering proprietary loans that are not.) Make sure that any counselor recommended by your lender is truly independent by asking whether he or she receives any funding from the lender or the mortgage industry. Even if you are applying for a loan that is not federally guaranteed, it is a good idea to get advice from a trusted financial adviser who has no interest in either the mortgage or any investment you plan to make with the proceeds. In any event, before you agree to a reverse mortgage, be sure to consult with legal and tax professionals who know the consequences of reverse mortgages for residents of your state and who are not connected in any other way to the transaction or the lender.
- **Be Skeptical of Reverse Mortgages as Part of an Investment Strategy:** If someone urges you to obtain a reverse mortgage to make an investment or purchase an insurance product or a security, such as a deferred annuity, be very skeptical, particularly if they are promising high returns. In essence, they are encouraging you to speculate with your home equity, which you may need for more critical purposes down the road. Also

consider what will happen if the returns turn out to be less than promised, or worse, you lose the principal. If you cannot sustain that kind of low return or loss, you should probably not be making the investment with your home equity.

- **Ask the Right Questions About the Proposed Investment Strategy:** Reverse mortgages are an extremely costly way to fund an investment. Before you obtain a reverse mortgage for investment purposes, make sure you understand both the terms of the loan AND the terms of the investment. What fees must you pay, directly or indirectly, for the reverse mortgage? What are the costs and fees associated with buying the investment? With selling it? How easy will it be to get your money out if you need it suddenly? Does the investment have a long surrender or lock-up period? What is the potential downside? Is it marketed and sold by the same person or entity that is offering the reverse mortgage? How is the reverse mortgage broker compensated? How is the seller of the investment compensated?

Source Material:

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