Reverse Mortgages Part 3 â€“ What you need to know - An ACCESS Special Project

November 17, 2015 - This is the third in our series of articles on reverse mortgages. In Part 1, we provided you with information on the history of reverse mortgages and how they have evolved through the years. In Part 2, we provided information on the qualification process for getting a reverse mortgage. In this article, we will give you information on the various types of reverse mortgages available, how they differ from other types of mortgages and their costs.

Part 1 - Click here

Part 2 - Click here

Part 4 - Not yet published

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Is there more than one type of reverse mortgage?
Yes, there are three types of reverse mortgages.

- Single purpose â€“ these are issued by certain government agencies and by nonprofit organizations. Borrowers can only use the funds they receive for a specified purpose such as paying property taxes or home improvements.

- Proprietary â€“ these loans and the rules governing them are developed by the companies that issue the loans.

- Federally Insured â€“ also known as Home Equity Conversion Mortgages (HECM). These are the most prevalent type of reverse mortgages and are the type that you may have seen advertised. This article will only focus on this type of loan.

How is a reverse mortgage different from a regular home mortgage?

There are significant differences between a standard home loan and a reverse mortgage. You probably already know about some of these differences. For instance, with a reverse mortgage, the bank lends you money without any monthly repayment requirements. You probably also know that you can live in your house until you sell it or until your death

without making any repayments.

But there are other critical differences between a home loan and a reverse mortgage that you may not be aware of.

- HECMs are expensive â€“ Reverse mortgages are actually a very expensive way to borrow money. See the next section for more details.

- Reverse mortgages are negative amortizing loans. This means that the balance you owe increases even if you are not taking additional money out. This is an important point if you think that you may have to borrow against your home in the future. With a reverse mortgage, after a period of time you may not have any remaining equity in your home. If you are interested in learning more about negative amortization, there is a good explanation on Wikipedia.

- If you are married and your loan is setup incorrectly, your spouse could be forced to sell your home upon your death or if you move out of the house for any reason inclusive of moving into a rest home or long term care facility. Again, you will find more details below.

Are there costs associated with taking out a reverse mortgage?

Yes, but you shouldnâ€™t have to pay these fees out of your own pocket. They will be deducted from the proceeds of your loan.

Most reverse mortgages include one-time fees for loan origination, appraisal, recording, and title. Additional fees may also apply depending upon where you live. In addition to one-time fees, there are ongoing charges for mortgage insurance. Mortgage insurance is a requirement on all reverse mortgages.

Anyone considering a reverse mortgage should ask their lender to provide an estimate of all one time and annual fees prior to taking out a loan.

How much money can I borrow with a reverse mortgage?

This depends on your age at the time you take out the reverse mortgage, the way that you elect to access your money (monthly payments or a lump sum), the amount of equity you have in your home and the amount you currently owe on your home.

The older you are at the time you take out your loan, the more money you can receive. This is true whether you elect to take a lump sum or monthly payments. To see an example, use the reverse mortgage calculator found here. If you currently owe money on your home, the amount of money that you will have access to will be reduced because your current home loans must be repaid when you close on your reverse mortgage.

Of course, the overall amount of money you can borrow will be capped by the amount of equity you have in your home; up to the FHA limit of $625,000.

When my reverse mortgage closes, how is the money distributed to me?

That depends on how you choose to have the money distributed.

You can elect to receive monthly payment, take a lump sum, or combination of these two options; receiving a smaller up-front payment and then receiving monthly checks from your lender for any remaining amount. You can also elect to have your reverse mortgage set up as home equity line of credit. In this scenario, you would only take out money as you need it.

As of April 27, 2015, borrowers will only be able to gain access to 60% of the money available to them during the first 12 months of the loan. This is true regardless of which pay-out option you select. Any remaining money can be paid out in subsequent years.

Will I be charged interest on a reverse mortgage?
Yes.

Reverse mortgages are just like any other type of loan. You will accumulate interest charges on the money that you borrow. Just as with a regular mortgage, some reverse mortgages have a fixed interest rate while others have a variable rate.

Since you will not be making any payments on your reverse mortgage, the interest charges will be added to the balance of your loan and become due when your home is sold.

Why do I have to pay for mortgage insurance?

In a typical mortgageâ€¦ like the one that you used to purchase your homeâ€¦ mortgage insurance may be required to ensure that if you donâ€™t make your loan payments, the bank can be repaid on any loss associated with your loan. But in a reverse mortgage, you donâ€™t have to make any repayments until you sell your home or pass away. So why do you need to pay for mortgage insurance?

The federal government recognized the fact that by the time a homeowner dies or sells their property, the amount of money owed on their reverse mortgage could exceed the value of their home. HUD requires mortgage insurance precisely for this reason. Under this circumstance, the federal government will reimburse the bank making the loan for any loss.

In our next article, weâ€™ll cover reverse mortgage defaults, repayment and some of the available alternatives to reverse mortgages.
Links to other articles in this series:
Part 1 - Click here

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