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Reverse Mortgages: Changes Brought About by the Housing and Economic Recovery Act

I. INTRODUCTION

A reverse mortgage allows a homeowner to withdraw the equity in her home in the form of a loan with a balance that increases rather than decreases over time. Generally, the homeowner is not required to repay the loan until the home is sold. While this product can be beneficial for homeowners who have substantial home equity but insufficient income, this product has many drawbacks.

The media has reported a number of horror stories of elderly persons being pressured into reverse mortgage loans that they neither need nor want. For example, on the Consumer Reports website, there is an anecdotal story of an eighty-year-old woman who wanted to borrow some money “to fix her porch” but ended up getting a reverse mortgage for $209,000 and purchasing two annuities, including one with a withdrawal penalty of twenty percent for any withdrawals made during the first ten years.

In contrast, other consumers take out reverse mortgages to pay for luxury items that would otherwise be beyond their means.

1. E.g., U.S. Department of Housing and Urban Development, A Turning Point in the History of HUD’s Home Equity Conversion Mortgage Program, U.S. HOUSING MARKET CONDITIONS, 5, 6, First Quarter 2008 [hereinafter, HUD, A Turning Point].
For example, a borrower couple reportedly used proceeds from a reverse mortgage in order to take a trip to Cancun, Mexico.6

Consumer interest in reverse mortgages is expected to sharply increase over the next twenty years as the baby boomers reach age sixty-two, the age at which homeowners become eligible for a reverse mortgage.7 Between 2005 and 2015 the “owner heads of households” between the ages of sixty and sixty-nine is expected to increase by fifty-three percent.8

In a time of falling home prices, lenders may be opening themselves up to an unacceptable amount of risk by loaning money secured by an asset with a potentially declining value that could leave them unable to recover the entire amount of the loan.9 This may not be an issue, however, if the reverse mortgage is the type insured by the Federal Housing Authority (FHA), because if the value of the home is insufficient to cover the amount of the loan, the mortgage insurance will cover the remainder of the loan, limiting risk to lenders.10 An advantage to lenders is that reverse mortgage borrowers are less likely to default on their loans because no payments are due until the loan becomes due at the borrower’s death or transfer of the home, at which point homes may have regained some of the value they have lost.11

On July 30, 2008, George W. Bush signed the Housing and Economic Recovery Act (HERA)12 into effect. Although HERA focused more generally on preventing mortgage foreclosures on traditional mortgages, it also addressed many of the criticisms of reverse mortgages.13 Notwithstanding these important statutory changes, this Note will argue that there are still problems with reverse mortgages. These loans should be used with caution as

7. U.S. DEP’T OF HOUSING AND URBAN DEVELOPMENT, HECM Program: Coming into its Own, RESEARCH WORKS, Sept. 2008, at 3 [hereinafter HUD, HECM Program].
8. Id.
10. HUD, A Turning Point, supra note 1, at 6.
11. Id. at 10.
13. Id. § 2122 (to be codified at 12 U.S.C. § 1715z-20).
they may only be appropriate for a small segment of the population. Moreover, current real estate market conditions may work to reduce supply of this product as its demand increases.

Part II of this Note provides an overview of the history and mechanics of reverse mortgages. Part III addresses the perceived problems with reverse mortgages that HERA sought to address. Part IV considers the problems that still remain with reverse mortgages after the passage of the Act.

II. REVERSE MORTGAGE OVERVIEW

A. History of Reverse Mortgages

Reverse mortgages have been around since 1961, when the first reverse mortgage was originated in Portland, Maine. Nevertheless, they did not enter the mainstream until the Demonstration Program of Insurance of Home Equity Conversion Mortgages for Elderly Homeowners was established in 1988. This Demonstration authorized the FHA to insure 2,500 home equity conversion mortgages (HECMs) (a type of reverse mortgage) issued by the Department of Housing and Urban Development (HUD) through lending institutions selected by lottery. In 1998 the HUD Appropriations Act established HECM as a permanent program. This limit of 2,500 mortgages was gradually increased by amendments to 150,000 in 1998, and to

14. See infra Part II.
15. See infra Part III.
16. See infra Part IV.
20. HUD, A Turning Point, supra note 1, at 7.
275,000 in 2006.\textsuperscript{21} Fannie Mae established a secondary market for home equity conversion mortgages, which by increasing liquidity, helped increase the number of lenders willing to provide home equity conversion mortgages.\textsuperscript{22} In 2006, the first reverse mortgage-backed securities were issued and Fannie Mae announced that it would begin issuing HECM backed securities as well.\textsuperscript{23} In 2007, the National Reverse Mortgage Lenders Association and the Hollister Group LLC established a Reverse Mortgage Market Index, which catalogues information on reverse mortgages that is vital for investors.\textsuperscript{24} This information is expected to facilitate growth in the reverse mortgage secondary market, which should "boost liquidity to support such products and reduce borrower costs."\textsuperscript{25}

While there are many different types of reverse mortgages, this Note will focus on HECMs.\textsuperscript{26} The federal government

\begin{itemize}
  \item \textsuperscript{22} See HUD, \textit{A Turning Point}, supra note 1, at 10; Sawyer, supra note 17, at 622–623.
  \item \textsuperscript{23} HUD, \textit{A Turning Point}, supra note 1, at 10; National Reverse Mortgage Lenders Association, \textit{Fannie Mae Hopes to Expand Secondary Market for Reverse Mortgages}, Oct. 24, 2006, http://www.nrmlaonline.org/rms/secondary_markets.aspx?article_id=444 (stating that in 2006 there were two private securitizations, one using HECMs from Seattle Mortgage Company and the other using HECMs from Financial Freedom).
  \item \textsuperscript{24} Richard Cowden, \textit{Mortgages: Ginnie Mae Statement Recognizes Creation of First-Ever Reverse Mortgage Market Index}, 89 BNA BANKING REP. 43 (2007) (stating that the Index "provide[s] critical market, housing, and demographic data on reverse mortgages").
  \item \textsuperscript{25} Id. The secondary market enhances liquidity through the purchase of mortgages from lenders. These purchases provide cash to the lender which the lender can then use to make new loans. See Freddie Mac, \textit{Our Role Within the Secondary Market}, http://www.freddiemac.com/corporate/company_profile/our_role_secmkt/index.html (last visited Jan. 7, 2009).
  \item \textsuperscript{26} A popular type of reverse mortgages for individuals who own a home with a high appraisal value is a jumbo reverse mortgage, which has no set limit on the amount of the loan other than the value of the home. Yet, due to the failure of the main funders, Indy Mac Bank and Lehman Brothers, such reverse mortgages may no longer be available. \textit{Jumbo Reverse Mortgages: A Dying Breed}, HULIQ, Sept. 17, 2008, http://www.huliq.com/2818/68681/jumbo-reverse-mortgages-%E2%80%93-dying-breed. Another non-HECM option is the Fannie Mae Home Keeper reverse mortgage, which in one transaction, allows an individual to purchase a new home and take out a reverse mortgage on the property. See Wiener, supra note 6 (describing
established this type of reverse mortgage and it is insured by the FHA. The FHA insurance protects both the borrower and the lender by guaranteeing that the borrower will receive her payments and that the lender will receive the full amount of the loan if the value of the home at the time of sale is not sufficient for repayment. HECMs are also subject to the Truth in Lending Act. Ninety percent of all reverse mortgages are HECMs. Moreover, in a time of declining home prices, the availability of these non-HECM options is all but non-existent. Last year there were fifteen non-HECM reverse mortgage products, and by September 2008, Peter Bell, the president of the National Reverse Mortgage Lenders Association reported that only one or two were still available.

different reverse mortgage options). Public sector HECM’s are another option, but they are not widely available. See AARP, Selecting a Lender, http://www.aarp.org/money/revmort/revmort_decisions/a2003-03-27-lender.html (last visited Jan. 7, 2009). They are similar to other HECMs except that, unlike other HECMs which do not restrict the use of the loan proceeds, the loan proceeds in a public sector HECM must be used for a specified purpose, and generally an individual can have only one of these loans on their property. See Hammond, supra note 18, at 84, 91; AARP, Selecting a Lender, supra. An option available to some seniors is a private reverse mortgage funded by their children. In this scenario, the children take out a mortgage on their parents’ home to obtain capital to fund the reverse mortgage and then make payments to the parent. See Sawyer, supra note 17, at 646 (describing how a private reverse mortgage works and the benefits they offer). An alternative agreement, which is not a reverse mortgage, is a REX Agreement offered by REX & Co., where homeowners promise up to fifty percent of any increase in the value of their home as consideration for a cash payment by REX & Co. with no monthly payments. Eleanor Laise, Tapped Out: Pinched Consumers Scramble for Cash, WALL ST. J., June 2, 2008, at A1 (describing how a REX Agreement works); see also REX & Co., How It Works: You Shouldn’t Have to Make Payments to Unlock Your Own Equity, http://www.rexagreement.com/index.php/​rex/​how_it_works (last visited Feb. 8, 2009) (explaining how the REX Agreement works).

27. See Sawyer, supra note 17, at 625–626.
28. HUD, A Turning Point, supra note 1, at 6-7.
32. Id.
B. Who Qualifies for a Reverse Mortgage? How do they Work?

Similar to other FHA loans, the requirements for a HECM are more restrictive than other loans on the market. In order to qualify for an HECM, an individual must be at least sixty-two years old and own the home to be used as security for the reverse mortgage. There must be no debt secured by the home or any amount owed on a mortgage has to be paid off by the initial reverse mortgage proceeds. The home must be built for one to four families and the mortgagor must live in the home. Additionally, HUD has minimum standards for safety and structural soundness for any property FHA insures.

No minimum income, however, is required to qualify for a reverse mortgage, which makes this type of loan particularly attractive to low income seniors who might be unable to qualify for other types of loans. The FHA does require, however, that potential borrowers obtain counseling by an independent third party prior to taking out the loan. At this counseling session, prospective borrowers will learn the details of HECMs as well as alternative financial arrangements.

A reverse mortgage works much like the name implies. Instead of the borrower making monthly payments to the lender, as in a traditional mortgage, the lender (mortgagee) in a reverse mortgage makes payment(s) to the borrower (mortgagor). The mortgagor may elect to be paid in one of five different ways: equal monthly installments, a line of credit, a lump sum, monthly term

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33. 12 U.S.C. § 1715z-20(d) (2006) (listing the requirements to obtain a reverse mortgage); Hammond, supra note 18, at 91.
34. Sawyer, supra note 17, at 627.
38. HUD, A Turning Point, supra note 1, at 7 (describing the protections offered by the FHA).
39. Id.
40. Id. at 6 (describing the term “reverse mortgage”).
payments, or a combination thereof. Approximately three-quarters of borrowers elect to take out a line of credit. The amount that borrowers are eligible to borrow depends on their age, the value of their home, and the FHA loan limits. The older the homeowner, the more they are eligible to borrow. The mortgagor does not make any monthly payments, instead the loan does not become due until (i) the home is no longer the borrower’s principal dwelling; (ii) the borrower sells or otherwise transfers the home; or (iii) the borrower dies.

The loan is a “rising debt” loan, because the balance increases over time. The accruing interest and principal amount of the payments to the mortgagor are a lien held by the mortgagee on the home that must be paid once the mortgagor no longer lives in the home. The title remains in the name of the mortgagors and they may leave the property, subject to the reverse mortgage debt, to their beneficiaries as they could a property without a reverse mortgage. The loan is a non-recourse loan, meaning that the borrower cannot owe more than the value of the home.

III. PERCEIVED PROBLEMS WITH REVERSE MORTGAGES
ADDRESS BY HERA

In December 2007, the Senate Special Committee on Aging held a hearing regarding the HECM program. Several experts testified as to the program, its successes, and changes that needed

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41. See id. at 7 (describing the five payment options in more detail).
42. HUD, HECM Program, supra note 7, at 3.
43. Reverse Mortgages can be a Costly way to Tap Home Equity, CONSUMER REP., Oct. 2008, at 12.
44. Id. The borrower is not able to borrow up to the entire value of the home. HUD limits all payments to a “principal limit,” that is based on a calculation using a table of “principal limit factors” such as the borrower’s age and the interest rate. That factor is multiplied by the value of the home to determine the “principal limit.” HUD, A Turning Point, supra note 1, at 7.
45. 12 C.F.R. § 226.33, supra note 29 (describing the reverse mortgage requirements in detail).
46. See generally Hammond, supra note 18, at 86 (describing reverse mortgages).
47. Id.
49. See 12 C.F.R. § 226.33(a), supra note 29 (stating the loan is non-recourse); see also Reilly, supra note 48, at 19 (defining non-recourse loans).
Additionally in December 2007, the AARP Public Policy Institute issued its extensive report on reverse mortgages which included a number of proposed changes to the product. HERA addressed a number of the changes suggested by and criticisms from this testimony, report, and other critics. Part A of this subsection provides a general overview of HERA, while Parts B - G discuss individual changes HERA made to HECMs in direct response to some of the dominant criticisms of the program.

A. General Overview of HERA

HERA was passed for the broad purpose of “[providing] needed housing reform and for other purposes.” At the time of its enactment, the Act was “the most significant piece of financial services legislation to be enacted since the Gramm-Leach-Bliley Act of 1999.” It may have been eclipsed, however, by the Emergency Economic Stabilization Act of 2008, which was enacted October 3, 2008. HERA has three main subparts, the Federal Housing Finance Regulatory Reform Act of 2008, the Foreclosure Prevention Act of 2008, and the Housing Assistance Tax Act of 2008.

First, the Federal Housing Finance Regulatory Reform Act of 2008 created a new agency, the Federal Housing Finance Agency, and gave that agency authority over the Office of


51. AARP Report, supra note 30.


Finance, the Federal Home Loan Banks, Freddie Mac, and Fannie Mae.\(^\text{56}\) Fannie Mae and Freddie Mac were placed in government conservatorship in September, pursuant to HERA.\(^\text{57}\) The Act also increased the limits of the loans Freddie Mac and Fannie Mae can purchase to $417,000 for a single family residence, or up to a $625,000 limit in high-cost areas.\(^\text{58}\)

Secondly, the Act includes the Foreclosure Prevention Act of 2008 that increased the FHA loan limit to 115% of the median area home price and is intended to help families prevent foreclosure and encourage the purchase of properties that have been foreclosed upon.\(^\text{59}\) The changes to the HECM program were enacted under this subpart of HERA.\(^\text{60}\) The following describes the changes to reverse mortgages brought about under the Foreclosure Prevention Act.

B. Funding for Counseling

Before HERA was passed, in order to qualify for an FHA-insured HECM, mortgagors were required to have third-party counseling.\(^\text{61}\) This counseling included information about other financial options, financial effects of taking out a HECM, along with a disclosure that a HECM may affect the borrower’s ability to qualify for government assistance, may result in taxation, and that the borrower’s estate may be adversely affected.\(^\text{62}\) Private lenders have provided much of the funding for these counseling programs because Congress did not provide HUD adequate financing for the

\(^{56}\) Id. § 1311.


\(^{62}\) Id.
counseling (there was a cap of $1,000,000). This situation is problematic because private lenders may choose which programs to fund, thereby allowing them "to be the de facto arbiters of counseling quality." While most agree that an hour to an hour and a half is necessary for a counseling session to fully explain the process to the potential mortgagor, some seniors have reported that they were counseled for only around ten minutes regarding the loan.

HERA addressed two related problems regarding the counseling for reverse mortgages. First, it amends the counseling provision to require that counseling be provided "by an independent third party that is not, either directly or indirectly, associated with or compensated by a party involved in – (i) originating or servicing the mortgage; (ii) funding the loan underlying the mortgage; or (iii) the sale of annuities, investments, long-term care insurance, or any other type of financial or insurance product."

To help effectuate the change, HERA removed the annual funding cap of $1,000,000 for counseling and instead allows the HUD Secretary to use his or her discretion "to adequately fund" the counseling program. HERA also extends counseling to homeowners "who elect not to take out a [HECM]." These actions directly addressed concerns that the counseling provided to seniors was not objective and too closely tied to providers of reverse mortgages, annuities, and other products. Adequate

63. 12 U.S.C. § 1715z-20(m) (2006) (stating that “up to a total of $1,000,000 shall be available” to fund counseling); AARP Report, supra note 30, at 116 (describing the problems with counseling and the importance of government funding for counseling).

64. AARP Report, supra note 30, at 116.


67. Id. § 2122(a)(8) (to be codified at 12 U.S.C. § 1715z-20(I)). However, the removal of this cap does not guarantee that the counseling will be adequately funded, or that HUD will have the money to fund it.

68. Id.

69. Duhigg, Tapping into Homes Can Be Pitfall for the Elderly, supra note 65.
funding is necessary in order to provide objective counseling funded through HUD.  

C. Inconsistent Maximum Loan Amounts

Prior to HERA, two homes with the same appraisal value and homeowner equity could each have a very different maximum loan amount depending solely on their geographic location. This variance was due to the loan limits set by the FHA that varied by county from $200,160 to $362,790. Thus, someone who owned a high value home and lived in a county with a low maximum cap would be unable to tap into additional equity beyond the loan limit. The higher amount of equity merely provided “an extra cushion against claims” for the lender and FHA.

Like it did for “forward” mortgages, HERA increases the maximum loan limit for reverse mortgages to $417,000 for a single-family residence with the limit adjusted for inflation annually. The Act also includes an increase in the maximum loan amount for high-cost areas to “the lesser of 150% of such limitation for such size residence or the amount that is equal to 115% of the median house price in such area for such size residence.” This works out to a maximum of $625,500 for a loan secured by a single-family residence, adjustable for inflation. This increased national loan

70. See AARP Report, supra note 30, at 116.
71. See Meg Burns Statement, supra note 50 (explaining why there needs to be an increased national loan limit for reverse mortgages); Reilly, supra note 48, at 40.
72. Brandon, How the Housing Law Affects Reverse Mortgages, supra note 3. See 12 U.S.C.A. § 1717(b)(2) (2001) (stating that the loan limit “may be increased by the corporation (taking into account construction costs) not to exceed 240 per centum of such dollar amounts in any geographical area for which the Secretary of Housing and Urban Development determines . . .”).
73. See Reilly, supra note 48, at 40; AARP Report, supra note 30, at 110.
75. Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, § 1124, 122 Stat. 2654 (2008) (to be codified at 12 U.S.C. § 1717(b)(2)) (stating that the limit for a two family residence is $533,850, the limit for a three family residence is $645,300, and for a four family residence the limit is $801,950).
76. Id.
77. Id.
78. See id. (150% of $417,000 is $625,500).
limit may make HECMs more attractive to homeowners with home equity above the old limit, who could previously only access this additional equity if they took out a private reverse mortgage without a loan cap. Taking out a HECM instead of a private reverse mortgage will allow these borrowers to take advantage of the protections uniquely offered by HECMs. This increased limit will therefore allow HECMs to further increase their market share by allowing them to compete with private lenders for homeowners with greater equity, meaning that more potential borrowers will receive independent third party counseling before taking out a reverse mortgage.

The increased national limit has taken on an even greater importance following the failures of IndyMac and Lehman Brothers, who were the two main lenders of the jumbo reverse mortgages. The HECM may be the only reverse mortgage option available for many seniors, and an increased national limit will assist in enabling the HECM to serve seniors with equity in their homes that exceeds the former localized loan caps.

79. See Meg Burns Statement, supra note 50 (explaining the need for a higher national loan cap); see also David T. Rodda, et al., U.S. DEP’T OF HOUSING AND URBAN DEV., EVALUATION REPORT OF THE FHA HOME EQUITY CONVERSION MORTGAGE INSURANCE DEMONSTRATION 61 (2000) [hereinafter Rodda, Evaluation Report] (explaining that low loan limits are a deterrent to some homeowners).

80. HUD, A Turning Point, supra note 1, at 7 (describing the counseling requirement required for HECM borrowers and the guaranteed loan payment by HUD).

81. See Meg Burns Statement, supra note 50 (describing the importance of an increased national loan limit); see also HUD, A Turning Point, supra note 1 at 7 (describing the HECM counseling requirement as a “protection”).

82. Hulio, supra note 26. A private equity company, Dune Capital Management, was formed to purchase IndyMac, including Financial Freedom, in a deal that is expected to close by March 31, 2009. The Associated Press, Equity Partnership is Formed to Buy Remnants of IndyMac Bank for $13.9 Billion, N.Y. TIMES, Jan. 3, 2009, at B3.

83. See Hulio, supra note 26; see also Brad Finkelstein, Inlanta Reverses Up to 30% of Volume, HOME EQUITY WIRE, Sept. 1, 2008, at 3 (stating that “[j]umbo programs are non-existent right now”).
D. High Cost of a Reverse Mortgage

With substantial upfront fees and interest accruing on the principal, the cost of a reverse mortgage is high. In fact, sixty-three percent of individuals considering reverse mortgages do not even apply for one due to the "high cost." Before the passage of HERA, the origination fees for an HECM were two percent of the value of the home, up to a maximum of $7,256, regardless of the amount of the actual mortgage. When initially taking out the loan, mortgagors must also pay two percent of the value of the maximum amount that can be borrowed, and then another one-half percent annual premium. In addition, as with any mortgage, there are closing and appraisal fees.

With a reverse mortgage, the mortgagor does not make monthly payments and, thus, the debt increases as the interest accrues and the equity in the home decreases, opposed to a traditional mortgage, where the debt decreases as the equity increases. The interest on the money borrowed compounds, making a reverse mortgage a rising debt loan.

The new law reduces the maximum cap on the origination fees from $7,256 to $6,000, which is a change many critics demanded, making the loan more affordable to seniors. The origination fee under the new Act "shall be equal to [two] percent of the maximum claim amount of the mortgage, up to a maximum claim amount of $200,000 plus [one] percent of any portion of the

86. AARP Report, supra note 30, at 110 (stating that FHA loan section 203(b) set the maximum at $7,256).
89. Duhigg, Tapping into Homes Can Be Pitfall for the Elderly, supra note 65.
90. See id.; see also Powell, supra note 84.
91. See AARP Report, supra note 30 at 110 (discussing maximum origination fee amount); see also Brandon, How the Housing Law Affects Reverse Mortgages, supra note 3 (discussing the reduced maximum fee amount brought about by the Act).
maximum claim amount that is greater than $200,000." These fees are capped at “a maximum origination fee of $6,000” adjustable “in accordance with the annual percentage increase in the Consumer Price Index of the Bureau of Labor Statistics of the Department of Labor in increments of $500.” The new law results in a reduction of $1,256 in fees, but the overall fee remains too high according to many critics. Yet, some lenders do not charge the maximum fee, and the fees charged are often negotiable.

E. Using Proceeds to Fund Long-Term Care Insurance

Under the 2000 American Home Ownership and Economic Opportunity Act, if the reverse mortgage payments were used exclusively to fund a qualified long-term care insurance contract, the up-front insurance premium was waived. The waiver was an attempt by the government to address the problems of funding long-term care and to encourage the elderly to purchase their own long-term care insurance. This waiver has never been implemented by HUD; therefore, individuals taking out reverse mortgages solely to fund long-term care insurance did not receive the waiver for the initial insurance premium. Nonetheless, the waiver has been criticized because taking out a reverse mortgage to pay for long term care insurance can “double or triple the cost

93. Id.
94. Brandon, How the Housing Law Affects Reverse Mortgages, supra note 3 (explaining the high fees of originating the loan); see, e.g., Levenson, supra note 37 (explaining why reverse mortgages are still an expensive loan, even after the reduction of origination costs brought by the Act).
95. Brandon, How the Housing Law Affects Reverse Mortgages, supra note 3 (discussing the importance of comparing fees between lenders and negotiating for lower fees).
97. See DAVID T. RODDA, REFINANCING PREMIUM, supra note 74, at 76 (explaining that the government has been encouraging the purchase of long term care insurance in order to offset the cost of long term care charged to Medicare and Medicaid).
of the insurance over time." Long-term care insurance is a very expensive product and critics have pointed out that funding such a product with another expensive product, a reverse mortgage, may be an inappropriate use of resources.

Other issues with the "linkage" of the two products include the differences in target age groups and populations. The ideal time to purchase long term care insurance is when an individual is middle aged, as the premiums become very expensive once a person is in their seventies or eighties. In contrast, a borrower is not even eligible to take out a HECM until age sixty-two, and will be able to receive a higher loan amount the older they are when they take out the reverse mortgage. Additionally, most individuals who take out reverse mortgages have few assets other than their house, and have lower incomes. Yet, most holders of long-term care insurance are middle to upper class and one reason they take out long-term care insurance is to protect other assets.

Additionally, one requirement of a reverse mortgages is that the mortgagor must live in the home. If the mortgagor must go into long-term care outside the home for a year or more, the mortgagor may be forced to sell the home in order to repay the loan. Due to these problems, critics have urged the repeal of the waiver brought about by the 2000 Act.

99. See id. at 114–115.
100. See id. at 115 (explaining the dangers of using proceeds from an HECM to fund long term care insurance and recommending repeal of the waiver of initial mortgage insurance premiums).
103. AHLSTROM, supra note 101, at 12 (explaining the "mismatch" of ideal age for a reverse mortgage and long term care insurance).
104. Id. at 13 (describing the typical reverse mortgage borrower).
105. Id. at 11 (describing the typical purchaser of long term care insurance).
106. See 12 C.F.R. § 226.33(a)(2)(iii), supra note 29 (stating that the loan is due when the home is no longer the borrowers' "principal dwelling").
107. See AHLSTROM, supra note 101, at 12–13; Laise, supra note 26. In order to ensure that the home is the mortgagor's principal residence, the mortgagor "must make annual certification of his or her principal residence." Annual Determination of Principal Residence, 24 C.F.R. § 206.211 (2008).
HERA removed the long-term care insurance waiver. This waiver of initial mortgage insurance premiums was seen as a counterproductive incentive to take out a HECM to fund long-term care insurance. There is nothing in the old or amended law, however, that forbids borrowers from using part or all of the proceeds they receive to fund long term care insurance. Therefore, the appropriateness of using the proceeds from a reverse mortgage to fund the insurance should be addressed on a case-by-case basis during the required third party counseling session in order to educate borrowers about whether such an arrangement would be appropriate for them.

F. Sale of Annuities in Tandem with Reverse Mortgages

Probably the most frequent problem with reverse mortgages cited by the media was the use of the proceeds from a reverse mortgage to fund long-term annuities. This purchase defeats the purpose of a reverse mortgage by tying up the senior’s assets, oftentimes until after death. After making such a purchase, the senior may then be left with insufficient payments from the reverse mortgage to make ends meet. “Long-term annuities are almost always inappropriate for seniors, as they can tie up retirement savings far beyond one’s life expectancy.” According to the Association of American Retired Persons (AARP), “it is extremely unlikely that you can safely earn more from an investment than the loan would cost.” Additionally,

114. Watch out for Sneaky Sales Tactics, supra note 4.
115. See e.g., Charles Duhigg, Tapping into Homes Can be Pitfall for the Elderly, supra note 65.
116. Senator Herb Kohl Statement, supra note 50; see also Kaplan, supra note 112.
using the proceeds from a reverse mortgage to fund an annuity results in the payment of fees to fund the annuity and payment of fees for the reverse mortgage.\textsuperscript{118} Finally, for purposes of Social Security Insurance and Medicaid, payments from an annuity are counted as income, further negatively impacting the customer's finances.\textsuperscript{119}

Prior to the passage of HERA, there were no limitations on the sale of annuities with a reverse mortgage.\textsuperscript{120} HERA, however, adds several restrictions regarding the sale of reverse mortgages and annuities.\textsuperscript{121} First, the third-party counseling may not be performed by a party who also sells annuities.\textsuperscript{122} Second, no party “that participates in the origination” of a reverse mortgage insured by the FHA can be involved in any way with “any other financial or insurance activity” or “require the purchase of any other financial or insurance product.”\textsuperscript{123} Lastly, the Act explicitly provides that the mortgagor or any other party involved may not require the mortgagor to purchase an annuity or other insurance or “similar product” in order to also purchase the reverse mortgage.\textsuperscript{124}

The banking industry objected to these provisions.\textsuperscript{125} The lender receives high fees for both reverse mortgages and annuities, therefore making the combination sale an attractive source of income.\textsuperscript{126} HERA, however, clearly forbids such “cross-selling” of reverse mortgages and annuities.\textsuperscript{127} Elimination of this practice should soften the concerns of reverse mortgage critics.

\textsuperscript{119} See AARP, \textit{Spending your Equity}, supra note 117.
\textsuperscript{122} Id. § 2122(a)(3)(B) (to be codified at 12 U.S.C. § 1715z-20(d)(2)(B)).
\textsuperscript{123} Id. § 2122(a)(9) (to be codified at 12 U.S.C. § 1715z-20(m)).
\textsuperscript{124} Id.
\textsuperscript{125} Legislative Update, supra note 53.
\textsuperscript{126} See Duhigg, \textit{Tapping into Homes Can be Pitfall for the Elderly}, supra note 65.
\textsuperscript{127} See LISSA L. BROOME & JERRY W. MARKHAM, REGULATION OF BANK FINANCIAL SERVICE ACTIVITIES: CASES AND MATERIALS 251-253 (3d ed. 2007) (explaining the prohibition of “tying” arrangements which are defined as requiring the purchase of one financial product in order to purchase a second financial
G. Cooperative Units Not Eligible

Prior to HERA, seniors who owned a cooperative unit as their principal residence were not eligible to use the unit as security for HECMs. Some private lenders, including Financial Freedom, did offer non-HECM reverse mortgages on cooperatives. Yet, many cooperative boards were hesitant to approve these reverse mortgages. In HERA, the definition of "mortgage" and "first mortgage" has been adjusted by the insertion of additional language to allow owners of cooperatives to obtain HECMs. Perhaps the boards of cooperative apartments will be more willing to approve a HECM than other reverse mortgages due to the FHA insurance.

Most cooperative apartments are located in cities and many have risen in value over their purchase price. The new inclusion of cooperatives under HERA allows these urban seniors a way to tap into this equity without selling their residence. This is especially beneficial as many of the owners of these cooperative apartments are seniors on fixed budgets. These reverse mortgage borrowers will now have an additional option available to them and be able to take advantage of the unique protections offered by HECMs.

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128. Bob Tedeschi, Reverse Mortgages Retooled, N.Y. TIMES, Oct. 26, 2008, at RE11 (stating that one of the changes HERA brings is the opportunity to apply for HECMs to owners of cooperative apartments).
129. See Jay Romano, Reverse Mortgages: A Windfall for Co-ops, N.Y. TIMES, Mar. 5, 2006, available at http://www.nytimes.com/2006/03/05/realestate/mortgages/05 home.html (stating that reverse mortgages have been available to cooperative apartment owners for "several years" from lenders such as Financial Freedom).
130. See id.
132. See Romano, supra note 129.
134. See id. (stating that under the new law, owners of co-ops will be able to apply for a reverse mortgage).
135. Id. (stating that many owners of co-ops are widows who "barely make it on fixed incomes").
136. See HUD, A Turning Point, supra note 1, at 7 (describing the counseling product); H.J. Cummins, Cashing out the Nest Egg, STAR TRIBUNE (Minneapolis - St. Paul), Sept. 7, 2008, at 1D. Such regulation is a natural extension of other "anti-tying" prohibitions.
IV. PROBLEMS REMAINING AFTER PASSAGE OF THE HOUSING AND ECONOMIC RECOVERY ACT

HERA addressed many of the criticisms of HECMs, however, there are still problems with the Program, and potential dangers for both borrowers and lenders. This section discusses each of these issues separately. The remaining problems include: (1) educating seniors; (2) the high cost of HECMs; (3) the remaining volume cap on the Program; (4) the potential loss of the home to foreclosure; (5) difficulties of servicing the loans; and (6) risks for abusing the product.

A. Educating Seniors

According to a 2007 Harris poll, only sixty-four percent of consumers had heard of reverse mortgages.137 Of those sixty-four percent, thirty-four percent reported that they were “somewhat knowledgeable” about reverse mortgages and only fifteen percent stated they were “very knowledgeable.”138 In terms of their impression of reverse mortgages, only twenty percent had a “somewhat favorable” impression of the product.139 The AARP Public Policy Institute attributes some of this negativity to “sensational news coverage” of some of the higher cost loans that were made in the mid-1980s to late 1990s and have since become due.140

Additionally, some individuals believe that they could end up owing more than their home is worth, if their loan amount exceeds the value of their home.141 None of these views are an accurate description of the product, however, which, “when used properly . . . can be an effective way for seniors to tap into the equity of their house as a means to bolster their retirement requirement required for HECM borrowers and the guaranteed loan payment by HUD).

137. AARP Report, supra note 30, at 72.
138. Id.
139. Id.
140. Id. at 73.
security."¹⁴² When the loan becomes due, the amount owed to the lender cannot be greater than the home’s value at the time of sale.¹⁴³

Although HERA requires “adequate” funding for counseling sessions provided by an independent third party for people already interested in taking out an HECM,¹⁴⁴ there is nothing in HERA that addresses educating the public generally.¹⁴⁵ Many seniors are either afraid of the loans, believe there is a “stigma” attached to getting one, or do not know much about them in general.¹⁴⁶ If the public were better educated about reverse mortgages, the demand for the loans could increase which would make the loans more profitable for lenders and encourage more lenders to enter the market.¹⁴⁷ More lenders in the marketplace would encourage competition, thereby potentially decreasing the costs of reverse mortgages.¹⁴⁸ If the public were better educated about reverse mortgages, more seniors could benefit from them at lower costs and others who either do not need them or have other options would know to avoid these products.¹⁴⁹

B. High Cost

While the new Act reduced the origination fees for reverse mortgages, they are still expensive loans.¹⁵⁰ For example, a loan of $90,000 at an interest rate of six percent would result in a $238,000 balance in twelve years.¹⁵¹ A 2003 actuarial analysis “found that

¹⁴² Senator Herb Kohl Statement, supra note 50.
¹⁴³ Madonna & Archambault, supra note 141; see also Reilly, supra note 48, at 19.
¹⁴⁴ See supra Part II.B. (discussing HERA’s counseling requirements).
¹⁴⁶ See DAVID T. RODDA, ET AL., U.S. DEP’T OF HOUSING AND URBAN DEV., NO PLACE LIKE HOME: A REPORT TO CONGRESS, 43 - 44 (2000) [hereinafter RODDA, NO PLACE LIKE HOME]; see also Meg Burns Statement, supra note 50.
¹⁴⁷ See id.
¹⁴⁸ AARP Report, supra note 30, at ix – x; RODDA, EVALUATION REPORT, supra note 79, at v (explaining need for increased “consumer outreach and education” in order to increase the volume of loans and to attract more lenders to the market).
¹⁴⁹ See RODDA, NO PLACE LIKE HOME, supra note 146, at 43 - 44.
¹⁵⁰ Reverse Mortgages can be a Costly way to Tap Home Equity, supra note 43.
¹⁵¹ Id.
the mortgage insurance charged was about $1,000 per loan more than was needed to cover the program's anticipated liabilities.\textsuperscript{152} HERA does not call for a reduction in the insurance amount but does order a study of the costs of the program and includes an analysis of the mortgage insurance premiums as part of that study.\textsuperscript{153} If the amount of insurance were decreased by $1,000 this would reduce the closing costs to $5,000, making the loan somewhat more attractive to potential borrowers.\textsuperscript{154}

AARP has recommended, but HERA has not provided, a "lite" reverse mortgage with lower closing costs for individuals who only need to borrow small amounts that would also permit these borrowers to subsequently increase the amount borrowed without a formal refinancing of the loan.\textsuperscript{155} HERA does not take into account seniors who need to borrow smaller amounts of money.\textsuperscript{156} The upfront closing costs are calculated based on the value of the home, not on the amount of the loan.\textsuperscript{157} Therefore borrowing only a small amount is particularly expensive.\textsuperscript{158}

Moreover, HERA did not address the reduction of costs to refinance a reverse mortgage.\textsuperscript{159} Currently, no low-cost refinancing option exists, making a refinance to access increased equity or a lower interest rate costly.\textsuperscript{160} The cost discourages seniors from taking out a smaller initial loan and then refinancing later if more money is needed, thus losing the portion of the market that would find such an arrangement attractive.\textsuperscript{161}

\textsuperscript{152}. AARP Report, supra note 30, at 110.
\textsuperscript{154}. See id. at § 2122(c), (to be codified at 12 U.S.C. 1715z-20(r)).
\textsuperscript{155}. See AARP Report, supra note 30, at 112.
\textsuperscript{157}. See AARP Report, supra note 30, at 112.
\textsuperscript{158}. See id.
\textsuperscript{159}. See Housing and Economic Recovery Act of 2008, § 2122(c) (to be codified at 12 U.S.C. § 1715z-20(r)).
\textsuperscript{160}. See AARP Report, supra note 30, at 112 (recommending the development of a "lite" reverse mortgage product).
\textsuperscript{161}. See id. (supporting a reduced cost refinance).
C. Volume Cap on HECMs

Prior to the passage of HERA, the number of FHA-insured HECMs was limited to 275,000 by statute. The increasing popularity of HECMs meant that there was a risk of reaching that limit and being unable to grant additional loans to qualified seniors. Senator Gordon Smith supported removing the volume cap in order to assist more seniors. Meg Burns of HUD testified that “such a cap is no longer appropriate or necessary, now that the program has been tested for eighteen years and has proven to be a real success story – a model for the entire industry.” These recommendations are in line with the AARP’s suggestion that greater numbers of HECMs would lead to more competition and lower prices for consumers.

While many called for the elimination of the volume cap, HERA maintains the aggregate number of reverse mortgages that can be insured by the FHA at 275,000. This cap will not allow lenders the opportunity to increase the volume of the loans they close that are FHA-insured, or encourage lenders not already providing the loans to enter the market. Additionally, with the higher loan limits after HERA, individuals who would have sought jumbo non-HECM reverse mortgages will be more likely to look to HECMs which may increase demand, but the volume cap remains the same as when the loan amount was more limited.

163. See Bob Tedeschi, Many Choose to go in Reverse, N. Y. TIMES, Feb. 11, 2007, http://www.nytimes.com/2007/02/11/realestate/11mort.html?_r=1&scp=1&sq=bob%20tedeschi%20many%20choose%20to%20go%20in%20reverse&st=cse# (stating that officials in the mortgage industry were worried they would have to stop offering reverse mortgages because they were quickly reaching the statutory limit).
165. Meg Burns Statement, supra note 50.
166. AARP Report, supra note 30, at 109.
169. See HULIQ, supra note 82; AARP Report, supra note 30, at 109-110.
D. Loss of Home to Foreclosure

Mortgagors are required to maintain mortgage insurance on the property and pay all taxes and other assessments on the property, or risk losing their home to foreclosure. Low income seniors are at a greater risk than working borrowers of regular mortgages of running out of funds and being unable to make these monthly payments. Lenders are not required to foreclose on borrowers who do not keep up their payments, but “no clear policy guidelines have been developed for dealing with foreclosures.” Lenders who wish to sell their loans for securitization will require that all payments by the mortgagor be current.

After the passage of HECM, seniors taking out reverse mortgages still face the risk of foreclosure, if they are unable to pay the property taxes on their home or do not keep the house in repair. This becomes a problem when the amount of the loan is less than those expenses, especially considering that the senior no longer has any equity in their home to secure a loan.

The issue of foreclosure is difficult to address as the home must be kept up and used as a principal residence in order to protect the lenders’ security interest in the home. There are however, some possible solutions to this problem. Insurance payments could be rolled into the loan and paid by the lender, but property taxes vary by year and would not be amenable to such an arrangement. Additionally, seniors who leave their home because they must go into long-term care could be exempted from the requirement of living in the home if they meet certain conditions,

171. See AARP Report, supra note 30, at 111.
172. See id.
175. See Reverse Mortgages can be a Costly way to Tap Home Equity, supra note 43.
such as having an adult child or other responsible agent looking after the home.

E. Loans Difficult to Service

Originators of reverse mortgages will need to meet certain requirements in order to be licensed to provide HECMs, which is a “challenge.” Reverse mortgage lenders must be able to understand a loan that is “more complex,” than a regular mortgage loan and become familiar with different application documents.

Additionally, the loan process for HECMs involves more time and effort on the part of the lender. These loans frequently involve multiple meetings with the potential borrowers and quite a bit of “handholding.” Furthermore, the lender receives no payments until the loan becomes due. The development of a robust secondary market would provide liquidity to lenders issuing reverse mortgages. If more lenders begin offering reverse mortgages this will “help make the business more profitable by spreading marketing costs,” thereby making reverse mortgages more attractive to lenders.

F. Risks for Abuse

Some lenders view reverse mortgages as a replacement for subprime lending as a new way to generate revenue. Currently, the “penetration of the product is only one percent of its potential market,” and lenders forecast tremendous growth due to the

177. Moed, supra note 9.
178. RODDA, NO PLACE LIKE HOME, supra note 146, at 41.
179. Id.
180. See Emily Brandon, This Mortgage Works in Reverse, U.S. NEWS & WORLD REPORT, Sept. 15, 2008, at 84.
183. Dymi, supra note 176.
184. Finkelstein, supra note 83.
10,000 baby-boomers turning sixty-two years old every day.\textsuperscript{185} There has been broad interest in purchasing Financial Freedom, a subsidiary of the failed Indy Mac that specialized in reverse mortgages.\textsuperscript{186} "Reverse mortgages is the asset you want to own,' [David Peskin, CEO of Lender Lead Solutions] said. 'I don't see anybody writing down reverse mortgages.'\textsuperscript{187}

With the increased interest in providing reverse mortgages there has also been an increase in advertising, some including celebrities such as Robert Wagner.\textsuperscript{188} These commercials add to the misunderstanding of the product.\textsuperscript{189} With the government's money at stake insuring these products that are secured by homes that may be declining in value along with the general decline in the real estate market, lenders should be careful that the reverse mortgage market does not fall prey to the same fate as the subprime market.\textsuperscript{190}

V. CONCLUSION

HERA addressed many concerns related to reverse mortgages, but lenders should still be cautious in promoting these products to the elderly. Reverse mortgages are a useful tool in the right situation, but can be a costly loan that risks depleting home equity for those who have other options.\textsuperscript{191} For low-income senior homeowners who are having trouble making ends meet during tough economic times, a HECM may be appropriate.\textsuperscript{192} A HECM would provide cash to them without the obligation of monthly

\textsuperscript{185} Dymi, supra note 176.
\textsuperscript{186} Kate Berry, With Indy Mac on Block, Many See 'Reverse' Opportunity, AM. BANKER, Aug 1, 2008, at 1.
\textsuperscript{187} Id.
\textsuperscript{188} See Reverse Mortgages can be a Costly Way to Tap Home Equity, supra note 43.
\textsuperscript{189} See id.
\textsuperscript{190} See Cummins, supra note 127.
\textsuperscript{192} See id.
The HECM would also allow them to stay in a home that they may not be able to sell in the current housing market. This type of rising debt loan may not, however, be appropriate for seniors who are looking for extra money to finance a more extravagant lifestyle, or who could afford to make monthly payments on a traditional loan. HECMs also remain a poor choice for seniors needing to borrow only a small amount of money for a onetime expense due to the high upfront costs of the loan. The independent third party counseling required by HERA and the increased funding provisions should reduce the number of unnecessary HECMs taken out by borrowers.

In our current economy lenders are looking for an alternative product to subprime mortgages to hopefully generate profits but this product may not be the answer. Reverse mortgages are more complicated than forward mortgages and require a larger investment of time on the part of the lender. Additionally, the borrower does not make any payments on the loan until it becomes due, meaning that the lender may have to wait several years or more for payment, a problem that could be somewhat alleviated by growth in a secondary market. In a time of declining home prices, there is also a risk that the amount of the reverse mortgage loan will be greater than the value of the home when it is sold, requiring the FHA to pay the remainder of the

193. Brandon, This Mortgage Works in Reverse, supra note 180.
195. See Brandon, How the Housing Law Affects Reverse Mortgages, supra note 3; Charles Duhigg, Questions to Ask Before Taking a Reverse Mortgage, supra note 113.
196. See AARP Report, supra note 30, at 112.
198. See Cummins, supra note 127 (comparing the reverse mortgage industry and its sales tactics to the adjustable rate mortgage market).
199. See Finkelstein, supra note 83 (explaining the lengthy process of selling the reverse mortgage product); see also Moed, supra note 9 (explaining the costs, training and research involved in offering reverse mortgages).
200. See Levenson, supra note 37 (explaining that no payments are made until the home is no longer the primary residence); see also Cowden, supra note 24 (explaining that the development of a secondary market for reverse mortgages will increase liquidity).
loan to the lender. The federal government may be weary of making such payments after already spending billions of dollars investing in the banking industry following the subprime mortgage debacle and subsequent financial crisis.

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201. See Moed, supra note 9 (explaining the risk of declining home values to the reverse mortgage lender).