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HUD PROPOSES MAJOR EXPANSION OF REVERSE MORTGAGE PROGRAM TO HELP MORE SENIOR CITIZEN HOMEOWNERS

WASHINGTON -- The Department of Housing and Urban Development proposed legislation today to dramatically expand a reverse mortgage insurance program, making millions of elderly homeowners eligible to borrow against the value of their homes.

HUD Secretary Henry Cisneros said the legislation, submitted to Congress today, would allow the Federal Housing Administration's reverse mortgage program to continue beyond its scheduled expiration in the year 2000.

HUD's proposed legislation would also remove the cap that limits the program to insuring 50,000 reverse mortgages -- clearing the way for hundreds of thousands of the loans to be made in the years ahead.

In addition, Cisneros said HUD will launch a major effort to make more older Americans aware of the reverse mortgage program and to provide counseling to help people determine if they would benefit from a reverse mortgage.

More than 12 million homeowners age 62 and older would be eligible to participate in the expanded reverse mortgage program, and the number would grow as the Baby Boom generation ages. To qualify for a reverse mortgage, borrowers must have paid off their home mortgages or have only a small mortgage balance remaining.

"Reverse mortgages reward older Americans who've worked hard all their lives and want to stay in their homes," Cisneros said. "The cash provided by these innovative loans makes a crucial difference in the lives of elderly homeowners."

A study by Cornell University estimated that over 620,000 poor elderly homeowners could raise their incomes above the poverty level with reverse mortgages. The study found that 87 percent of poor elderly homeowners have paid off their mortgages.

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While a traditional mortgage requires a homeowner to make monthly payments to a lender, a reverse mortgage allows the homeowner to receive payments from a lender on a monthly basis, in a lump sum, or as a line of credit. The lender recovers its loan plus interest when the home is sold.

FHA provides insurance on loans made by private lenders to elderly homeowners under the reverse mortgage program.

The program was capped at 50,000 loans and approved to run only until the year 2000 because it began as a demonstration program in 1989. More than 16,000 reverse mortgages have been issued so far under HUD's program.

The program's temporary nature, the loan cap, a shortage of counselors and limited outreach efforts to publicize reverse mortgages combined to hold down lender and borrower participation.

"The demonstration phase for HUD's reverse mortgage program is over," Cisneros said. "Our program is a proven success and we need to move forward to extend its benefits to many more older Americans."

About 125 lenders issue HUD's reverse mortgages everywhere in the United States except South Dakota (where no lender has been found) and Texas (where the State Constitution prohibits reverse mortgages).

Joseph S. Perkins, President-elect of the American Association of Retired Persons, said the group supports increasing the availability of reverse mortgages to older Americans.

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________________________________ said Perkins.

Cisneros said the citizen outreach and counseling programs will be launched with $200,000 in HUD funds. He said HUD will ask Congress for an additional $1 million supplemental appropriation this year. HUD will use the funds to:

- Expand counseling and education programs that provide details about receiving and repaying reverse mortgages. Telephone counseling will be offered to older people living in areas where there are shortages of counselors.

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- Produce brochures, public service announcements for the broadcast and print media, and videotapes explaining how the reverse mortgage program works. The brochures and videos will be distributed to lenders, senior citizen groups and individuals. Information will also be placed on the Internet.

- Provide information about FHA reverse mortgage insurance on a toll-free telephone line and mail callers additional material. The toll-free line is 1-800-217-6970.

In addition, AARP will use its publications, meetings and mailings to inform older Americans about reverse mortgages. HUD will work with other senior citizen organizations as well to also disseminate information to their members.

Among Americans 65 and older, 79.1 percent are homeowners -- the highest rate in history and up from 77.1 percent in 1992. A total of 83 percent of senior citizen homeowners have paid off their home mortgages.

HUD's reverse mortgage program is part of the Administration's National Homeownership Strategy. The strategy is designed to raise the national homeownership rate to an all-time high of 67.5 percent by the year 2000.

Since 1993 the number of American homeowners has increased by more than 3 million families.

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Is a Reverse Mortgage the Thing for You?

In the Right Circumstances It Can Work Wonders, but There Are Plenty of Reasons for Caution

By Albert B. Crenshaw
Washington Post Staff Writer

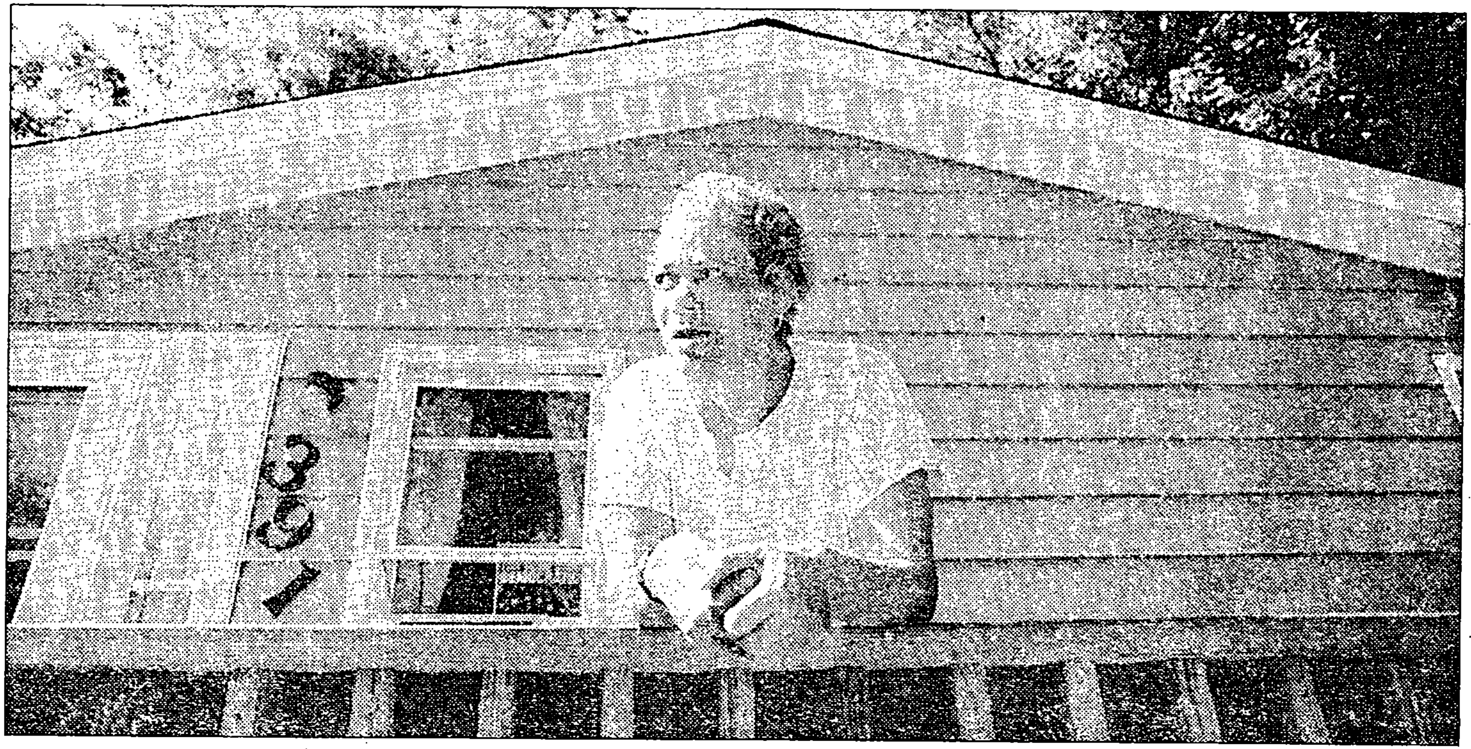
A couple of years ago, Sylvia Simpson was struggling. A widow in her sixties who had raised nine children and even managed to buy a house while working at mostly low-wage jobs, she had been forced by ill health to retire. With only Social Security and a small pension, she quickly found she couldn't make ends meet.

"I found myself in a dilemma. I wasn't able to pay taxes; the house was going down" because she couldn't afford the upkeep, and she even slipped behind on the mortgage she had had since 1979, she said.

But today, Simpson remains in her house in Kensington and her money worries are largely taken care of, thanks to an increasingly popular financing tool, the reverse mortgage.

These mortgages are loans that allow older people to tap the equity in their homes without having to sell or to take on conventional debt that would require monthly payments.

Equity is the market value of the house—what it could be sold for, minus any mortgage debt on it. Many seniors have substantial equity in their homes; they have been paying down their mortgage balances over



BY CRAIG HERNDON—THE WASHINGTON POST

For Sylvia Simpson of Kensington, a reverse mortgage meant access to $56,000 of the equity in her home, which she used to make improvements and set up a cash reserve. Reverse mortgages are growing in popularity, but many financial planners don't like them.

the years, reducing the debt, and they bought before the big run-up in real estate prices of the late 1970s and early 1980s.

In a normal mortgage, a home buyer begins with little or no equity and builds it up over the years with mortgage payments. In a reverse mortgage, the homeowner begins with a lot of equity and reduces it by borrowing against it.

There are no monthly or other periodic payments by the reverse mortgage borrower. Instead the lender waits for repayment until the borrower dies or moves out and the property is sold. At that point, the lender is entitled to a return of the principal and accrued interest.

For Simpson, a reverse mortgage meant access to $56,000 of the equity she had built up over the years. She was able to pay off her old mortgage, fix the leaking roof and add a small porch. She even has a reserve to draw on, should she need it.

Since the mortgage need not be repaid until she dies, moves or sells the house, her income is available for living expenses, and she is able to meet her other obligations. "I just added 10 years to my life. I don't have that pressure anymore," she said recently.

But in some situations, borrowing money against the value of your home can be expensive, and you may not get as much as you expect.

If demographers are right, thousands, perhaps millions, more Americans will be following Simpson's example in the coming decades. The reasons are both economic and emotional.

The nation's population is growing older, and for a majority of families the house is their largest asset. Not only have older people typically been paying down their mortgages for many years, but in many cases there has been substantial appreciation that has added handsomely to the equity.

However, as is reported almost daily in the news media, a great many of these families have done little other saving. After educating their children and perhaps helping support their own parents, a generation is facing retirement with modest cash resources and doubts about the ability of the government's Social Security and Medicare programs to help.

And with life expectancies at record highs, retirees will have to stretch their resources for 20, 25 or 30 years. "People could spend a quarter of their lifetimes in retirement," said Mathew H. Greenwald, a sociologist here who has studied retirement savings patterns.

To get by, many of these people will have to go to where the money is: their house. More than three-quarters of Americans 65 and older own their own homes, accumulating roughly $1 trillion of equity. But getting the cash out isn't easy.

Reverse mortgages are one way around this problem. For many, they may be the only practical way to hang on to their houses and put food on the table. However, experts caution that they can be very expensive, and that borrowers should be sure they understand all the ramifications, including the fact that the loan may eat up all the equity, leaving nothing for heirs.

Many financial planners don't like reverse mortgages. "We've looked at them extensively and we are not impressed. Conceptually it's a great idea. Unfortunately, the implementation . . . leaves a lot to be desired," said Ric Edelman of Edelman Financial Services in Fairfax.

Reverse mortgages have been around for a number of years, but only recently have they become common. The Federal Housing Administration gave them a boost seven years ago when it began a pilot program of government insurance that has encouraged lenders to try a market whose risks remain largely unknown.

FHA has insured 16,000 of these loans so far, and the Clinton administration has asked Congress to lift the ceiling of 50,000 loans and extend the program past the current deadline of 2001.

At the same time, other lenders are moving in. The Federal National Mortgage Association, or Fannie Mae, this year began its Home Keeper reverse mortgage program, and Household Finance and TransAmerica Corp. also have programs.

See MORTGAGES, Page 10

HOW IT WORKS: Assume the Smiths bought a house in 1965 for $28,000 and that last year its value had appreciated to $160,000, and their mortgage was paid off.

■ **Suppose they decide they need a reverse mortgage** to make ends meet. If they take a loan that would provide them with $300 a month, or $3,600 a year, at 1 percent per month interest, at the end of one year they would owe $3,600 of principal and $243 of interest for a total of $3,843. Their equity in their house, assuming no appreciation, would have declined to $156,157.

$160,000 (Equity)
— **3,600** ($300/month loan)
— **243** (1% interest/month)

$156,157 (Remaining equity)

■ **After five years,** they would owe $18,000 in principal and $6,746 in interest, for a total debt of $24,746. Their equity, again assuming no appreciation, would have declined to $135,254.

$160,000 (Equity)
— **18,000** ($300/month loan for 5 years)
— **6,746** (1% interest/month for 5 years)

$135,254 (Remaining equity)

■ **At the end of 10 years,** they would owe $36,000 in principal and $33,702 in interest for a total of $69,702. **Their equity would now be $90,298.** Note, though, that if their house had appreciated 2 percent a year over the 10 years, its value would have climbed to about $195,000, so that their equity would be slightly more than $125,000.

MORTGAGES, *From Page 9*

"We feel this is a market that is going to develop, possibly slowly at first, then grow much larger, maybe in five or more years," said Fannie Mae vice president Robert Sahadi. The company has done only about 100 Home Keepers so far, but has fielded 130,000 telephone inquiries since it announced the program earlier this year.

"There are a lot more choices now. That's good news for consumers," said Bronwyn Belling, a reverse mortgage expert with AARP.

At the same time, the various programs have significant differences in such things as fees, the way the amount that can be borrowed is calculated, and how it can be withdrawn by the homeowner.

"The moral is one size doesn't fit all," Belling said. "It used to be that the homeowner should look at the reverse mortgage and all the alternatives [to it]. Now they should look at each of the reverse mortgages as well."

In general, though, reverse mortgages work the same way:

The lender appraises the house and agrees to lend a certain amount of money against the homeowner's equity. The money usually may be taken as a lump sum, as a stream of payments, as a line of credit to be drawn down as needed or as some combination of these.

Repayment is not required until the owner dies, moves out of the house or sells it. At that point the entire loan (principal and interest) is due. The bank doesn't take title to the house. Instead the owner or heirs typically sell it and repay the loan out of the sale proceeds. If the house fetches more than the debt, they keep the excess. If it fetches less, that is the bank's loss.

Unlike a normal mortgage, where the interest rate is the key factor, "a reverse mortgage's ultimate cost depends on several things, some of which you don't know at the time you take it out," Belling said.

First, the lender cannot always be certain how much money will be borrowed nor when it will be repaid. This means that lenders make an actuarial calculation in figuring how much they will lend: The younger the borrower is and the longer the life expectancy, the smaller the amount that will be lent.

Different lenders use different formulas. Fannie Mae, for example, will generally lend less to a couple than to a single person because "with all other things equal, with two borrowers, one will outlive the actuarial expectations," said Laura Barriere of Fannie Mae.

Lenders also must gauge the future value of the property. Unlike a conventional mortgage, in which the loan balance is paid down over time, the loan balance in a reverse mortgage rises as interest accumulates along with the principal. Thus, for the lender to recover an investment the property must be worth as much as the principal and interest combined.

Lenders are limited to the value of the house. They cannot try to recover additional money from the borrower or heirs if the house sale doesn't cover the loan.

If the home more than covers the loan, the borrower or heirs get the excess, although some lenders will allow higher loan amounts in exchange for a percentage of the leftover equity. Borrowers or heirs are not required to sell the property, but they usually do. If they are able and wish to, they can repay the loan from other sources.

Interest rates are also high, in part reflecting the uncertainties in the product. Thus, if a borrower took a loan in the form of $300-a-month payments at 12 percent, after 10 years the debt would be $69,702, consisting of $36,000 in monthly loan payments and $33,702 in interest charges.

Thus, someone with a $300,000 or $400,000 house might be able to draw out only about $100,000, Belling said. She noted that it really isn't that different from a conventional mortgage, where the amount of interest paid over the life of the loan may be two, three or four times the principal.

"Still, it is somewhat of a sticker shock for some people to realize how little they can get," she said.

Fees such as appraisals, application costs and points also tend to be front-loaded, so reverse mortgages can be an expensive way to borrow money for someone who isn't able to stay in the house very long. In other words, borrowers agree to pay significant costs at the beginning; if they die or move away after only a few years, this sharply raises the effective cost.

On the other hand, borrowers who outlive expectations get a better deal. In fact, they may get a sort of windfall if their house depreciates or doesn't appreciate enough to cover the fees and interest, because their liability is legally limited to the value of the house.

"People who live too long and whose houses don't appreciate are basically subsidized by people who take out reverse mortgages and aren't able to stay in the house very long and have to pay them back," Belling said.

The Federal Reserve gave consumers a useful tool recently with new regulations that require lenders to provide the "total annual loan cost" to borrowers. This is an "all-in" amount showing how much the borrower would receive and how much would be owed two years after the loan closes, at the borrower's life expectancy and at 140 percent of the borrower's life expectancy.

The disclosure also includes what would be owed if the home appreciates at various rates.

In addition to the expense, reverse mortgages are likely to eat up the value of the house and thus the inheritance children may be expecting. Planners and other experts recommend exploring alternatives. Among them:

■ **Refinance.** Planner Edelman recommends refinancing when possible and advises clients to invest the cash and try to earn as much as possible. However, older homeowners with little income may have trouble qualifying for a new mortgage.

■ **Sell.** Many homeowners have ready markets for their houses, and a sale generates cash. But the owner then needs to find another place to live, something many seniors don't want to do. In some cases they may face painful capital gains taxes on the profits. President Clinton has proposed eliminating capital gains tax on sales of principal residences, which would help, but the prospects of that proposal are not clear.

Owners older than 55 can, of course, exclude from tax up to $125,000 of the gain on sale of their primary residence. But in areas like Washington, where prices have soared over the past 30 years, gains for long-time homeowners may still be large enough to make taxes a consideration.

If a reverse mortgage seems the best way to go, be sure to consult the rest of your family (especially heirs) and financial advisers. Indeed, most lenders require counseling before the loan closes. ■

Resources

■ The FTC, a government agency, offers a free "Facts for Consumers" flyer on reverse mortgages. Write to the Federal Trade Commission, Public Reference Branch, Room 130, Sixth St. and Pennsylvania Ave. NW, Washington, D.C. 20580.

■ The American Association of Retired Persons offers a free Home Equity Information Kit that includes a 47-page booklet entitled "Home-Made Money, a Consumer's Guide to Home Equity Conversion"; a four-page "Fact Sheet on Home Equity Conversion and Reverse Mortgages"; and a "Reverse Mortgage Lenders List." Send a postcard with your name and address to Home Equity Information Kit (D15601), AARP Fulfillment (EE01079), 601 E St. NW, Washington, D.C. 20049.

■ Fannie Mae, the big buyer of home mortgages, publishes "Money From Home: A Consumer's Guide to Reverse Mortgage Options." It's 106 pages and free. To get a copy call 800-7-FANNIE, or write Fannie Mae, Office of Public Information, 3900 Wisconsin Ave. NW, Washington, D.C. 20016.

■ National Center for Home Equity Conversion, an educational group in Minnesota, publishes "Your New Retirement Nest Egg: A Consumer Guide to Reverse Mortgages." It's 346 pages and costs $19.95. Order by mail from the National Center for Home Equity Conversion, 7373 147th St., Suite 115, Apple Valley, Minn. 55124. A state-by-state list of reverse mortgage lenders is available. Send $1 and a self-addressed, stamped envelope to Reverse Mortgage Locator at the same address.