

Reverse Mortgages Basics

Senior homeowners sometimes find themselves in need of greater cash flow. If you find yourself in this position, you might be able to utilize the equity you've built in your home in lieu of taking out a second loan or selling your property. What you can do is take advantage of what's called a reverse mortgage. A reverse mortgage is a unique type of loan that can be a great way to brighten your overall financial picture.

The Benefits

What exactly is a reverse mortgage? Just like the phrase says, a "reverse" mortgage means that instead of making monthly mortgage payments, you *receive* them instead. These cash payments are tax free, and in most cases will not affect your Social Security or Medicare benefits. You won't ever have to face the prospect of being forced out of your home. Moreover, the loan does not have to be repaid at all unless you move, sell the home, or pass away. If you are able to get this type of loan, the sum you can borrow will depend on your age (generally, the older you are, the more you'll be able to receive), the specific type of reverse mortgage it is, your home's value, where it's located, and current interest rates.

Here are the basic requirements needed in order to qualify for a reverse mortgage:

- You have to be at least 62 years old
- You must reside in the home
- The home must have equity in it

The following are a few types of reverse mortgages:

- **Single-purpose reverse mortgages** are offered to low or moderate-income seniors by some government and nonprofit organizations. On the plus side, borrowing costs tend to be more inexpensive with this type of loan. However, availability can be limited, they can be restricted by your income, and the cash you receive can only be used for such purposes like home improvements, repairs, or property taxes.
- **Home Equity Conversion Mortgages (HECMs)** are widely available and backed by the Department of Housing and Urban Development (HUD). There are no income restrictions or medical requirements and you can use the money for whatever you like. The catch is that to get a HECM, the majority of your existing mortgage must be paid off, and you must first meet with a HUD-certified counselor who will explain the loan to you in detail.
- **Proprietary reverse mortgages** are private loans. They are typically the most expensive option. They may be suitable if your home's value is very high; they can give larger cash advances than HECMs. There are no income limits and the money can be used for any purpose.

The Drawbacks

Although reverse mortgages can be helpful in that they increase your cash flow, be aware that there are a few downsides to consider:

- These loans are not free! They come with origination fees, closing costs, and servicing fees, all of which can be steep. Moreover, you will be charged interest on the outstanding balance.
- Most reverse mortgages have variable interest rates. In other words, if the rate goes up, the loan becomes more expensive.
- Your total debt will increase rather than decrease over time.
- Your heirs may inherit property with a large outstanding balance since you are using some or all of your home's equity,
- For tax purposes: you cannot deduct interest on reverse mortgages on your tax return until the loan is at least partially repaid.

Know Before You Borrow

It can be a challenge to choose which type of reverse mortgage to pursue. Be prepared to ask lots of questions, including:

- Is the interest rate I can receive fixed or variable?
- How much will the origination fee, closing costs, and servicing fees cost me?
- What will the Total Annual Loan Cost be?

HECM and proprietary loans can seem almost identical in many ways, so request a side-by-side comparison from the lender or counselor when trying to decide between the two.

You should never feel any sales pressure when looking into reverse mortgages. Don't decide before you're ready or if you don't fully understand a product you're considering. If you change your mind, you can cancel (in writing) within three business days after signing a reverse mortgage contract, for any reason and without penalty. The lender must return any financing fees you may have paid once the loan is canceled.

The process of receiving a reverse mortgage usually turns out to be a positive experience. Fraud does exist, however. If you suspect illegal activity has taken place, don't hesitate to file a complaint with your state Attorney General's office or state banking regulatory agency, as well as the Federal Trade Commission: www.ftc.gov; 877-382-4357.

Resources

For more information about reverse mortgages, contact:

AARP Foundation
Reverse Mortgage Education Project
601 E Street, NW
Washington, DC 20049
800-209-8085
www.aarp.org/revmort/list

U. S. Department of Housing and Urban Development (HUD)
451 7th Street, SW
Washington, DC 20410
888-466-3487
www.hud.gov