

# FTC FACTS for Consumers

## Reverse Mortgages: Proceed with Care



Whether seeking money to pay for medical treatment, finance a home improvement, buy long-term care insurance, or supplement their income, many older Americans are turning to “reverse mortgages.” They allow older consumers to convert the equity in their homes to cash while retaining home ownership.

With a “regular” mortgage, you make monthly payments to the lender. But with a reverse mortgage, you receive money from the lender and generally do not have to repay it for as long as you live in your home. In return, the lender holds some — if not most or all — of your home’s equity.

Introduced in the late 1980s, reverse mortgages can help homeowners who are “house-rich-but-cash-poor” remain in their homes and still meet their financial obligations. The proceeds of the loan are tax-free, there are no minimum income requirements, and for most reverse mortgages, the money can be used for any purpose.

# Facts for Consumers

But, reverse mortgages also tend to be more costly than other loans, and there have been cases of abuse by unscrupulous lenders.

If you're considering a reverse mortgage, it's important to understand how the loans work and what your rights and responsibilities are.

## THE BASICS

There are several types of reverse mortgages:

- the federally insured Home Equity Conversion Mortgage (HECM), administered by the Department of Housing and Urban Development (HUD)
- single-purpose reverse mortgages, usually offered by state or local government agencies for a specific reason
- proprietary reverse mortgages, offered by banks, mortgage companies, and other private lenders and backed by the companies that develop them.

To qualify for a reverse mortgage, you must be at least 62 and have paid off all or most of your home mortgage. Income is generally not a factor, and no medical tests or medical histories are required. If you seek an HECM, you also must undergo free mortgage counseling from an independent government-approved "housing agency." Financial institutions offering proprietary reverse mortgages may require similar counseling or homeowner education.

The amount you can borrow depends on your age, the equity in your home, the value of your home, and the interest rate. If it's an HECM, federal law limits the maximum amount that can be paid out.

You can be paid in a lump sum, in monthly advances, through a line of credit, or a combination of all three.

## COMMON FEATURES

Reverse mortgages offer special appeal to older adults because the loan advances, which are not taxable, generally do not affect Social Security or Medicare benefits. Depending on the plan, reverse mortgages generally allow homeowners to retain title to their homes until they permanently move, sell their home, die, or reach the end of a pre-selected loan term. Generally, a move is considered permanent when the homeowner has not lived in the home for 12 *consecutive* months. So, for example, a person could live in a nursing home or other medical facility for up to 12 months before the reverse mortgage would be due.

However, be aware that:

- Reverse mortgages tend to be more costly than traditional loans because they are rising-debt loans. The interest is added to the principal loan balance each month. So, the total amount of interest owed increases significantly with time as the interest compounds.
- Reverse mortgages use up all or some of the equity in a home. That leaves fewer assets for the homeowner and his or her heirs.
- Lenders generally charge origination fees and closing costs; some charge servicing fees. How much is up to the lender.
- Interest on reverse mortgages is not deductible on income tax returns until the loan is paid off in part or whole.
- Because homeowners retain title to their home, they remain responsible for taxes, insurance, fuel, maintenance, and other housing expenses.

## GETTING A GOOD DEAL

If you decide to consider a reverse mortgage, shop around and compare terms. Look at the:

- annual percentage rate (APR), which is the yearly cost of credit.

- type of interest rate. Some plans provide for fixed rate interest; others involve adjustable rates that change over the loan term based on market conditions.
- number of points (fees paid to the lender for the loan) and other closing costs. Some lenders may charge steep costs, which your lender may offer to finance. However, if you agree to this, you'll take out fewer proceeds from the loan or you'll borrow an extra amount, which will be added to your loan balance and you'll owe more interest at the end of the loan.
- total amount loan cost (TALC) rates. The TALC rate is the projected annual average cost of a reverse mortgage, including all itemized costs. It shows what the single all-inclusive interest rate would be if the lender could charge only interest and no fees or other costs.
- payment terms, including acceleration clauses. They state when the lender can declare the entire loan due immediately.

Under the federal Truth in Lending Act, lenders must disclose these terms and other information before you sign the loan. On plans with adjustable rates, they must provide specific information about the variable rate feature. On plans with credit lines, they must inform the applicant about appraisal or credit report charges, attorney's fees, or other costs associated with opening and using the account. Be sure you understand these terms and costs.

Reverse mortgages come with different provisions. For example, with some reverse mortgages, the lender may take a share of equity appreciation. This could create issues for the homeowner or heirs, particularly if the value of the home rises unexpectedly during the loan. Carefully read any provision of the contract about shared appreciation.

Also, be cautious about reverse mortgages offered by door-to-door and other home solicitation lenders. There have been various problems with these types of lenders. Some of the problems have involved steep points and loans that primarily seek to take the owner's equity.

You generally have at least three business days after signing a reverse mortgage contract to cancel it. The cancellation must be in writing.

## REPORTING POSSIBLE FRAUD

If you suspect that a lender is violating the law, register your concerns with the lender or loan servicer. You also may wish to file a complaint with:

- your state Attorney General's office or state banking regulatory agency
- the Federal Trade Commission (FTC). File a complaint online at [www.ftc.gov](http://www.ftc.gov) or call toll-free 1-877-FTC-HELP (1-877-382-4357).

## CONSUMER ADVICE

Is a reverse mortgage right for you? Before you decide, consider all your options; you may qualify for other less costly credit plans. Information to help you decide is available from:

### AARP

601 E Street, NW  
Washington, DC 20049  
1-800-424-3410  
[www.aarp.org/revmort](http://www.aarp.org/revmort)

### The National Center for Home Equity Conversion

360 N. Robert Street, #403  
St. Paul, MN 55101  
1-651-222-6775  
[www.reverse.org](http://www.reverse.org)

# Facts for Consumers

## **U.S. Department of Housing and Urban Development (HUD)**

451 7<sup>th</sup> Street, SW  
Washington, DC 20410  
1-888-466-3487  
[www.hud.gov/offices/hsg/sfh/hecm/rmtopten.cfm](http://www.hud.gov/offices/hsg/sfh/hecm/rmtopten.cfm)

HUD also can refer you to a HUD-approved reverse mortgage counselor. Call HUD toll-free at 1-888-466-3487 or 1-800-569-4287.

## **Federal Trade Commission**

Consumer Response Center  
600 Pennsylvania Avenue, NW  
Washington, DC 20580  
[www.ftc.gov](http://www.ftc.gov)  
1-877-FTC-HELP (1-877-382-4357)

The FTC works for the consumer to prevent fraudulent, deceptive, and unfair business practices in the marketplace and to provide information to help consumers spot, stop, and avoid them. To file a complaint or to get free information on consumer issues, visit [www.ftc.gov](http://www.ftc.gov) or call toll-free, 1-877-FTC-HELP (1-877-382-4357); TTY: 1-866-653-4261. The FTC enters Internet, telemarketing, identity theft, and other fraud-related complaints into Consumer Sentinel, a secure online database available to hundreds of civil and criminal law enforcement agencies in the U.S. and abroad.



Federal Trade Commission  
Bureau of Consumer Protection  
Office of Consumer and Business Education

*November 2003*