Course Objective

This course was created to teach and educate CPAs, accountants, EAs, attorneys, financial planners and insurance advisors about an exciting "new" financial program that is so powerful, it is changing the lives of our senior citizens.

Each year the number of seniors that are using this program is doubling. In the not too distant future, more of the major financial institutions will be offering this program. A purpose of this course is to provide advisors with another solution to help them differentiate themselves in the marketplace as well be positioned to provide the best advice possible to client.

This general overview will help readers understand this country's shifting senior demographics. It will also permit advisors to show senior clients how they can unlock tremendous home wealth while still living in their homes for life. This course will enable advisors to be among the first in their community to talk to clients about a program many advisors heretofore have ignored. Should advisors continue to ignore it, they will do so at their own financial detriment and potentially leave themselves open to E&O or malpractice suits. Today, seniors want to know about **all** their financial options.

Reverse Mortgages

Introduction

This course will focus upon what a reverse mortgage is, how it works, why it works and why it should be considered for many clients over the age of 62. This material will compare the various reverse mortgage programs to each other and the course will also dissect some case studies that highlight the salient aspects of each program.

The reverse mortgage industry is undergoing a cataclysmic change. Investors and lenders now understand that this market has tremendous upside potential. While the amount of closed loans has increased over 500% since 2001, market penetration is a fraction of one percent. In years to come the reverse mortgage landscape will not be recognizable.

In the past, the industry had few programs, and a one size fits all mentality. The programs of the future will take into account the varying needs of our elders. There will be new programs, with different types of interest rate structures and with different cost variations. These changes will put more money into the pockets of our elders.

Wall Street sees the potential in the reverse mortgage industry, especially as the baby boomers become of age. The first new permutation has occurred. Already we have seen the introduction of an FHA reverse mortgage with a lower margin. The standard FHA program contained a margin of 1.50 over the CMT and the 10 year bond yield. That was the standard from the type the model FHA program was introduced in 1989. Now, experts agree that a new standard has been created. It is commonly referred to as the HECM 100. The margin is reduced to 1 point of the above noted indices. AT this point in time no one can predict how long this standard will last. As more secondary market investors discover this burgeoning market, it is fair to say, it probably will not remain the standard for a significant period of time.

In addition to this we have seen a change in the proprietary reverse mortgage as well. Here too, margins have been lowered. This will also result in putting more money into the pockets of our elders. It is also important to note that since this course was created, more lenders have added their own proprietary programs. The proprietary program, noted below is the model upon which the others have been based upon.

The examples and case studies contained in this course are for didactic purposes only. As the reverse mortgage industry updates interest rates on a weekly basis, it is impossible to track these changes in the course material. More importantly these materials will provide you with the key concepts that the industry uses to arrive at a given result.

Proceeds from reverse mortgages can act as an emergency investment vehicle, an estate planning device or a retirement facilitator. In order to begin a discussion on this topic it will help to have a good definition of just what it is.

What is a reverse mortgage?

A reverse mortgage is a special and different kind of loan that is easy to obtain if you are at least 62 years of age and own your own home, condo (PUD) or co-op (only in New York). A reverse mortgage converts a portion of the value (equity) of a home into instant cash. The pool of money that is created by a reverse mortgage can be received by a senior homeowner(s) in a variety of ways.

One of the key aspects to a reverse mortgage is that the client is NOT required to pay monthly mortgage payments. Additionally, there is NO personal liability attached to the loan. A reverse mortgage loan is non-recourse, except that the client's home does serve as collateral.

One other key feature to a reverse mortgage is that there are **no income, asset or credit requirements** to obtain the loan**.** That means you could have a client who has poor credit, no income and no other assets besides a home with equity and the client could obtain a reverse mortgage to raise money for a variety of needs.

The concept of reverse mortgages is easy to understand and clients, once they learn about how they work, gravitate to them because of the tremendous and immediate benefit with lack of putting up significant assets when implementing a reverse mortgage.

Who can use reverse mortgage?

Age 62 is one of a few "magic numbers" you will see in this material. Each homeowner must be at least 62. If one spouse is 62 and one is not, then the "couple" cannot obtain such a loan.

On the other hand, should the younger spouse be removed from the title, the older spouse can obtain the reverse mortgage. Should you be faced with such a situation with one of your clients, you should pay close attention to the following example.

Let's take an example: A husband and wife are 68 and 60 respectively. If the wrong person dies first – (in this case the husband), the reverse mortgage loan must be paid back. (Remember, in order to get a reverse mortgage for this couple, the clients had to take the 60 year old spouse off the title and the mortgage. Therefore, when the older spouse dies, the mortgage, which is tied to husband's death, must be repaid via the terms of the reverse mortgage).

Usually to pay back the loan, the surviving spouse who inherited the entire home is forced to sell the home. However, that is not always the preference for paying back a reverse mortgage. Nearly every reverse mortgage is sold with the incorporation of life insurance which is used to pay off the mortgage after one or both spouses die. The life insurance if used in the above example would be used to pay off the mortgage. This would be an ideal situation since the 60 year old spouse would have the money (liquid and tax free) to pay off the mortgage and then would not have to move out of her residence. This is explained in more detail later.

Home ownership can be accomplished in a variety of ways. A home that is a primary residence can be owned in severalty (individually), jointly, in trust or with a life estate. If one sets up a revocable trust, a reverse mortgage can still be an option provided the beneficiaries are the seniors. The children can be beneficiaries upon the death of the surviving parent. Title to the property must be in the trustees and the trustees do not have to be the borrowers (seniors). The trust will be amended at closing to permit a reverse mortgage.

An irrevocable trust on the other hand is more troublesome. Typically, such a trust is created as an asset protection device or estate transfer tool.

Whenever such a trust is used it generally precludes the senior from accessing the corpus (assets) of the trust. Accordingly, drawing down the proceeds from the reverse mortgage would be a prohibited activity.

The amount of money that can be created or manufactured (as a salesman would say) from a reverse mortgage is dependent upon the program used. Generally speaking, it can be said that three things will determine how much a client can receive from a reverse mortgage:

1. The age of the youngest borrower.

2. The value of the home (up to a certain limit for some programs).

3. The interest rate (for some programs). We will get into the specifics for each program when we look at the case studies.

The pool of money that is created from a reverse mortgage can be received in a variety of ways. Again, the ways will vary under the differing programs. The options that may be available are lump sum, partial lump sum, monthly payment, line of credit or any combination. The differences will become clearer as we peruse the case studies and look at some of the aforementioned pictures.

One of the key things that sets a reverse mortgage apart from any other kind of loan is that its is a **non recourse loan**. There is no personal liability to the borrower, their estate or to their heirs.

Let's look at a worst case scenario.

> Assume for a moment that the amount that ultimately becomes due on the reverse mortgage is greater than the value of the home. (This could happen due to out of the normal interest rate increases, if property significantly decreased in value or if the client just happened to live much longer than anticipated) When the house is sold by the estate, it nets, let's say, $300,000. Let us also assume that the amount due on the loan is $400,000. The difference of $100,000 does not become a liability of the estate.

Enter into a partnership with your home

Another key thing that makes a reverse mortgage loan special and different is that **monthly mortgage payments are not required**. Interest and servicing fees accrue over time. This means as with any negative amortization loan, that the amount that becomes due will be always increasing because mortgage payments are not required.

Harnessing the power of reverse mortgages

A reverse mortgage is nothing short of a life changing event for many clients. The look on the face of our clients tells the whole story. For some, the weight of the world has been lifted from their backs. They are ready to take on the world again. Many of our seniors did not make the best investing or financial decisions throughout their earning years. Their need for immediate money has been satisfied with this program. They get the best of both worlds: their equity is transformed into cash AND they can **still stay in their home.**

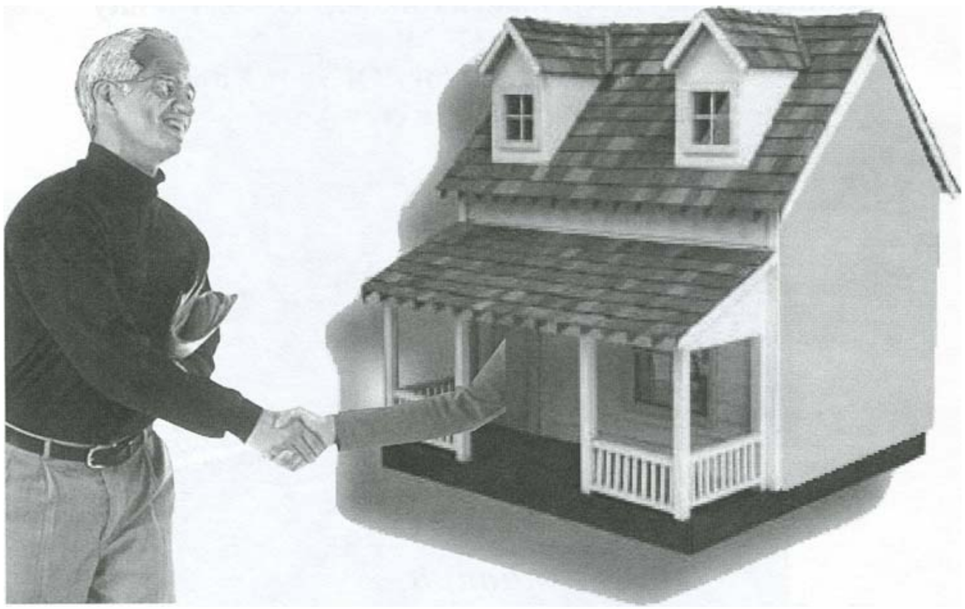
Preliminary observations

Many of our clients have told us straight out that they never expected to live as long as they have. As a population, we are living longer. The birth rate as a percentage of the population has been down for many years. It is estimated that over the next 16 years the over age 50 population will grow by 74%, while the under age 50 population will grow by a small fraction of that amount. No state currently has a senior population greater than 17%. In the next 20 years, 30 states will have a senior population that exceeds 20%.

Social Security is not getting our seniors where they need to be. Ida Mae Fuller was the first recipient of Social Security. Over a few years she paid in about $30. She received back over $23,000. Sara Knauss lived to be over 115. Between her, a daughter and a grandson they collectively received Social Security for over 100 years. Imagine what will happen when we have tens of millions of Saras and Ida Maes receiving these benefits. Many of our clients wish they had done things differently, but each one thanks God that they have a home they can depend upon.

The following picture tells it all when it comes to understanding the essence of what a reverse mortgage is.

"I've Taken Care of **"It's now my turn**



you all these years."' **To take care of you."**

Condo's and Co-Ops too

Medicare has done wonderful things. It has kept a substantial number of people out of poverty. Its goal of protecting our older citizens from facing catastrophic medical bills has not been fully realized. Medicare is the government's answer to health care insurance. Because it is insurance, the government pays only a portion of a claimant's bill. Each insured is responsible for the yearly deductible and daily co insurance under Part A and the remaining 20 percent of the doctor bills under Part B.

It is important for individuals to purchase private health coverage for the part that the government does not pick up. Medicare's payment to the hospitals is diagnosis based. This means that the hospital gets paid the same if the patient is in the hospital two or seven days. There is a great incentive for hospitals to discharge patients as quickly as possible. The need for long term care becomes critical.

Question: How does this become affordable for clients who live only on their social security and or a modest pension benefit?

Many seniors believed that the stock market was infallible. They were wrong. Many of our clients have lost a significant amount of their portfolio. They do not like the insecure feeling that comes along with their error in judgment, but are now forced to deal with the reality that their "nest egg" is not big enough to live in a manner that is acceptable to them and their children.

We see many client who have never considered financial and/or estate planning. Tremendous opportunities abound for those who see that there is a way to help these seniors. In order to do that, you must understand the market. Understanding reverse mortgages and how they can help your older clients meet their "living" needs becomes very important.

Brutal facts of reality

We have many seniors who live in big homes but have little savings. Typically, the older clients, even they do not have a sizeable liquid estate, have figured out a way to pay down the debt on their personal residence, many times to zero. While the client has no or little debt on their house, many still have trouble paying their monthly bills. They are unable to realize their life's hopes and dreams due to a lack of money. So whether we are talking about a client living in a $200,000 home or a client living in a home valued at greater than a million dollars, a reverse mortgage can satisfy diverse needs. There is a special proprietary program specifically created for those who live in high value homes and a great deal of money can be extracted from the value of these homes.

Question: What financial program can ameliorate years of wrong financial decision making?

Reverse mortgage advantages

In just a few pages we covered a wide area. Let us take a moment to recap the huge advantages of this unique program.

A senior will never make a monthly mortgage payment to a lender. In fact the opposite is true. The senior will have a choice (these options vary from program to program) of how they will RECEIVE their funds when they convert a portion of their home value into a pool of cash. The senior will always remain the owner of the home. The senior borrower can use the money just about any way they like. The use of funds is limited by the creativity of the borrower. This important economic weapon will allow seniors all over the country to realize their hopes and dreams.

The three reverse mortgage plans

As of this writing there are three national reverse mortgage programs. The model program upon which the others are based was created and authorized by Congress in 1989. This is the FHA or HECM (Home Equity Conversion Mortgage) or HUD Reverse Mortgage. All three designations refer to the same government (federal) insured loan program. This program comprises over 90% of the reverse mortgage market.

In 1996 Fannie Mae came out with their HomeKeeper reverse mortgage program. The unique feature it has is that it is the only program that one can use to purchase a home. (It is rumored that FHA will be coming out with a similar program). For the time being, the FHA requires the client to buy the home for all cash before it will do the reverse mortgage. With Fannie Mae, they will allow a client buy a new home with some debt and then use the Homekeeper program to get the equity out via a reverse mortgage. (Depends on how old someone one is). The purpose of these programs is to get into a home with no home mortgage payment.

Finally in 2001, Lehman Bros. developed a proprietary reverse mortgage program. Many advisors call it the “Jumbo” reverse mortgage program. This program was updated and revised in 2006 and is now called the Cash Advantage. The name change reflects a change in the margin, which was lowered to 3.5 per cent from 5 per cent. This change provides additional source of funds to the senior borrower. It also contains some unique features that we will discuss when we review the case studies.

Reverse mortgages are here to stay

Reverse mortgages are here to stay because they fulfill a pressing need. Because expenses are increasing (especially health care and long term care) at a rather alarming pace and because most seniors did not expect the longevity train to take them for a ride. Additionally, because most basic financial and estate planning has been ignored by out clients, there must continue to be a way to trade a portion of the value of the home for cash for a client’s living needs.

The numbers tell a rather compelling story. The last census (2000) indicated that there were 35 million people age 65 and over in this country. That number is expected to double in the next 25 years. At that time there will be 70 million people who have reached their 65th birthday. The most explosive growth in the senior market place, however, is occurring in the 85 and over age bracket. The 2000 census told us that there were 4 million seniors age 85 and over. It is estimated by 2050 that the number will increase to 20,000,000. That is an astounding projection.

Let’s take a quick look at the effect that an aging population can have on a family. Consider this: eighty five percent of seniors who are age 65 and over have one chronic illness. Thirty percent over age 85 will have 3 chronic illnesses. Ten percent of those who reach age 65 will suffer from Alzheimer’s or some form of dementia. This number will increase to almost 50% when one reaches age 85. Take into account that Medicare **will not** pay for custodial care and will only pay for 100 days of skilled nursing care per benefit period only if the person is improving in health. It will cover 100% for the first twenty days. From day 21-100 it will not cover the daily co-insurance amount. This amount alone could grow to over $8,000. Seniors are wrong to believe that their government will pick up the total cost for their skilled nursing care.

The financial and emotional toll of aging can cause havoc within the family. Children who have children of their own have the added financial and sometimes physical burden of meeting the needs of a parent. Children are sometimes forced to become caregivers because funds are scarce. About 20% of family caregivers spend 40 hours per week caring for their loved ones. Sometimes children will sacrifice promotions at work, or may have to quit their job to care for a parent(s). It is not unusual for a child to suffer from burnout soon after taking on this responsibility. If another sibling is not available to lend a hand or respite care is not available, it is a recipe for disaster. Many of the baby boomers will spend more time providing eldercare than childcare.

Question: How can parents regain their independence and release their children to live their own lives?

July 1983 marked a watershed moment in our history. It was the first time ever that the number of seniors exceeded the number of teenagers. In 1900 1 in every 25 person reached their 65th birthday. That number is now just less than 1 in 8.

Why a reverse mortgage works

It works because we are dealing with an asset (the home) that has carried the load of appreciating over the years. Now, after growing in value the home is going to return its love to the owner. Part of the value of the home is paying most of the closing costs of a reverse mortgage. If the client chooses, the only out of pocket expense is $450-$600 (depending upon the program). In return, a pool of money is thus created. It is the home that ultimately becomes responsible for paying the loan back. Remember, it is a non recourse loan.

Moving in Reverse

Many seniors are told to sell their homes and/or to go to their neighborhood bank to get a conventional mortgage. Let's play these options out. How many of you have represented elderly clients who sold their home? Even when everything goes well it is not a pretty picture. The emotional toll on a senior also needs to be considered. AARP in survey after survey says that a majority of our elders do not want to move. They want to stay in their homes. Their goal is to stay in the environment that contains much of their family and personal history. Usually they want to remain in an area that is familiar. The house is the story of their life.

After the home is sold, one then has to find a place to live. Often a smaller home will cost more than the home they just sold, so a sale often becomes financially impractical. Leasing new quarters also creates anxiety because the senior is compelled to give away or sell the place that stores so many of their precious memories (e.g. the client's personal residence).

Typically when one applies for a mortgage, income, assets and credit are reviewed. Front end and back end ratios are determined. Credit scores are carefully perused. While some of our elders may, in fact, be able to qualify for a conventional loan, they do not want the headache or the responsibility of paying it back on a monthly basis. Making those monthly payments is something they can do without. Many seniors on the other hand cannot qualify for a conventional loan.

Question What is a client to do if they don't want to sell or can't or chose not to obtain a conventional mortgage**?**

Risk reversal

This concept is not spoken about enough. A reverse mortgage is 100 percent risk free. First, no document requires that a borrower continue the process if they subsequently have a change of mind. **Second, every reverse mortgage has a counseling component to it.** The purpose of the independent counseling is to insure that every senior understands the concept and is not coerced into action. Third, federal law provides that even after signing the closing documents, every senior has three days to reconsider. If at that time they change their minds, then any funds that they paid out must be returned. This is a 100% risk free loan.

Our "senior pioneers"-a bit of a review and some things new

Once Again Seniors are blazing new financial trails - this time with reverse mortgages. Earlier, many of today's seniors and/or their parents also pioneered the concept of a thirty year loan.

In the early 1900's it was quite difficult for individuals to obtain mortgages. A down payment of 50% was usually required. The mortgage then was a 5 year, interest only balloon mortgage.

The cataclysm of the Great Depression marked the end of unregulated mortgage banking in this country. Many home owners could not repay their debt or refinance their existing loans. Banks lost the ability to lend when their depositors withdrew their funds.

Roosevelt's New Deal helped to restore the public's confidence in the mortgage banking industry. Soon the thirty year amortized loan became available, along with standard interest rates and standard underwriting guidelines. Loans were securitized. This added liquidity to the mortgage financial markets.

Seniors were doing things no one had done before. They were signing newly created documents. Today these very documents are considered "standard". Back then, seniors were taking on 30 years of monthly payments. At the time this was unheard of. Back then, a thirty year loan was a vastly different concept. Today this is considered standard.

Back then the United States government insured these thirty year loans. This was historic. Today this is standard.

Years ago people were warned that they would lose their homes, that they would go broke if they signed these hard to understand mortgage documents. Imagine that.

Now let us fast forward to the present. There is this new financial concept that many seniors are now exploring. While reverse mortgages have been around since the early 1960's, they were unregulated and took on many forms and were called by different names. Relatively few were done. As mentioned before, it wasn't until 1989 that Congress authorized the first government insured standardize reverse mortgage. Who says that history does not repeat itself? Now seniors are being asked to sign documents attorneys, accountants and financial planners have not seen before. Seniors are being told that if they get a reverse mortgage they will lose their home. Imagine that. It's shocking to think that a CPA/account or attorney would simple tell a client a concept like reverse mortgages is risky even though the advisor doesn't really understand the concept (sarcasm intended).

The bottom line is this. Conventional financing permitted seniors to raise their family in the home of their choosing. After many years of value appreciation, the reverse mortgage is permitting many seniors to stay in their home AND live the life they were heretofore only dreaming about living.

<u>The following is worth repeating</u>. A reverse mortgage is a special kind of loan. It is special because the senior who is at least 62 years of age never has to make monthly mortgage payments.

It is special because all reverse mortgage loans are non recourse loans. This means that there is no personal liability. If the amount that eventually becomes due is greater than the value of the house (assume that the home depreciated in value during the term of the reverse mortgage) then the most the bank can receive is the value of the home. This is an incredible feature. Compare this to the loan that you have on your home now. If the same scenario happened, your bank would sue you personally for the difference. This could never happen with a reverse mortgage.

It is special because it frees up a portion of the value that a senior can covert into cash. It provides a senior with a wonderful way to tap this equity without selling and without obtaining a loan with monthly payments. Many surveys indicate that a majority of seniors prefer to remain in their homes.

It is a special loan because it can become a life saver for both the children and the parents. Over two billion dollars a month is spent in this country by children to help mom and or dad. Many cannot do it anymore. The adult children have to put money away for their own retirement and for the college education of their own children.

The parents, on the other hand, by obtaining a reverse mortgage have reclaimed their independence and their dignity. In essence, the reverse mortgage transfigures the strained relationship between parent and child into an emotional loving relationship free from “required” financial obligations.

It is special because our seniors can receive the proceeds in a variety of ways. They can receive money each month, take a lump sum, a partial lump sum or put the money in a reverse mortgage line of credit. Once they make a choice, they can always change their minds. They are never locked in to a particular way to receive their money.

Professionals today will echo the negative refrain of their colleagues of years ago. Seniors will be told not to go through with the reverse mortgage because it is a scam. Yes a reverse mortgage is different. It certainly is not a scam. The government is insuring these loans.

Professionals today are saying that the closing costs are too high. Therefore do not get it. The closing costs can be financed. (Remember, not all programs have closing costs.). Another way to look at this is that the equity of the house is paying the closing costs. Should the seniors wish to they can pay the appraisal fee and the termite inspection out of pocket. This means that for $450 they can create a stream of money they can activate in a variety of ways, stay in their home and make their dreams come true while never worrying about making those monthly mortgage payments.

On top of all this the government is assuring seniors that they will receive every penny they are due, even if the lender goes out of business. In other words, they do not have to worry about a bank closing its doors. So if you focus upon the closing costs only you will be missing the bigger more important picture.

Professionals today are saying that the monthly payments are not indexed for inflation. Therefore don't get a reverse mortgage. While the individual payments are not automatically indexed for inflation, it must be noted that the principal limit and the line of credit contain a growth factor that provides much more money over the life of the loan than the amount noted in the net principle limit. You will never find this feature in any other kind of loan product. If you obtained a home equity line of credit from your neighborhood bank for $100,000 that you did not access for 2 years how much would your line of credit be worth after this 2 year period? The answer is the same $100,000. Your line of credit would not grow. However, a reverse mortgage line of credit would be worth much more than $100,000 under this scenario.

Reverse mortgages were supposed to, as time went on; increase the amount of money available for the client via a line of credit. This increase in value is built into some programs. **For example, with the FHA program, the client's line of credit will grow at 50 basis points above the current interest.** This assumes the client took a loan with a line of credit instead of the lump sum. While there is no "inflation rider", the money available via the line of credit does grow every year at an amount well above the current inflation rates.

Professionals today are saying that a reverse mortgage is a bad idea because the parent cannot leave the home mortgage free to their children. Sometimes the parent(s) makes the same argument. In this case, all one can do is walk away. Parents will not obtain a reverse mortgage when they feel it is their obligation to leave their major asset to their children. On the other hand, many parents believe that the home is the only financial vehicle that will protect them from their current financial storm. With the inclusion of life insurance, clients can get cash in hand at closing and still pass the home debt free to the children upon death.

Just like the 30 year mortgage changed the financial life for many of our ancestors, the reverse mortgage is doing the same for our seniors. In fact, the number of seniors obtaining this financing is doubling each year. There are now competing reverse mortgage programs including a special program for seniors who own high value homes. Years from now, when we look back on the evolution of this product, people will say "What was the fuss all about. It changed the lives of our senior citizens for the better. Homes were saved from mortgage and tax lien foreclosure. Seniors were able to afford long term care insurance, home care and life insurance. It enabled seniors to accomplish estate planning goals. Because people are living longer, a reverse mortgage can insure that they will not out live their money. And best of all, these pioneers have twice shown us that financial innovation can have a profound affect upon American society.

Things your clients will be told

This section is very important. Once your client leaves your office, he or she will call a friend or a family member to tell that person about the decision to get a reverse mortgage. This is when the client will be told about all the reasons not to go forward. Most of the things your client will be told will be incorrect. This section will point out the more salient misconceptions and rumors that will be repeated. Like anything that gets repeated, people believe what they hear. So this is our attempt to clear up these misconceptions once and for all.

RUMOR: Your client will be told that they have to make monthly mortgage payments.

TRUTH: They will never ever make monthly mortgage payments.

RUMOR: Your client will be told that the bank will own the house.

TRUTH: Your client will continue to own the house. The bank will never own the home while the client is living.

RUMOR: Your client will be told that their heirs could become responsible for paying this loan back.

TRUTH: It is a non - recourse loan. There is no personal responsibility for the borrower, their estate or their heirs.

RUMOR: The loan is due and payable when the first borrower dies.

TRUTH: The loan is not due and payable until the last surviving borrower dies, sells the home or is not using the residence for 365 consecutive days. The loan must be paid in full when the youngest borrower reaches their 150th birthday.

RUMOR: Reverse mortgages are only for seniors that are poor.

TRUTH: Seniors from every economic level and from all walks of life are taking advantage of the benefits offered by a reverse mortgage. Clients range from those who own modest homes to those who own multi million dollar homes.

RUMOR: A senior must enjoy good health to qualify for a reverse mortgage.

TRUTH: This is wrong. Unlike long term care insurance, reverse mortgages are not medically underwritten. One of the most pressing issues and questions facing our growing senior population is how to effectively finance the out of control costs of long term care. These proceeds can be used either as a sole payment source for an aide or as a supplement to the hours received for home care benefits through Medicaid. Taking into account all the reverse mortgage variables, seniors may very well be able to live their final years at home and avoid nursing home placement. This allows seniors to maintain their independence and their dignity and control over their long term care. Especially in New York, where the proceeds from a reverse mortgage are not a countable resource for Medicaid purposes.

RUMOR: Closing costs are way too expensive.

TRUTH: The numbers do not tell the whole story. Not all reverse mortgage programs have closing costs. While the actual closing costs figures may be a little higher than the typical FHA program closing costs, it is important to remember that they can be financed. The main reason for the higher costs is that the HECM requires mortgage insurance in an amount of 2% while the typical FHA program requires mortgage insurance in the amount of 1.5%. Also do not forget that with a reverse mortgage, the pool of money created is paid to the borrower without requiring monthly payments and without personal liability. If you were to compare these fees with the cost of selling, taking into account the Realtor's commission, a reverse mortgage is a great savings and your client gets to stay in their home. Even if the closing costs are not as low as your client would like them to be, the benefits will usually outweigh the initial costs. This will become abundantly clear when we examine the case studies.

Case Studies

We will begin by looking at the "jumbo" reverse mortgage program. This is the program that was created for high value homes. Age is a major factor when determining just how much of the value of the home can be converted into cash. The older one is, the greater the pool of money becomes. For these and all other illustrations, the closing costs are based on typical New York City metropolitan area costs.

Assume you have a client with a home that has a value of $1,500,000. The (nearest) age of the borrower is 75. Unlike the HECM program, age and value determine the Principal Limit (the starting point). Accordingly, this borrower could realize $484,000, with Zero closing costs under the original program. Now the amount realized is 709,500. The requirement is that 100% of the money is taken as one lump sum. (This requirement has not changed)

Under the new Combo Plan, the origination fee is paid by the lender. With this plan, 75% of the amount that can be realized must be taken in one initial payment. The balance of the funds can be placed in the reverse mortgage line of credit. Any monies placed in the line of credit will grow at a guaranteed rate of 5% APR tax free. Each of these options has a prepayment bar for 5 years. This is not a prepayment penalty. The bar simply means that a borrower can not make a ***voluntary prepayment.*** Selling, death and not using the home as a primary residence are typical maturity events that would not violate the 5 year prepayment bar.

The third plan or option is now called the Credit Line and has a total closing cost of over $22,000. Under this plan the amount that could be realized is less than the other two. However the difference here is that your client could take as much or as little as they want; there is no prepayment bar and your client could receive monthly payments and or put all or some of the proceeds in a reverse mortgage line of credit. Again, the amount placed therein will grow at a guaranteed 5% APR

The question of making a prepayment or interest payments often arises with this program as well as with the HECM and the HomeKeeper plans. If your client intends to keep the reverse mortgage in place, your client could not make an interest payment **and** get a tax deduction. See IRC section 163(a). The reverse mortgage balance is increasing each month due to the unpaid interest being added to the unpaid balance. One can say that the loan is paying itself interest each month. Also note that the line of credit is a revolving line of credit. Therefore, the IRS would not look kindly upon an “interest” payment being made when the result would be to increase the amount of money one could take out from the reverse mortgage.

The interest rate on a Jumbo is based upon the 6 month LIBOR Rate (London Interbank Offered Rate). The rate is discounted by 50 basis points for the first six months. After this time your client will receive the fully index rate at that time.

Estimates For:	DOB	Nearest Age	Age
Dr. John Smith	2/1/1932	75	75
Roslyn Heights, NY			
	Credit Line Cash Advt.	Combo Cash Advt.	Cash Out Cash Advt.
Initial Interest Rate	8.40%	8.40%	8.40%
Expected Interest Rate*	8.90%	8.90%	8.90%
Interest Rate Cap	14.90%	14.90%	14.90%
Monthly Service Fee	$20	$20	$20
Estimated Home Value	$1,500,000	$1,500,000	1,500,000
Lending Limit	$1,500,000	$1,500,000	$1,500,000
Percentage	100.00%	100.00%	100.00%
Credit line Growth Rate	5%	5%	5%
Principal Limit	$709,500.00	$709,500.00	$709,500.00
Service Set-Aside	$0.00	$0.00	$0.00
Available Principal Limit	$709,500.00	$709,500.00	$709,500.00
Initial Mort. Ins. Prem.	$0.00	$0.00	$0.00
Financed Origination Fee	$14,190.00	$0.00	$0.00
Other Financed Costs	$8,481.28	$8,481.28	$0.00
Net Principal Limit	$686,828.72	$701,018.720	$709,500.00
Debt Payoff Advance	$0.00	$0.00	$0.00
Tax & Ins. Set-Aside	$0.00	$0.00	$0.00
<u>Net Available to You</u>	$686,828.72	$701,018.72	$709,500.00
Cash Requested	$0.00	$523,613.72	$709,500.00
Credit line Requested	$686,82872	$177,375.50	$0.00
Remaining Cash	$0.00	$0.00	$0.00
	or	or	Or
Potential Tenure Payments	$0.00	$0.00	$0.00
Financed Fees and Costs	$22,671.28	$8,481.28	$0.00
Borrower Paid Costs	$0.00	$0.00	$0.00

If we make your client older, you will see that the amount realized will be greater. On the other hand, when there are two borrowers under the "jumbo" plan (and the Homekeeper plan) the amount that can be realized will decrease, as the bank must wait for the survivor to pass before the loan will be repaid. (Under the HECM plan, an additional borrower will not affect the amount available)The next two charts illustrate these points.

Estimates For:	DOB	Nearest Age	Age
Dr. John Smith	8/1/1920	85	85
Roslyn Heights, NY			
	Credit Line Cash Advt.	Combo Cash Advt.	Cash Out Cash Advt.
Initial Interest Rate	8.40%	8.40%	8.40%
Expected Interest Rate*	8.90%	8.90%	8.90%
Interest Rate Cap	14.90%	14.90%	14.90%
Monthly Service Fee	$20	$20	$20
Estimated Home Value	$1,500,000	$1,500,000	1,500,000
Lending Limit	$1,500,000	$1,500,000	$1,500,000
Percentage	100.00%	100.00%	100.00%
Credit line Growth Rate	5%	5%	5%
Principal Limit	$787,500.00	$787,500.00	$787,500.00
Service Set-Aside	$0.00	$0.00	$0.00
Available Principal Limit	$787,500.00	$787,500.00	$787,500.00
Initial Mort. Ins. Prem.	$0.00	$0.00	$0.00
Financed Origination Fee	$15,750.00	$0.00	$0.00
Other Financed Costs	$8,481.28	$8481.28	$0.00
Net Principal Limit	$763,268.72	$779,018.72	$787,500.00
Debt Payoff Advance	$0.00	$0.00	$0.00
Tax & Ins. Set-Aside	$0.00	$0.00	$0.00
Net Available to You	$763,268.72	$779,018.72	$787,500.00
Cash Requested	$0.00	$582,143.72	$787,500.00
Credit line Requested	$763,268.72	$196,875.00	$0.00
Remaining Cash	$0.00	$0.00	$0.00
	or	or	or
Potential Tenure Payments	$0.00	$0.00	$0.00
Financed Fees and Costs	$24,231.28	$8,481.28	$0.00
Borrower Paid Costs	$0.00	$0.00	$0.00

Estimates For:	DOB	Nearest Age	Age
Dr. and Mrs. Smith	2/1/1922	85	85
Roslyn Heights, NY	2/1/1922	85	85

	Credit Line Cash Advt.	Combo Cash Advt.	Cash OUt Cash Advt.
Initial Interest Rate	8.40%	8.40%	8.40%
Expected Interest Rate*	8.90%	8.90%	8.90%
Interest Rate Cap	14.90%	14.90%	14.90%
Monthly Service Fee	$20	$20	$20
Estimated Home Value	$1,500,000	$1,500,000	1,500,000
Lending Limit	$1,500,000	$1,500,000	$1,500,000
Percentage	100.00%	100.00%	100.00%
Credit line Growth Rate	5%	5%	5%
Principal Limit	$750,000.00	$750,000.00	$7500,00.00
Service Set-Aside	$0.00	$0.00	$0.00
Available Principal Limit	$750,000.00	$750,000.00	$750,000.00
Initial Mort. Ins. Prem.	$0.00	$0.00	$0.00
Financed Origination Fee	$15,000.00	$0.00	$0.00
Other Financed Costs	$8,312.28	$8481.28	$0.00
Net Principal Limit	$726,518.72	$779,018.72	$750,000.00
Debt Payoff Advance	$0.00	$0.00	$0.00
Tax & Ins. Set-Aside	$0.00	$0.00	$0.00
Net Available to You	$726,518.72	$741,518.72	$750,000.00
Cash Requested	$0.00	$554,018.72	$750,000.00
Credit line Requested	$726,518.72	$187,500.00	$0.00
Remaining Cash	$0.00	$0.00	$0.00
	or	or	Or
Potential Tenure Payments	$0.00	$0.00	$0.00
Financed Fees and Costs	$23,481.28	$8,481.28	$0.00
Borrower Paid Costs	$0.00	$0.00	$0.00

The next set of charts illustrates the HECM and the HomeKeeper Programs. Unlike the “jumbo” and Homekeeper programs, the HECM has three things that determine how much money one can get. These are the age of the youngest borrower, the value of the home up to the FHA lending limit for that area, and the Expected Interest Rate.

The Expected Interest Rate represents the yield on the 10 year bond plus a 1.5% margin (on the monthly adjustable). The annual adjustable has a 3.1% margin. In short, what all this means is that you can have two clients with the same age and identical value homes living in areas that have different FHA lending limits. The client who lives in the area with the higher FHA limit will have access to more funds than the client in the area with the lower limit. Notice the difference in the numbers in the next two charts.

Estimates For:	DOB	Nearest Age	Age
Dr. John Smith	2/1/1932	75	75
Maryland, NY			
	FHA/HUD Monthly Adj.	FHA/HUD Annual Adj.	Fannie Mae Standard
Initial Interest Rate	6.60%	8.20%	8.75%
Expected Interest Rate*	6.36%	7.96%	8.75%
Interest Rate Cap	16.60%	13.20%	20.75%
Monthly Service Fee	$30	$30	$30
Estimated Home Value	$400,000	$400,000	400,000
Lending Limit	$200,160	$200,160	$417,000
Percentage	50.04%	50.04%	100%
Credit line Growth Rate	7.10%	8.70%	0%
Principal Limit	$131,705.28	$107,485.12	$166,528.00
Service Set-Aside	$4,323.35	$3,764.52	$3,468.21
Available Principal Limit	$127,381.93	$103,721.40	$163,059.79
Initial Mort. Ins. Prem.	$4,003.20	$4,003.20	$0.00
Financed Origination Fee	$4,003.20	$4,003.20	$8,000.00
Other Financed Costs	$3,422.85	$3,422.85	$3,482.39
Net Principal Limit	$115,952.68	$92,292.15	$151,577.40
Debt Payoff Advance	$0.00	$0.00	$0.00
Tax & Ins. Set-Aside	$0.00	$0.00	$0.00
<u>Net Available to You</u>	$115,952.68	$92,292.15	$151,577.40
Cash Requested	$0.00	$0.00	$0.00
Credit line Requested	$0.00	$0.00	$0.00
Remaining Cash	$115,952.68	$92,292.15	$151,577.40
	or	Or	Or
Potential Tenure Payments	$804.60	$735.49	$1311.14
Financed Fees and Costs	$11,479.15	$11,479.15	$11,482.39
Borrower Paid Costs	$0.00	$0.00	$0.00

Estimates For:	DOB	Nearest Age	Age
Dr. John Smith	2/1/1932	75	75
Roslyn Heights, NY			
	FHA/HUD Monthly Adj.	FHA/HUD Annual Adj.	Fannie Mae Standard
Initial Interest Rate	6.60%	8.20%	8.75%
Expected Interest Rate*	6.36%	7.96%	8.75%
Interest Rate Cap	16.60%	13.20%	20.75%
Monthly Service Fee	$30	$30	$30
Estimated Home Value	$400,000	$400,000	400,000
Lending Limit	$362,790	$362,790	$417,000
Percentage	90.7%	90.7%	%
Credit line Growth Rate	4.89%	6.49%	100%
Principal Limit	$238,715.82	$194,818.23	$166,528.00
Service Set-Aside	$4,323.35	$3,764.52	$3,468.21
Available Principal Limit	$234,392.47	$191,053.71	$163,059.79
Initial Mort. Ins. Prem.	$7,255.80	$7,255.80	$0.00
Financed Origination Fee	$7,255.80	$7,255.80	$8,000.00
Other Financed Costs	$4004.45	$4,004.45	$3,451.37
Net Principal Limit	$215,876.42	$172,537.66	$151,608.42
Debt Payoff Advance	$0.00	$0.00	$0.00
Tax & Ins. Set-Aside	$0.00	$0.00	$0.00
Net Available to You	$215,876.42	$172,537.66	$151,608.42
Cash Requested	$0.00	$0.00	$0.00
Credit line Requested	$100,000.00	$100,000.00	$100,000.00
Remaining Cash	$115,876.42	$72,537.66	$51,608.42
	or	or	or
Potential Tenure Payments	$804.09	$578.08	$446.41
Financed Fees and Costs	$18,513.80	$18,513.80	$11,451.37
Borrower Paid Costs	$0.00	$0.00	$0.00

You will also notice that the FHA program has 2 different types of interest rates. The first one is called the initial interest rate. This is just like the note rate on any mortgage. The second noted rate is the Expected Interest Rate. It has one function - to determine how much money a senior can realize. Since the bond market fluctuates like the stock market, your client will never know exactly how much money will be available until the client gets closer to the closing date. After the closing, the subsequent fluctuation in the bond market no longer has any effect. Their numbers are now etched in stone because the loan is closed.

The Lending Limit on the left hand side of the chart is used in the downstate New York Metropolitan area. Your clients' lending limit will probably be different. (See the chart above). It is important to know just what it means. In the world of reverse mortgages, taking the above numbers into account, it means that $362,790 of the $400,000 (or $200,160 of the $400,000) home value is counted toward determining how much money could be available to your client. In our example, this means that the age of the client (75-the nearest age is used) together with the value up to the limit we just discussed, along with the Expected Interest Rate provides us with a beginning point. This beginning point is called the Principal Limit. It is from this point that amounts are deducted.

The first deduction is something called the Service Set Aside. Because your client will never make a mortgage payment, the lender that services this loan provides your client with a statement each month (and tracks the amount of funds used.) needs to get paid. This fee can be either $30 or $35. In our example it is $30. Actually, Fannie Mae makes these payments to the lender. Fannie Mae makes the payments because they actually purchase all the FHA paper. The amount that is put aside in this illustration is based on mortality tables and upon the Expected Interest Rate. The reason for this cushion is because Fannie Mae wants to be assured that when the loan is paid off, there is an amount that can be charged as reimbursement for paying the lender during the time this loan was in place. Because this amount remains the property of the borrower, interest is not being charged or accrued against this sum of money. The closing costs are deducted from the available principal limit.

The mortgage insurance premium makes up a substantial part of the closing costs. The purpose of the mortgage insurance is to insure that all seniors get every dime that is owed to them. The government stands behind every loan. In addition to this, the government will also protect the lenders as well. In the event that a sale does not bring in enough to pay the negative amortized balance, the government will make the lenders whole up to the FHA lending limit for that area.

The next cost noted is the origination fee. This fee, along with mortgage insurance amount is determined by multiplying the Maximum Claim Amount by 2 percent. The Maximum Claim Amount is the lesser of the appraised value or the FHA lending limit. In the example above, multiply the FHA lending limit by 2% to arrive at the appropriate fees.

The balance of the charges are an assortment of typical closing fees, with the bulk going to title insurance and title related charges as they exist in the New York Metropolitan area. When all is subtracted, you will see that the Monthly Adjustable provides significantly more money than the other two options. If you reside in an area that has a low FHA lending limit, you will find the Homekeeper will usually provide more funds than the HECM program. Head to head in a jurisdiction with the maximum FHA lending limit, FHA will always provide more access to funds than the HomeKeeper. This is because the internal calculations in the Homekeeper program are more conservative, notwithstanding the current single national limit of $417,000.

You will also notice that the annual adjustable has a cap of 5%, while the monthly adjustable has a cap of 10% over the start rate. The clients really look toward the program that provides them with the most funds, not the lowest interest rate.

The FHA is a very flexible program. Your 75 year old client living in Roslyn Heights can receive $1,498 per month under the tenure plan. This means that the money will never stop as long as your client is using the home as the primary residence. This means that the money will never stop even if they received a sum total greater than the $215,876.42. The money will never stop, even after many years have passed and there is no more equity in the home.

If your client needs more than this amount per month they can get it. For example, let's say that your client needs $2,000 per month.

They could receive that amount of money for 166 months. After that period of time the money will stop. Your client could even take a lump sum of $215,876.42 or a partial lump sum as well.

Your client can even combine payment options. They could take, say, about $800 per month. Then they could put about $100,000 in the reverse mortgage line of credit. The money that is in the line will grow at 50 basis points above the current note interest rate, tax free. While it is easier, to suggest that the money automatically grows at a predetermined rate, what is actually happening is that the credit limit is merely increasing. These funds are not invested earning money for the borrower.

It is important to remember that the margin on the standard FHA program has decreased to 1 point (from 1.5%). This means that FHA borrowers will receive even more funds. Typically a borrower will receive from $10,000 to $25,000 more, depending on age.

In contrast to the FHA program, the HomeKeeper program has a credit line option without the growth factor. Your client could not choose a term payment option either. The one thing that is unique to the Homekeeper program is that it can be used for a home purchase.

In Review

A reverse mortgage is the only way your clients can turn their home equity into cash while staying in the home that they love and while not having to pay a current interest payment on the loan. A reverse mortgage often is a lifesaver for both families. We discussed the sacrifices the adult children are making on behalf of their parents and in-laws. The reverse mortgage could prevent the emotional family volcano from exploding. The parents hate having to go to their kids asking for money. The parents can reclaim their independence and their dignity, while the adult children can now focus upon their own family.

Because we are living longer, we must be prepare for the unique challenges all of us will eventually face. We are probably past the time for depending on the government to take care of us. It is a time for becoming proactive. Beginning in the year 2012, 10,000 Americans per day will be turning 65. In the good old days, one got old, sick and died. That is no longer happening. There is a new paradigm. We grow old, get sick and survive….for many years.

A National Council on Aging study shows that reverse mortgages will keep millions of our seniors in their homes. Not only will it free up funds for home care but will allow millions of our elders to make needed improvements to the home. This will enable seniors to stay in the home. In fact, it is estimated that over half a trillion dollars can be extracted by over 13 million seniors who suffer from some kind of physical impairment. A significant number of seniors who suffer from Macular Degeneration, or another malady that requires that they either stay in the home or make improvements that will allow them to stay in the home. As the saying goes, “money does not grow on trees.”

Seniors do not buy long term care insurance because it is too expensive. Let us not forget that Social Security is the largest source of funds for people over the age of 65. A reverse mortgage will make that which was not affordable very affordable.

There are about 22 million senior households in this country. About 17 million of these households own their home mortgage free. The home will continue to represent the biggest untapped source of equity. Many of our elders are literally sitting on a gold mine. By showing your clients how they can easily and safely extract this gold, convert it into cash, use the proceeds for any purpose, while never having to make a mortgage payment, you will have forever changed their lives….for the better.

