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HUD's Reverse Mortgage Insurance Program: Home Equity Conversion Mortgages

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Summary

Reverse mortgages allow older homeowners to borrow against the equity in their homes and repay the loans at a later time, after they sell the home or pass away. Reverse mortgages differ from traditional forward mortgages both in the way in which borrowers receive the loan proceeds and the way in which the loans are repaid. Like traditional forward mortgages and home equity lines of credit, borrowers may receive a lump sum payment from the loan or have an available line of credit. However, additional options include monthly payments over a period of time or monthly payments for the life of the borrower, as long as the borrower remains in the home.

The Department of Housing and Urban Development (HUD) provides Federal Housing Administration (FHA) insurance for reverse mortgages through the Home Equity Conversion Mortgage (HECM) program. Reverse mortgages need not be insured by HUD; nevertheless, nearly all reverse mortgages are now insured through the HECM program. If homes with HECM loans are sold for less than the amount owed, the program will reimburse lenders up to a maximum claim amount (typically the appraised value of the home at the time the HECM was entered into). HUD has insured approximately 900,000 HECMs since the program's inception as a demonstration in 1988. It was made permanent in 1998.

Homeowners can qualify for HECMs if they are age 62 or older and occupy their home as a principal residence. Potential borrowers are also required to go through a counseling process, and satisfy certain financial criteria to ensure that they will be able to maintain payments toward property taxes and homeowner's insurance while they live in the home. The loan amount for which borrowers qualify depends on their age, the interest rate, and the value of the home. Borrowers pay both up-front and annual insurance premiums to participate in the HECM program.

Recent years have brought uncertainty in the financial stability of the HECM loan portfolio, part of the FHA Mutual Mortgage Insurance (MMI) Fund. One reason for this is an increasing number of borrowers withdrawing the maximum loan amount at loan closing. A high loan amount increases the risk that a loan balance may eventually eclipse the home's value. This has occurred in particular when borrowers fail to make payments toward property taxes and insurance, and the unpaid amounts are added to the loan balance. HUD, with authorization from Congress (via the Reverse Mortgage Stabilization Act of 2013 (P.L. 113-29)), has taken steps to protect the FHA MMI fund. These include requiring HECM applicants to go through a financial assessment (previously, borrower financial criteria were not taken into account) and reducing the amount that borrowers can draw during the first year of the loan.

Another issue HUD has been compelled to address is how non-borrowing spouses are treated when HECM borrowers pass away. A court found that HUD interpreted the statute incorrectly when it required loans to be due and payable on a borrower's death when a non-borrowing spouse was present in the home. As a result of the court decision, HUD issued mortgagee letters allowing non-borrowing spouses to avoid foreclosure or paying off the loan balance. They may instead remain in the home on the death of a borrower as long as the non-borrowing spouse meets certain conditions. In addition, the age of non-borrowing spouses is now part of the actuarial calculation used to determine loan amounts.

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Introduction

The Home Equity Conversion Mortgage (HECM) program, administered by the Department of Housing and Urban Development's (HUD's) Federal Housing Administration (FHA), is a reverse mortgage insurance program whereby older homeowners—those age 62 and older—borrow against the equity in their homes and FHA insures lenders against potential losses associated with the loans. Unlike conventional mortgages, HECM borrowers receive payments, either periodically or in a lump sum, and the mortgages are paid off when the home is sold. If a home is sold for less than the balance of the reverse mortgage, FHA will reimburse the lender up to a maximum claim amount. Borrowers pay an up-front fee, or premium, when they enter into HECMs, and pay annual premiums based on a loan's principal balance.

The HECM program came about as a demonstration in 1988. The impetus for creating a program to help older homeowners obtain reverse mortgages was to make home equity available for aging in place—particularly for homeowners with lower incomes who may otherwise have difficulty with maintenance and other expenses. Another idea was that reverse mortgage proceeds could be used to pay for long-term care expenses. Offering government insurance was also a means to encourage private lenders to enter into the reverse mortgage market. The HECM program became permanent in 1998 and has insured approximately 900,000 reverse mortgages since its creation.

The HECM program has faced financial difficulties in recent years, particularly since the economic downturn in 2008 and resulting declines in home values. Changes in the way HECMs are used, including increases in borrowers taking up-front lump-sum payments, also contributed to financial difficulties. A number of borrowers, having maximized their loans, faced loan default due to failure to pay property taxes and homeowner's insurance. The financial status of the program resulted in HUD making changes, including imposition of credit requirements for borrowers. In addition, HUD faced legal challenges in its regulatory interpretation of how non-borrowing spouses should be treated after the death of a borrower. As the result of a court decision, HUD has attempted to ensure that non-borrowing spouses are protected from foreclosure.

This report discusses the basics of how the HECM program works, including borrower eligibility, the amount that can be borrowed, and procedures for lender claims ("Basics of the Home Equity Conversion Mortgage (HECM)"); facts about HECMs and borrowers ("What Do We Know About HECMs?"); current issues facing the HECM program ("What Are Current Issues Surrounding HECMs?"); and the legislative history of the HECM program ("How Did the HECM Program Come About?").

Basics of the Home Equity Conversion Mortgage (HECM) Program

What Are Reverse Mortgages?

In a traditional "forward" mortgage, homeowners borrow money against the value of their homes and make monthly payments over time toward principal and interest until the mortgage is paid off. Typically forward mortgages are used to purchase homes, but homeowners may also take out second mortgages or home equity lines of credit (HELOCs) to pay for home improvements or other needs. Reverse mortgages are based on the same concept of using home equity for home maintenance and other needs, but reverse mortgages differ from forward mortgages primarily in the way that borrowers pay back the amount owed.

As with HELOCs, reverse mortgage borrowers receive money based on the equity in their home, either as a lump sum or through periodic payments. But instead of making monthly payments to repay the loan balance, a borrower is to pay back the reverse mortgage, plus accumulated interest and fees, either when they move out and sell the home or when they die and the home is sold by their estate. As a result, the term of the reverse mortgage is not fixed, unlike a forward mortgage, which extends most often for 15 or 30 years. The way in which the amount of the mortgage is determined also differs. In addition to using the home's value, the borrower's age and the interest rate are used to try to ensure that the loan balance and added interest do not outstrip the home's value.

Why Get a Reverse Mortgage?

Reverse mortgages are targeted to older homeowners and present an option for extra income as borrowers age. The ability to borrow against home equity may appeal to homeowners with lower monthly incomes and little savings. If a home is a borrower's primary asset, accessing home equity can help with everyday expenses, home improvements or modifications, or extraordinary costs that arise. Borrowers who already have home mortgage or other debt may also use reverse mortgages to pay down debt so they have fewer monthly expenses. In some cases reverse mortgages may help seniors who would otherwise not be able to remain in their homes to age in place while they remain physically able.

What Is the HECM Program?

HUD's HECM program offers FHA insurance for lenders that extend reverse mortgages to older homeowners, with borrowers paying the insurance fees. Reverse mortgages are made by private lenders, not the federal government, and for a time there was a market for reverse mortgages that did not involve government insurance. However, particularly since the 2008 economic downturn, nearly all reverse mortgages are insured through the HECM program.[1] In the HECM program, HUD offers insurance to protect lenders against losses on their loans. Lenders must be approved by FHA, and the program statute and regulations determine the amount of the loans that borrowers may enter into. Borrowers pay up-front and annual insurance premiums to HUD, and if the amount of the loan exceeds the sale price at the end of its life, HUD reimburses the lender for the difference up to a maximum claim amount. (For a discussion of the maximum claim amount, see "How Much Can Be Borrowed?")

The HECM program is governed by statute and HUD regulations, but HUD may also make changes to the program via mortgagee letters.[2] While the HECM statute uses the term

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[1] See, for example, Consumer Financial Protection Bureau, *Reverse Mortgages: Report to Congress*, June 28, 2012, Appendix I, http://files.consumerfinance.gov/a/assets/documents/201206_cfpb_Reverse_Mortgage_Report.pdf ("Today the proprietary market has all but disappeared."); and Donald L. Redfoot, *How Recent Changes in Reverse Mortgages Impact Older Homeowners*, AARP Public Policy Institute, February 2011, http://assets.aarp.org/rgcenter/ppi/ltc/fs211-economic.pdf.

[2] The HECM program is codified at 12 U.S.C. §1715z-20, the regulations are at 24 C.F.R. Part 206, and Mortgagee (continued...)

"mortgagor" to refer to borrowers and "mortgagee" to refer to lenders, this report uses the terms borrower and lender, respectively.

Who Qualifies for HECMs?

The statute governing HECMs sets out eligibility standards for both borrowers and properties.

- **Age of Borrower:** To participate in the HECM program, HUD requires homeowners to be at least 62 years of age or older.[3]
- **Type of Home:** The home being mortgaged must be a one-to-four family residence, with the homeowner occupying one of the units as their primary residence.[4] While most borrowers already occupy their homes, HECMs can also be used to purchase property.[5] In the case of a purchase, a borrower must pay the difference between the HECM and purchase price with cash from sources approved by HUD.[6]
- **Borrower Financial Characteristics:** Until recently, the HECM program did not have income or other financial requirements for borrowers because loans are repaid from home sale proceeds. However, due to the failure of approximately 10% of HECM borrowers (representing about 54,000 loans) to pay property taxes or homeowner's insurance,[7] Congress gave HUD the authority to set financial requirements.[8] (For more information about this situation, see "Financial Status of HECMs.") Effective April 27, 2015, lenders must conduct a financial assessment of new HECM borrowers.[9] Borrowers' credit histories and records in

(...continued)

Letters are available on HUD's website, http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmml.

[3] The HECM statute defines a homeowner as "any homeowner who is, or whose spouse is, at least 62 years of age or such higher age as the Secretary may prescribe." 12 U.S.C. §1715z-20(b)(1). Through regulation, HUD has established that the youngest borrower must be 62 years of age or older. 24 C.F.R. §206.33.

[4] 12 U.S.C. §1715z-20(d)(3).

[5] 12 U.S.C. §1715z-20(m).

[6] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2009-11, HECM for Purchase Program*, March 27, 2009, http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_14704.doc.

[7] See Consumer Financial Protection Bureau, *Reverse Mortgages, Report to Congress*, June 28, 2012, p. 132, http://files.consumerfinance.gov/a/assets/documents/201206_cfpb_Reverse_Mortgage_Report.pdf (hereinafter: *CFPB Reverse Mortgages, Report to Congress*). See also U.S. Congress, House Committee on Financial Services, Subcommittee on Housing and Insurance, *Sustainable Housing Finance: The Government's Role in Multifamily and Health Care Facilities Mortgage Insurance and Reverse Mortgages*, 113th Cong., 1st sess., May 16, 2013, p. 11, http://financialservices.house.gov/uploadedfiles/113-21.pdf.

[8] P.L. 113-29 gave HUD the authority to "establish, by notice or mortgagee letter, any additional or alternative requirements that the Secretary, in the Secretary's discretion, determines are necessary to improve the fiscal safety and soundness of the program authorized by this section."

[9] U.S. Department of Housing and Urban Development, Mortgagee Letter 2015-06, Home Equity Conversion Mortgage (HECM) - Delay in Effective Date for Financial Assessment and Property Charge Funding Requirements for the Payment of Certain Property Charges, February 26, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-06ml.pdf.

paying property charges are assessed, particularly payment of property taxes and homeowner's insurance.[10]

How Much Can Be Borrowed?

The amount that can be borrowed is based on the interaction of two factors:

- The **Maximum Claim Amount (MCA)**—The MCA is the lesser of a home's appraised value or the HECM loan limit for the area in which the home is located.[11] The maximum HECM loan limit is tied to the Freddie Mac conforming loan limit.[12] The current limit is $625,500 for a single-unit residence.[13] Amounts are higher for properties with 2-4 units. The MCA is the maximum that HUD will pay toward a lender's claim on insurance benefits.[14]
- The **Principal Limit Factor (PLF)**—PLFs are factors set by HUD based on borrower age, mortgage interest rate, and expected home value appreciation.[15] The PLFs are percentages applied to the MCA to determine the principal limit (i.e., the amount that can be borrowed). The older the borrower and the lower the interest rate, the higher the PLF; PLFs do not change for ages above 90 years. For example, PLFs announced in June 2014 range from 0.130 (for a borrower age 62 at a 10% interest rate) to 0.750 (age 90 at a 3% interest rate).[16] The PLF is based on the age of the youngest borrower or non-borrowing spouse, and HUD publishes separate PLFs to be used when non-borrowing spouses are under age 62. This ensures that loan amounts take into account the amount of time that both spouses are likely to remain in the home.

The **Principal Limit (PL)**, the amount that a homeowner can borrow, is determined by multiplying the MCA and the PLF. As an example, assume a borrower who is 75 years of age and has a home valued at $200,000. The initial interest rate on the loan is 5%. The PLF in this case would be 0.614 (based on PLFs announced in June 2014), resulting in a principal limit of

[10] U.S. Department of Housing and Urban Development, *HECM Financial Assessment and Property Charge Guide*, November 10, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-22ml-atch2.pdf (hereinafter *HECM Financial Assessment and Property Charge Guide*).

[11] 24 C.F.R. §206.3.

[12] The HECM statute, at 12 U.S.C. §1715z-20(g) and §1715z-20(m)(2), refers to the Freddie Mac maximum loan limits at 12 U.S.C. §1454(a)(2).

[13] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2014-25, Federal Housing Administration's (FHA) Maximum Loan Limits Effective for Case Numbers Assigned on or after January 1, 2015 through December 31, 2015*, December 5, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-25ml.pdf. HUD cites its authority in 12 U.S.C. §1715z-20(m)(2) and §1715-20(g). The latter provides that "In no case may the benefits of insurance under this section exceed the maximum dollar amount limitation established under section 1454 (a)(2) of this title for a 1-family residence."

[14] U.S. Department of Housing and Urban Development, *Handbook 4235.1, Home Equity Conversion Mortgages*, paragraph 3-8, http://www.hud.gov/offices/adm/hudclips/handbooks/hsgh/4235.1/42351c3HSGH.pdf (hereinafter: *HUD Handbook 4235.1*).

[15] PLFs are available at http://portal.hud.gov/hudportal/documents/huddoc?id=HECM_PLF__2014.xls.

[16] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2014-12, Home Equity Conversion Mortgage (HECM) Program: New Principal Limit Factors*, June 27, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-12ml.pdf (hereinafter *HUD Mortgagee Letter 2014-12*). The table is available at http://portal.hud.gov/hudportal/documents/huddoc?id=PLF_Tables_18-99.xls.

$122,800. The principal limit available to the borrower is reduced by any up-front fees, and if a borrower has an existing mortgage on the property the proceeds must be used to pay it off.

How Are Disbursements Made?

Borrowers can opt for loan payouts in a number of different ways: as a lump sum, a line of credit, in monthly payments for a term of months, in monthly payments for the borrower's lifetime, or a combination of credit line and monthly payments. Borrowers who take up-front payments (either lump sum or line-of-credit) cannot exceed an initial disbursement limit. The initial disbursement limit is the greater of 60% of the principal limit (as described in the previous section) or any mandatory obligations (e.g., fees, debt payoff) plus 10% of the principal limit.[17] Total disbursements cannot exceed the principal limit. See **Table 1** for more information on each payment option.

Table 1. HECM Payment Options

Type of Payment	Method of Disbursement	Type of Interest Rate	Lump Sum Available?	Limit on Lump Sum	Percentage of Borrowers, 2013
Lump Sum at Closing	Single lump sum payment	Fixed	Yes	Up to the Initial Disbursement Limit.[a]	95%[b]
Line of Credit	Payments taken at borrower option.	Adjustable	Yes	Up to the Initial Disbursement Limit in first 12 months and Principal Limit (PL) thereafter.	
Term	Fixed monthly payments for a term of months.	Adjustable	No	—	1%
Modified Term	Combination of term of months and line of credit with a portion of the principal limit set aside for borrower draws.	Adjustable	Yes	Up to the Initial Disbursement Limit in first 12 months and PL thereafter.	2%
Tenure	Fixed monthly payments during the borrower's lifetime. The tenure option assumes payments until age 100.[c]	Adjustable	No	—	1%

[17] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2014-21, Revised Changes to the Home Equity Conversion Mortgage (HECM) Program Requirements*, November 10, 2014, p. 12, http://portal.hud.gov/hudportal/documents/huddoc?id=14-21ml.pdf (hereinafter *HUD Mortgagee Letter 2014-21*).

Type of Payment	Method of Disbursement	Type of Interest Rate	Lump Sum Available?	Limit on Lump Sum	Percentage of Borrowers, 2013
Modified Tenure	Combination of tenure payments and line of credit with a portion of the principal limit set aside for borrower draws.	Adjustable	Yes	Up to the Initial Disbursement Limit in first 12 months and PL thereafter.	1%

Source: HUD Handbook 4235.1, Chapter 5, Section 5-3; Mortgagee Letter 2014-11, Home Equity Conversion Mortgage (HECM) Program: Limit on Insurability of Fixed Interest Rate Products under the HECM Program, June 18, 2014, p. 5, http://portal.hud.gov/hudportal/documents/huddoc?id=14-11ml.pdf; Mortgagee Letter 2014-21; and Integrated Financial Engineering, Inc., Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund HECM Loans for Fiscal Year 2014, November 17, 2014, p. 26, http://portal.hud.gov/hudportal/documents/huddoc?id=AR2014MMIHECMRpt.pdf.

a. The Initial Disbursement Limit is the greater of 60% of the principal limit (as described in the previous section) or any mandatory obligations (e.g., fees, debt payoff) plus 10% of the principal limit.

b. Starting with the FY2013 HECM Actuarial Report, borrowers opting for the line-of-credit and lump-sum payments are aggregated. In FY2012, 60% of HECMs were lump sum and 34% line-of-credit. Integrated Financial Engineering, *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund HECM Loans for Fiscal Year 2012*, November 15, 2012, p. 26, http://portal.hud.gov/hudportal/documents/huddoc?id=ar2012_hecm_loans.pdf.

c. 24 C.F.R. §206.25(c).

How Much Are Mortgage Insurance Premiums?

Borrowers entering into HECMs must pay an up-front mortgage insurance premium (MIP) and an annual MIP.[18]

- The upfront premium depends on the amount made available to the borrower during the first 12 months of the loan:
  - **0.5%** when the amount available over the first 12 months of the loan is at or below 60% of the principal limit;
  - **2.50%** when the amount available over the first 12 months exceeds 60% of the principal limit.
- The annual MIP is **1.25%** of the loan amount outstanding.

Lenders add the annual premiums to the borrower's loan balance so that the premiums accrue and are repaid as part of the loan repayment. Lenders transfer the premium payments to HUD each month.[19]

For a short period of time, from 2010 to 2014, HUD made available the option for a lower up-front MIP in exchange for lower loan amounts through a product called the HECM Saver.[20] The upfront premium was .01% compared to 2.0% for the standard HECM product at the time.

[18] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2014-21*, p. 12.

[19] U.S. Department of Housing and Urban Development, *HUD Handbook 4235.1*, paragraph 7-3.

[20] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2010-34, Home Equity Conversion Mortgage Program – Introducing HECM Saver; Mortgage Insurance Premiums and Principal Limit Factor Changes* (continued...)

What Obligations Do Borrowers Have?

Unlike forward mortgages, HECM borrowers do not make monthly payments toward the balance of the loan, but they still must satisfy other obligations.

- **Counseling:** The HECM statute requires that potential borrowers go through counseling.[21] Further, spouses are to participate in counseling even if they will not be on the mortgage. Prior to 2011 it was recommended that non-borrowing spouses attend counseling, but in 2011 HUD issued a mortgagee letter making it a requirement.[22] (See "Spouses of Borrowers" for background.) Counseling must be provided by a counselor who has gone through the HUD approval process, which requires employment by a HUD-approved counseling agency, initial and continued success in passing a counseling exam, and training and education.[23] Counseling may occur over the phone or in person.[24] Counselors are to talk with potential borrowers about options other than HECMs, financial implications of HECMs, possible consequences regarding taxes or eligibility for benefits, or consequences to the borrower's estate.[25]

- **Principal Residence:** Borrowers must stay in the home as their principal residence, meaning that it is maintained as a permanent residence where the borrowers stay for the majority of the year.[26]

- **Good Repair:** Borrowers are to keep the home in good repair.[27]

- **Property Taxes and Homeowners Insurance:** Borrowers must pay their property taxes and homeowner's insurance.[28] In a forward mortgage, these payments are often added to the monthly mortgage payment to be set aside in an escrow account and paid on behalf of the borrower. However, this arrangement does not necessarily occur with HECMs, though borrowers have the option for lenders to set aside these payments and add them to the balance of the loan.[29] Similarly, if a borrower fails to make payments toward taxes and insurance, the lender may make the payments and add them to the balance of the HECM. However, in both cases, because many HECM borrowers take up-front lump-sum

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for HECM Standard, September 21, 2010, http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_14697.pdf.

21 12 U.S.C. §1715z-20(d)(2)(B).

22 See U.S. Department of Housing and Urban Development, *Mortgagee Letter 2006-25, Home Equity Conversion Mortgage Program: Home Equity Conversion Mortgage Counseling Requirements*, September 28, 2006, p. 2, http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_20424.doc; and *Mortgagee Letter 2011-31, Home Equity Conversion Mortgage (HECM): Revised Form HUD 92902, Certificate of HECM Counseling and Clarification of Counseling Guidance*, August 26, 2011, p. 2, http://portal.hud.gov/hudportal/documents/huddoc?id=11-31ml.pdf.

23 24 C.F.R. §206.304(b).

24 U.S. Department of Housing Urban Development, *Mortgagee Letter 2004-48, Home Equity Conversion Mortgage (HECM) Counseling Requirements Simplified*, December 30, 2004, pp. 1-2, http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_20429.doc.

25 12 U.S.C. §1715z-20(f).

26 24 C.F.R. §206.3.

27 24 C.F.R. §206.27(b)(5).

28 24 C.F.R. §206.27(b)(6).

29 24 C.F.R. §206.205.

payments, adding taxes and insurance to the loan balance may exceed the amount that they are entitled to borrow. As the result of failure of some borrowers to remain current on property tax and insurance payments, HUD issued new financial guidelines. For more information see the "Financial Status of HECMs" section of this report.

How Do HECMs End?

HECMs are designed to ensure that homeowners are not displaced.[30] HECMs become due and payable when a borrower dies or conveys the property.[31] In addition, HECMs may become due and payable upon the Secretary's approval if a borrower no longer resides in the home as a principal residence, has not lived in the home as a principal residence for 12 consecutive months for health reasons, or does not perform an obligation under terms of the mortgage.[32] As noted, such obligations include paying property taxes and homeowner's insurance and keeping the home in good repair.[33] In cases of unpaid property charges, lenders may give borrowers the opportunity to become current on payments before proceeding to foreclosure.[34]

When the HECM becomes due and payable, the lender is to notify HUD and let the borrower (or their estate[35]) know of their options. The borrower may do one of three things:[36]

- Pay the mortgage balance in full, including accrued interest and fees.
- Sell the home for at least the mortgage balance or 95% of the property's appraised value (the servicer is to obtain an appraisal within 30 days of notifying the borrower or becoming aware of the borrower's death, or at the borrower's request[37]).
- Provide a deed in lieu of foreclosure (i.e., a borrower signs the home over to the lender, typically satisfying the debt).

If none of these occur, within six months of notifying the borrower of due and payable status or becoming aware of the borrower's death, the lender is required to proceed to foreclosure.[38]

What If HECMs Exceed Home Values?

The FHA insurance provided through the HECM program protects lenders against the risk that a loan balance exceeds the home's value. A lender's options are the following:

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[30] 12 U.S.C. §1715z-20(j).

[31] 24 C.F.R. §206.27(c)(1).

[32] 24 C.F.R. §206.27(c)(2).

[33] 24 C.F.R. §206.27(b)(5)-(6).

[34] U.S. Department of Housing and Urban Development, Mortgagee Letter 2015-11, Loss Mitigation Guidance for Home Equity Conversion Mortgages (HECMs) in Default due to Unpaid Property Charges, April 23, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-11ml.pdf.

[35] See 24 C.F.R. §206.123, defining "mortgagor" to include the estate of the mortgagor for purposes of property sales.

[36] 24 C.F.R. §206.125(a)(2).

[37] 24 C.F.R. §206.125(b).

[38] 24 C.F.R. §206.125(d).

- **Assignment:** While HECMs are still active, lenders have the option to assign HECMs to HUD when a loan balance reaches 98% of the maximum claim amount (the lesser of its appraised value at the time the loan was extended or the FHA loan limit).[39] This may occur over long loan terms where adjustable interest rates rise significantly, for example, or where taxes and insurance payments are added to the loan balance. However, assignment may not occur if the mortgage is due and payable for reasons described in the previous section. When lenders assign mortgages to HUD, they make a claim for the outstanding balance up to the maximum claim amount.[40]
- **Claims:** After HECMs become due and payable, if a home is not sold for enough to cover the cost of the HECM loan balance, lenders can make a claim to HUD for the difference, up to the maximum claim amount.[41] What may be included in the claim amount depends on the way in which the property was disposed of—purchased by the lender, sold to another party at foreclosure, or sold by the borrower (or borrower's estate).[42]

What Consumer Protections Exist?

From the time federal involvement in home equity conversion was contemplated, advocacy groups and Members of Congress have made efforts to ensure that borrowers understand reverse mortgages and that protections exist to prevent exploitation.[43] As initially enacted in the Housing and Community Development Act of 1987 (P.L. 100-242), HECMs required that borrowers underwent counseling and that lenders make certain disclosures. Over the years, additional consumer protection provisions have been added to the law.

- As part of the FY1999 HUD appropriations act (P.L. 105-276), Congress required additional disclosures regarding charges included as part of HECMs, directed the HUD Secretary to work with consumer groups about consumer education, and gave the HUD Secretary discretion to impose restrictions ensuring that consumers do not pay unnecessary or excessive costs for obtaining the loans.
- The Housing and Economic Recovery Act (HERA, P.L. 110-289) prohibited HECM counselors from being associated with lenders or entities selling financial or insurance products, prevented lenders from selling financial or insurance products directly or requiring their purchase, and limited loan origination fees that can be charged.
- HERA also removed a provision in the HECM statute (added as part of the American Homeownership and Economic Opportunity Act of 2000, P.L. 106-

[39] 24 C.F.R. §206.107.

[40] U.S. Department of Housing and Urban Development, *HUD Handbook 4235.1*, chapter 8.

[41] 24 C.F.R. §206.123.

[42] 24 C.F.R. §206.129.

[43] See, for example, testimony of Leo E. Baldwin, AARP, U.S. Congress, Senate Special Committee on Aging, *Opportunities in Home Equity Conversion for the Elderly*, 97th Cong., 2nd sess., July 20, 1982, p. 44. See also U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, *Housing and Community Development Act of 1983*, report to accompany S. 1338, 98th Cong., 1st sess., May 23, 1983, S.Rept. 98-142, pp. 74-75.

569) that had allowed up-front mortgage insurance premiums to be waived when borrowers purchased long-term care insurance.

What Do We Know About HECMs?

HECM program loans are a very small portion of the mortgage market; at the program's peak in FY2009, about 115,000 new loans were insured out of 1.8 million FHA single family loans insured in the same year.[44] By comparison, the total number of mortgages originated in calendar year 2009 was nearly 9.4 million.[45] By FY2013, the number of HECMs was about 60,000.[46] The program has insured approximately 900,000 loans since its inception.[47] The average maximum claim amount, representing the ceiling on HUD's insurance obligation for a loan (and generally the appraised value of a home), was less than $100,000 in the early years of the HECM program, and has hovered around $250,000 in recent years.[48] (See **Figure 1** for the number of new loans endorsed in each year and average maximum claim amounts.)

[44] U.S. Department of Housing and Urban Development, *Monthly Report to the FHA Commissioner, September 2009*, September 2009, p. 8, http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/rmra/oe/rpts/com/commenu.

[45] Mortgage market data are available in HUD's FHA-Insured Single-Family Mortgage Market Share Reports at http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/rmra/oe/rpts/fhamktsh/fhamktqtrly.

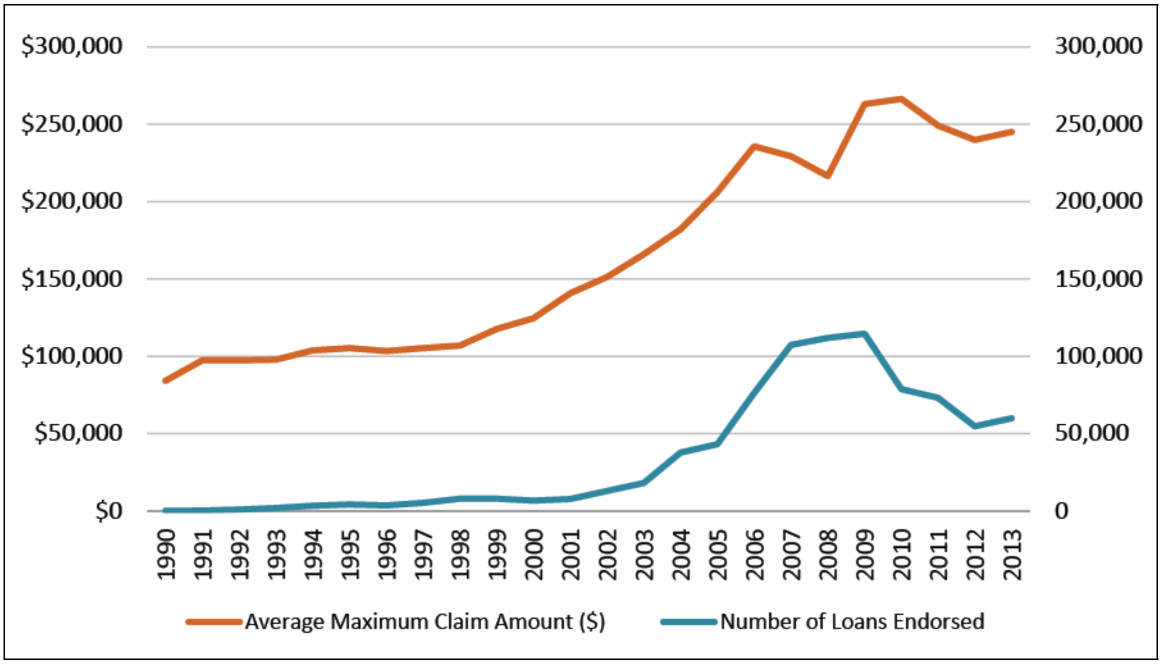
[46] Integrated Financial Engineering, Inc., *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund HECM Loans for Fiscal Year 2014*, November 17, 2014, p. 12, http://portal.hud.gov/hudportal/documents/huddoc?id=AR2014MMIHECMRpt.pdf (hereinafter *FY2014 HECM Actuarial Report*).

[47] Ibid., p. 1.

[48] Data from FY1990 to FY2012 are from the U.S. Department of Housing and Urban Development, *Home Equity Conversion Mortgage Characteristics*, September 2012, http://portal.hud.gov/hudportal/documents/huddoc?id=hecm0912.xls. HUD stopped making the data publicly available after FY2012, so FY2013 data are from the *FY2014 HECM Actuarial Report*.

Figure 1. Number of HECM Loans Endorsed and Average Maximum Claim Amount

FY1990-FY2013



Source: Data from FY1990 to FY2012 are from the U.S. Department of Housing and Urban Development, *Home Equity Conversion Mortgage Characteristics*, September 2012, http://portal.hud.gov/hudportal/documents/huddoc?id=hecm0912.xls. HUD stopped making the data publicly available after FY2012, so FY2013 data are from the *FY2014 HECM Actuarial Report*.

Since the inception of the HECM program, borrowers have gotten younger, the way in which borrowers choose to take disbursements has changed, and more borrowers appear to use HECMs to pay off existing mortgages and other debt.

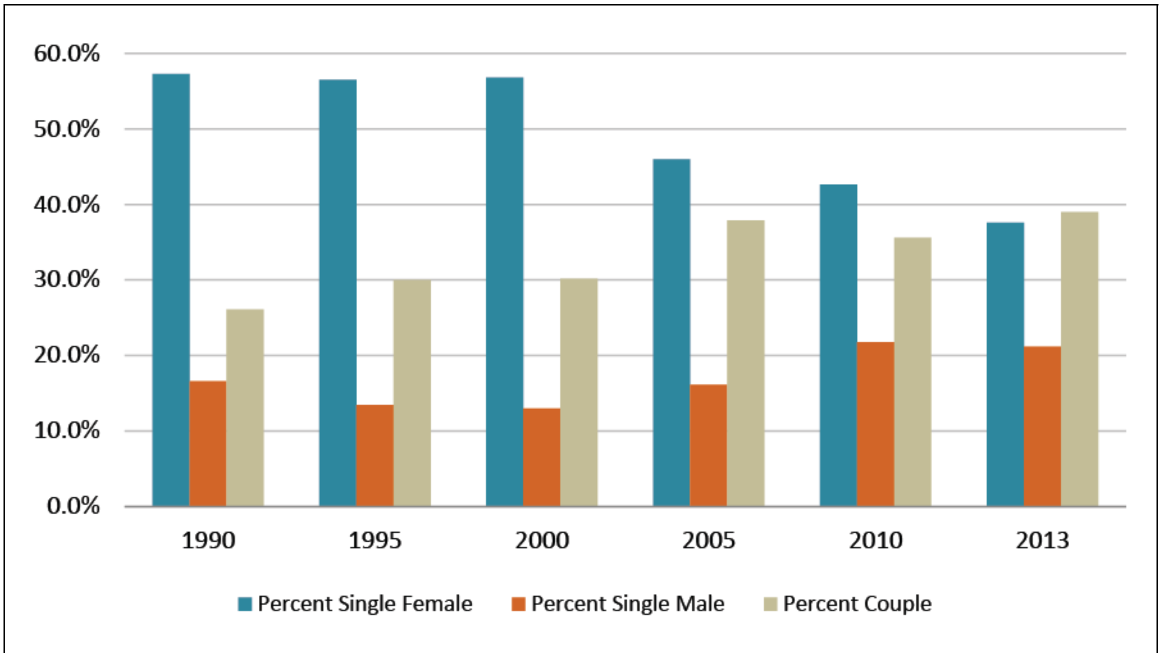
The average age of HECM borrowers has declined since the program's inception. In 1990, shortly after the HECM program was enacted as a demonstration, the average borrower age was about 77. Since then it has gradually declined to age 72 in 2013.[49] The gender of HECM borrowers has also changed over the years. Females made up more than 50% of HECM borrowers (compared to men and multiple borrowers/couples) through FY2002, but their percentages declined as the percentages of both male borrowers and couples increased. FY2013 was the first year in which couple borrowers exceeded female borrowers. Male borrowers also increased from the early years of the program, hovering around 15% in the beginning and rising to just over 20% in FY2013. The growing trend in couples borrowing could be due to the fact that borrowers are getting younger. In addition, increases in both male and couple borrowing could be related to treatment of non-borrowing spouses. Until recently, it was not uncommon for the younger spouse (generally women) to be removed from the deed and mortgage to increase the amount that could be borrowed. However, a change in rules to encourage both spouses to enter into HECMs may account for the most recent uptick in couple borrowing. See "Spouses of Borrowers" for more

[49] Ibid.

information about this issue. (See **Figure 2** for HECM borrower gender distribution for select years from FY1990 to FY2013.)

Figure 2. HECM Borrowers

Selected Years from FY1990-FY2013



Source: Data from FY1990 to FY2012 are from the U.S. Department of Housing and Urban Development, *Home Equity Conversion Mortgage Characteristics*, September 2012, http://portal.hud.gov/hudportal/documents/huddoc?id=hecm0912.xls. HUD stopped making the data publicly available after FY2012, so FY2013 data are from the *FY2014 HECM Actuarial Report*.

Notes: HUD data prior to FY2013 did not break out missing data. The *FY2014 HECM Actuarial Report* reported that data was missing for 2.3% of borrowers.

There is evidence that the credit situations of HECM borrowers may be less secure now than in earlier years of the program. In general, consumer debt, including mortgage debt, increased for homeowners age 65 and older during the 2000s.[50] In 2001, 22% of older homeowners had mortgage debt with a median amount of $43,400.[51] By 2011 the percentage had grown to 30% with a median mortgage amount of $79,000.[52] According to a 2011 survey of HECM counselors, a growing number of potential HECM borrowers gave their reason for pursuing a reverse mortgage as paying off debt—67% compared to 51% in a similar survey taken in 2006.[53] Of those

[50] Consumer Financial Protection Bureau, *Snapshot of older consumers and mortgage debt*, May 2014, p. 7, http://files.consumerfinance.gov/f/201405_cfpb_snapshot_older-consumers-mortgage-debt.pdf.

[51] Ibid., p. 8.

[52] Ibid.

[53] National Council on Aging and the Metlife Mature Market Institute, *Changing Attitudes, Changing Motives: TheMetLife Study of How Aging Homeowners Use Reverse Mortgages*, August 2011, p. 14, https://www.metlife.com/assets/cao/mmi/publications/studies/2012/studies/mmi-changing-attitudes-changing-motives.pdf.

counseled, 79% had existing debt, 40% of which was mortgage debt.[54] HUD has also acknowledged the increase in borrowers with existing property debt.[55]

Growing debt may be a reason behind the way in which borrowers take HECM disbursements. Until changes in 2014 that limited the initial draws for fixed-rate lump-sum or line-of-credit HECMs, borrowers took out large percentages of their HECM loans up front. For example, in each year from FY2010-FY2013, more than 70% of HECM borrowers withdrew between 80% and 100% of their principal limit during the first month of the loan.[56] In the early years of HECM loans, most borrowers either chose to take distributions as a line-of-credit, or combined term and tenure payments with lines of credit.[57] The changed disbursement preference can be traced to the advent of fixed interest rate HECMs. Fixed interest rate HECMs structured as closed-end loans began to become common in 2008, largely due to the ease of securitizing fixed-rate products, with HUD releasing guidance clarifying that lenders could offer fixed interest rate loans.[58] In fixed interest rate transactions, lenders require that borrowers take the entire amount of the loan up front as a lump sum (if fixed-rate products allowed future draws, lenders would have to absorb the cost of interest rate increases). Prior to 2009, lump sum payments made up less than 10% of HECMs; by the end of 2009 they made up nearly 70%.[59] Today, nearly all HECM borrowers choose to use either the closed-end lump-sum option or, using a line of credit, effectively withdraw most of the balance up front. For more information about limits on initial disbursements, see "How Are Disbursements Made?"

What Are Current Issues Surrounding HECMs?

Spouses of Borrowers

HUD's regulatory interpretation of the HECM statute created some difficulty for spouses of borrowers who themselves were not a party to the loan (i.e., non-borrowing spouses). The confusion centered on HUD interpreting the term "homeowner" in section 1715-20(j) of the code—"Safeguards to prevent displacement of homeowner"—in a way that a federal district court ruled was at odds with the statute. For years, HUD interpreted the statute to require that HECMs become due and payable upon the borrower's death, with the result that numerous non-borrowing spouses found themselves facing foreclosure or full loan repayment when their spouses passed away. Due to the court decision invalidating HUD's interpretation of the statute, HUD has changed the way in which non-borrowing surviving spouses are treated. This section explains the background and current status of non-borrowing spouses in HECM transactions.

The "Safeguards to prevent displacement of homeowner" section of the HECM statute states:

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[54] Ibid., p. 16.

[55] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2014-21*, p. 1.

[56] U.S. Department of Housing and Urban Development, *FY2014 HECM Actuarial Report*, p. 33.

[57] For example, see David T. Rodda, Christopher Herbert, and Hin-Kin (Ken) Lam, *Evaluation Report of FHA's Home Equity Conversion Mortgage Insurance Demonstration*, Prepared for U.S. Department of Housing and Urban Development, March 31, 2000, p. 30, http://www.huduser.org/Publications/pdf/hecmrpt.pdf.

[58] The origination of closed-end, fixed rate HECMs are described in detail in *CFPB Reverse Mortgages, Report to Congress*, pp. 82-88.

[59] Ibid., p. 90.

> The Secretary may not insure a home equity conversion mortgage under this section unless such mortgage provides that the homeowner's obligation to satisfy the loan obligation is deferred until the homeowner's death, the sale of the home, or the occurrence of other events specified in regulations of the Secretary. *For purposes of this subsection, the term "homeowner" includes the spouse of a homeowner* (emphasis added).[60]

Despite the statutory language including spouses as homeowners for purposes of deferring loan repayment, HUD interpreted the HECM statute to require that the mortgage become due and payable on the borrower's death, making the surviving non-borrowing spouse of a HECM borrower responsible for paying off the HECM.[61] HUD justified this policy by citing the importance of having both spouses as borrowers in order to protect the actuarial soundness of the HECM program.[62] For example, if HECMs are based on the age of an older borrower, allowing a younger non-borrowing spouse to remain in the home could cause interest and fees to accrue beyond the value of the house. Spouses may not be borrowers for a variety of reasons. If they are younger than age 62, HUD regulations do not allow them to be party to the HECM,[63] or a homeowner may remarry after entering into a HECM. Most commonly, perhaps, younger spouses were left off HECMs so that couples could obtain a larger principal limit with only the older spouse as the borrower.

Some surviving spouses were unaware that they would have to pay back the mortgage upon the mortgagor's death, resulting in at least two lawsuits against HUD, *Bennett v. Donovan*[64] and *Plunkett v. Castro*,[65] both protesting HUD's interpretation of the HECM statute and seeking relief from foreclosures against non-borrowing spouses.[66] In *Bennett*, a federal district court found that HUD's application of the regulations to the non-borrowing spouse plaintiffs was invalid, and that HUD had violated the statute in insuring the plaintiffs' loans.[67] A few months later, a group of four non-borrowing surviving spouses initiated the *Plunkett* suit, raising the same arguments as the plaintiffs in *Bennett*. The court remanded both cases to HUD to fashion a remedy. HUD presented two options for the six plaintiffs in *Bennett* and *Plunkett* to avoid moving from their homes: (1) the Mortgagee Optional Election (MOE) Assignment, whereby lenders could choose to assign HECMs to HUD if certain criteria were met;[68] and (2) the "Hold Election" option, whereby mortgage servicers could hold the HECM, subject to certain eligibility requirements,

[60] 12 U.S.C. §1715z-20(j).

[61] 24 C.F.R. §206.27(c)(1). "The mortgage shall state that the mortgage balance will be due and payable in full if a mortgagor dies and the property is not the principal residence of at least one surviving mortgagor, or a mortgagor conveys all or [sic] his or her title in the property and no other mortgagor retains title to the property."

[62] See, for example, U.S. Congress, House Committee on Financial Services, Subcommittee on Housing and Insurance, *Sustainable Housing Finance: The Government's Role in Multifamily and Health Care Facilities Mortgage Insurance and Reverse Mortgages*, Testimony of Charles Coulter, Deputy Assistant Secretary for Single-Family Housing, Federal Housing Administration, Department of Housing and Urban Development, 113th Cong., 1st sess., May 16, 2013.

[63] 24 C.F.R. §206.33. "The youngest mortgagor shall be 62 years of age or older at the time the mortgagee submits the application for insurance."

[64] 4 F. Supp. 3d. 5 (D.D.C. 2013).

[65] 2014 U.S. Dist. LEXIS 119805 (D.D.C. August 28, 2014).

[66] The *Bennett* and *Plunkett* cases were eventually consolidated, with the *Bennett* plaintiffs transferred to *Plunkett*. See *Plunkett*, 4 F. Supp. 3d at 2-3.

[67] *Bennett*, 4 F. Supp. 3d at 14-15.

[68] This MOE Assignment is described in *Plunkett*, 2014 U.S. Dist. LEXIS 119805 at *12-13.

until its balance reaches 98% of the maximum claim amount and then assign the HECM to HUD.[69]

At the *Plunkett* court's direction, HUD has also taken steps to provide similar protections to non-borrowing spouses not involved in either lawsuit. The options depend on the date on which the HECM was entered into. For HECMs entered into following the court decision, HUD is able to set loan amounts that account for non-borrowing spouses remaining in the homes.

- **Loans Entered Into On or After August 4, 2014**
  - Foreclosure will be deferred as long as the non-borrowing spouse continues to occupy the home; however, no additional payments will be made after the death of the borrower.[70] As part of this change, HUD began publishing principal limit factors (which help determine the amount of the loan) that take into account the age of non-borrowing spouses.[71]
- **Loans Entered Into Prior to August 4, 2014**
  - On June 12, 2015, HUD issued a mortgagee letter (ML 2015-15) giving lenders the option to assign HECMs to HUD, with HUD deferring payment of the HECM as long as the non-borrowing spouse fulfills certain conditions.[72] In addition, no further disbursements will be made during the deferral period. The option is similar to the Mortgagee Optional Election (MOE) Assignment available to the *Bennett* and *Plunkett* plaintiffs, though less restrictive. Non-borrowing spouses must meet certain conditions, including (1) being married at the time of HECM extension and at borrower death, or being in a committed relationship but prohibited from marrying at the time the borrower entered into the HECM and later marrying, (2) residing and continuing to reside in the property as a principal residence, and (3) obtaining marketable title within 90 days of the borrower's death or the ability to remain in the property for life. To qualify, the HECM cannot be due and payable for reasons other than the borrower's death at the time of assignment, and non-borrowing spouses must keep up with property tax and insurance payments.
  - If HECMs are ineligible for assignment or a lender chooses not to assign the loan to HUD, then foreclosure should proceed within six months of the borrower's death.

The road to the MOE Assignment option for non-borrowing spouses was not straightforward. In January 2015, HUD issued a mortgagee letter (ML 2015-03) with an assignment option based on the MOE Assignment offered to *Bennett* and *Plunkett* plaintiffs, but then rescinded it shortly

[69] The Hold Election is described in *Plunkett v. Castro*, 2014 U.S. Dist. LEXIS 163824 at *3-10 (D.D.C. November 24, 2014).

[70] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2014-07, Home Equity Conversion Mortgage (HECM) Program: Non-Borrowing Spouse*, April 25, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-07ml.pdf.

[71] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2014-12*.

[72] U.S. Department of Housing and Urban Development, HUD Mortgagee Letter 2015-15, Mortgagee Optional Election Assignment for Home Equity Conversion Mortgages (HECMs) with an FHA Case Number assigned prior to August 4,2014, June 12, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-15ml.pdf.

thereafter, in April 2015.[73] While the proposal would have given lenders the option of assigning a HECM to HUD after the borrower's death, unlike the final MOE Assignment in ML 2015-15, it included conditions regarding the loan balance that would have been difficult for non-borrowing spouses to fulfill. ML 2015-03 required either that the Principal Limit Factor (PLF) for the non-borrowing spouse had to have been greater than or equal to the PLF of the borrowing spouse at the time of origination or that the non-borrowing spouse's current PLF would result in a principal limit greater than the HECM balance. Given that non-borrowing spouses are almost always younger than borrowing spouses, the financial tests would have proved a barrier for many. After interested parties raised objections,[74] HUD rescinded ML 2015-03 and issued ML 2015-15 just over one month later. HUD estimates that allowing non-borrowing spouses with loans entered into prior to August 4, 2014, to remain in their homes will result in a cost to the FHA insurance fund.[75]

Financial Status of HECMs

HUD has made changes to the HECM program as a result of financial problems faced by the loan portfolio. Concerns about the financial stability of the HECM loan portfolio arose with the release of the FY2012 HECM actuarial report.[76] The report estimated that the HECM portfolio of loans entered into between 2009 and 2012 had a negative economic value of $2.8 billion as of the end of FY2012.[77] This meant that the combination of funds that the HECM program had on hand, plus mortgage insurance premium revenue expected in the future from HECMs existing at the time of the analysis, were not expected to be enough to cover anticipated future claims on existing HECMs (assuming no loans are insured going forward). In FY2013, the FHA Mutual Mortgage Insurance Fund (of which HECMs are a part) required a mandatory appropriation of $1.7 billion, largely due to the status of HECMs, and an additional $4 billion was transferred from the MMI capital account to the HECM financing account.[78] This section discusses the

[73] The two mortgagee letters are ML 2015-03, Mortgagee Optional Election Assignment for Home Equity Conversion Mortgages (HECMs) with FHA Case Numbers assigned prior to August 4, 2014, January 29, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-03ml.pdf; and ML 2015-12, Mortgagee Optional Election Assignment for Home Equity Conversion Mortgages (HECMs) with FHA Case Number assigned prior to August 4, 2014 - Rescission, April 30, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-12ml.pdf.

[74] For example, see Comments to the Department of Housing and Urban Development on Notice and Request for Comment Regarding the Alternative Option for Claim Payment Announced in Mortgagee Letter 2015-03 from the National Consumer Law Center, Consumers Union, California Reinvestment Coalition, Housing and Economic Rights Advocates, Institute on Aging, and The National Housing Law Project, http://www.nclc.org/images/pdf/foreclosure_mortgage/reverse-mortgages/comment-hud-mortgagee-letter-02032015.pdf.

[75] HUD Determination on Remand issued February 5, 2015, in response to the *Plunkett* court's direction. HUD estimated that, if the requirements of ML 2015-03 were followed, the cost of the MOE Assignment would be $439 million.

[76] Since 2009, new HECMs have been insured through FHA's Mutual Mortgage Insurance (MMI) Fund, which insures most FHA single-family mortgages. Mortgage insurance premiums are paid into the MMI Fund, and, in turn, any claims are paid out of the fund. The MMI Fund is subject to annual actuarial review, and a report regarding HECMs is released separately. For more information about the MMI Fund, see CRS Report R42875, *FHA Single-Family Mortgage Insurance: Financial Status of the Mutual Mortgage Insurance Fund (MMI Fund)*, by (name redacted).

[77] Integrated Financial Engineering, Inc., *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund HECM Loans for Fiscal Year 2012*, November 15, 2012, p. 13, http://portal.hud.gov/hudportal/documents/huddoc?id=ar2012_hecm_loans.pdf (hereinafter *FY2012 HECM Actuarial Review*).

[78] Integrated Financial Engineering, Inc., *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund HECM Loans for Fiscal Year 2013*, December 11, 2013, p. 17, http://portal.hud.gov/hudportal/documents/huddoc?id=IFEFY2013MMIActRev_HECM.pdf. The HECM financing account holds funds to cover expected future losses on FHA-insured loans.

reasons behind financial instability and actions taken by Congress and HUD to shore up the HECM portfolio.

Reasons for Financial Instability

Contributing factors to the status of the HECM account at the time of the FY2012 Actuarial Review included declines in home values after the housing market decline that began in 2008; longer loan life than expected; an increase in the number of homes conveyed to FHA (versus retained and sold by the borrower or lender), meaning that FHA had to maintain and market the homes; and an increasing number of borrowers who withdrew the maximum lump sum payment at loan closing rather than receiving smaller amounts.[79] This latter change increased the risk that principal balances could eventually outstrip home values. Because borrowers may quickly exhaust loan proceeds, especially by paying off existing debt, they may not have sufficient income for upkeep, property taxes, and homeowner's insurance, and those costs could be added to the loan balance. When balances rise, the chances increase that HUD may have to pay claims to lenders.

The number of borrowers failing to pay property taxes and homeowner's insurance was of particular concern to HUD and Congress. As of 2012, approximately 10% of HECM borrowers (representing about 54,000 loans) had failed to pay property taxes or homeowner's insurance and were reportedly at risk of losing their homes.[80] Unlike many forward mortgages, lenders do not automatically set aside funds in an escrow account for these payments, and if borrowers fail to make payments, lenders have the authority to make the payments and add them to borrowers' loan balances.[81] In large part, lenders paid the outstanding debts, adding them to borrower loan balances.[82] For many borrowers, adding taxes and insurance to the loan balance exceeded the amount that they were entitled to borrow.

When borrowers fail to pay property taxes and/or insurance, the loan is delinquent.[83] Once that happens, lenders do not have the option of assigning the HECM to HUD.[84] In early 2011, HUD issued a mortgagee letter clarifying that lenders are to enter into loss mitigation efforts with borrowers when they become delinquent, including offering options like repayment plans or refinancing.[85] If those efforts fail, then a lender is to issue a due and payable notice. Borrowers still have the option to become current on payments, sell the home, or supply the deed in lieu of foreclosure, but absent these things occurring, lenders must proceed to foreclosure.

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[79] See U.S. Department of Housing and Urban Development, *FY2012 HECM Actuarial Review*, pp. . ii-iii, 17-18, and U.S. Congress, House Committee on Financial Services, Subcommittee on Housing and Insurance, *Sustainable Housing Finance: The Government's Role in Multifamily and Health Care Facilities Mortgage Insurance and Reverse Mortgages*, Written Testimony of The Office of Housing/Federal Housing Administration, 113th Cong., 1st sess., May 16, 2013, p. 3, http://financialservices.house.gov/uploadedfiles/hhrg-113-ba04-wstate-hud-20130516.pdf.

[80] See Consumer Financial Protection Bureau, *Reverse Mortgages, Report to Congress*, p. 132.

[81] 24 C.F.R. §206.205(c).

[82] HUD Office of Inspector General, *HUD Was Not Tracking Almost 13,000 Defaulted HECM Loans With Maximum Claim Amounts of Potentially More Than $2.5 Billion*, August 25, 2010, p. 2, http://www.hud.gov/offices/oig/reports/files/ig1060003.pdf.

[83] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2011-01, Home Equity Conversion Mortgage Property Charge Loss Mitigation*, January 3, 2011, http://portal.hud.gov/hudportal/documents/huddoc?id=11-01ml.pdf (hereinafter *HUD Mortgagee Letter 2011-01*).

[84] 24 C.F.R. §206.107(a)(1).

[85] U.S. Department of Housing and Urban Development, *HUD Mortgagee Letter 2011-01*.

Actions Taken to Restore Financial Stability

The number of delinquencies due to failure to pay property taxes and insurance prompted Congress and HUD to take actions to protect the insurance fund. In August 2013, Congress enacted the Reverse Mortgage Stabilization Act of 2013 (P.L. 113-29). The law gave HUD the ability to use notices or mortgagee letters to "to improve the fiscal safety and soundness of the reverse mortgage program." Previously, a notice and comment period had been required, which HUD indicated was too time-consuming a process to allow timely changes to be made to protect the HECM insurance fund.[86] After enactment of P.L. 113-29, HUD initiated a number of program changes:

- In 2013, HUD limited lump sum payments by making them available only for HECMs extended under a product existing at the time called the HECM Saver. The HECM Saver offered lower up-front mortgage insurance premiums (0.01%) in exchange for low loan amounts.[87]
- Later in 2013, HUD eliminated the HECM Saver and applied new lump sum payment limits to all HECMs. HUD reduced the amount that borrowers could draw during the first 12 months of the loan and increased mortgage insurance premiums if initial draws exceed 60% of the principal limit.[88] (See "How Much Can Be Borrowed?")
- While lenders have never allowed future draws on fixed interest rate HECMs, HUD acknowledged that the possibility of this occurring presented a risk to the stability of the insurance fund. So in 2014 HUD stated that it will only insure fixed rate loans where all proceeds are taken up front in a lump sum without any possibility of future draws.[89]
- As of April 27, 2015, HUD requires that borrowers' credit histories and their ability to pay taxes and insurance be taken into account in approving HECMs.[90] This had not previously been required, unlike with many forward mortgages where credit history and ability to repay have often been a component of eligibility. FHA issued a *Financial Assessment and Property Charge Guide* along with a Mortgagee Letter containing details about what lenders should consider in

[86] See, for example, U.S. Department of Housing and Urban Development, *HUD FY2014 Congressional Budget Justifications,* FHA Mutual Mortgage Insurance Fund, p. Z-13, http://portal.hud.gov/hudportal/documents/huddoc?id=FHAMUTUALMORTINSFUND.pdf.

[87] U.S. Department of Housing and Urban Development, Mortgagee Letter 2013-01, Home Equity Conversion Mortgage Program – Consolidation of Pricing Options and Principal Limit Factors for Fixed Interest Rate Mortgages, January 30, 2013, http://portal.hud.gov/hudportal/documents/huddoc?id=13-01ml.pdf.

[88] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2013-27, Changes to the Home Equity Conversion Mortgage Program Requirements*, September 3, 2013, http://portal.hud.gov/hudportal/documents/huddoc?id=ML13-27.pdf.

[89] U.S. Department of Housing and Urban Development, Mortgagee Letter 2014-11, Home Equity Conversion Mortgage (HECM) Program: Limit on Insurability of Fixed Interest Rate Products under the HECM Program, June 18, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-11ml.pdf.

[90] U.S. Department of Housing and Urban Development, Mortgagee Letter 2015-06, Home Equity Conversion Mortgage (HECM) - Delay in Effective Date for Financial Assessment and Property Charge Funding Requirements for the Payment of Certain Property Charges, February 26, 2015, http://portal.hud.gov/hudportal/documents/huddoc?id=15-06ml.pdf.

determining eligibility.[91] Borrowers may be required to set up a "life-expectancy set-aside account," an escrow account where a portion of funds that would otherwise be proceeds to the borrower are deposited to ensure payments are made.[92]

How Did the HECM Program Come About?

While reverse mortgages were made privately on a small scale starting in the 1970s,[93] the initial federal government involvement occurred as a one-time grant through the Administration on Aging (AoA), within the Department of Health and Human Services, called the Home Equity Conversion Project. AoA awarded a grant to researchers in the State of Wisconsin to conduct a feasibility study for reverse mortgages.[94] The Wisconsin Department of Aging had already begun a "Reverse Mortgage Study Project" in 1978. It used the AoA funding to conduct consumer research and provide technical assistance on six pilot projects across the country that experimented with lending against home equity for seniors.[95]

About the same time that the Home Equity Conversion Project was underway, as part of the 1980 White House Conference on Aging, the conference's Mini-Conference on Housing for the Elderly released a report with recommendations for providing housing assistance as individuals age. One of the recommendations was to develop a way in which seniors could use home equity to supplement their income; the reverse mortgage was one of the options proposed.[96] In 1982, partially in response to the mini-conference recommendations, the Senate Special Committee on Aging held a hearing on the issue of home equity conversion,[97] and later released an informational report about options for converting home equity into income.[98]

The HECM Program from 1988 to 2000

Legislation to enact a home equity conversion mortgage program was introduced in the 98th and 99th Congresses, but no laws were enacted.[99] In the subsequent Congress, in 1988, the HECM

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[91] U.S. Department of Housing and Urban Development, *Mortgagee Letter 2014-22, Home Equity Conversion Mortgage (HECM) Financial Assessment and Property Charge Requirements*, November 10, 2014, http://portal.hud.gov/hudportal/documents/huddoc?id=14-22ml.pdf.

[92] U.S. Department of Housing and Urban Development, *HECM Financial Assessment and Property Charge Guide*, p. 75.

[93] U.S. Congress, Senate Special Committee on Aging, *Opportunities in Home Equity Conversion for the Elderly*, 97th Cong., 2nd sess., July 20, 1982.

[94] Kristina Peterson and Ingrid Heinsohn, *The Uses of Research Sponsored by the Administration on Aging, Case Study No. 6, the Home Equity Conversion Project*, American Institutes for Research, Gerontological Research Institute, August 1982, pp. 4-5.

[95] Ibid., p. 8.

[96] *White House Conference and Aging, 1981: Reports on the Mini-Conferences, MCR 1-42*, December 30, 1981, p. 332.

[97] U.S. Congress, Senate Special Committee on Aging, *Opportunities in Home Equity Conversion for the Elderly*, 97th Cong., 2nd sess., July 20, 1982.

[98] U.S. Congress, Senate Special Committee on Aging, *Turning Home Equity Into Income for Older Homeowners*, committee print, 97th Cong., 2nd sess., July 1982, (Washington: GPO, 1982).

[99] These included the Housing and Community Development Act of 1983 (S. 1338) and the Home Equity Conversion Mortgage Act (H.R. 4276) in the 98th Congress and the Housing Act of 1986 (H.R. 1) and the Banking Stability, Housing Improvement, and Consumer Protection Act of 1986 (H.R. 5576) in the 99th Congress.

program was enacted as a demonstration, the Home Equity Conversion Mortgage Insurance Demonstration (P.L. 100-242). The program was based on a combination of provisions from both a Senate-passed bill (S. 825) and a House-passed bill (H.R. 4) that were brought together in conference.[100] Based on hearings and congressional committee reports leading up to the program's enactment, the rationale for creating a reverse mortgage insurance program was to help seniors with lower incomes, and who had available home equity, remain in their homes and pay for expenses that they might not otherwise be able to afford.[101]

In addition, both of the relevant House and Senate committees discussed in their respective reports regarding HECMs the need for government insurance as a means to encourage private lenders to enter into reverse mortgages. For example, the House Committee on Banking, Finance, and Urban Affairs, in its report accompanying H.R. 4, explained its inclusion of the HECM demonstration:

> This demonstration program is designed to encourage private lenders to provide home equity conversion mortgages because many financial institutions have been hesitant to enter the field due to laws that do not recognize these types of mortgage instruments as well as the fact that the concept itself is relatively new.[102]

The committee report went on to cite with approval the fact that the bill contained protections for borrowers such as required counseling and the prohibition on involuntary displacement. The Senate Committee on Banking, Housing, and Urban Affairs report accompanying S. 825 contained similar language.[103]

P.L. 100-242 provided that HUD could insure up to 2,500 HECMs from the date of the demonstration program's enactment through September 30, 1991. The program had the following characteristics:

- Only those owning single-unit homes qualified (i.e., properties with two or more units did not qualify).
- Borrowers were allowed to prepay the mortgage without penalty.
- The law allowed for a fixed or variable interest rate.
- Homeowners were not liable for any balance outstanding on the mortgage after sale.
- The law included the requirement that borrowers receive counseling from a third party (not the lender) regarding other financial options besides a reverse

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[100] U.S. Congress, *Housing and Community Development Act of 1987*, conference report to accompany S. 825, 100th Cong., 1st sess., November 6, 1987, H.Rept 100-426, pp. 214-215.

[101] See, for example, U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, *Housing and Community Development Act of 1983*, report to accompany S. 1338, 98th Cong., 1st sess., May 23, 1983, S.Rept. 98-142, p. 74: "These mortgages would reduce the financial hardships of elderly homeowners by permitting them to tap the accumulated equity to meet expenses such as paying maintenance, tax, utility and other living expenses without being forced to move."

[102] U.S. Congress, House Committee on Banking, Finance, and Urban Affairs, *Housing, Community Development, and Homelessness Prevention Act of 1987*, report to accompany H.R. 4, 100th Cong., 1st sess., June 2, 1987, H.Rept. 100-122, p. 65.

[103] U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, *Housing and Community Development Act of 1987*, report to accompany S. 825, 100th Cong., 1st sess., March 24, 1987, S.Rept. 100-21, p. 10.

mortgage, financial implications of a reverse mortgage, and "a disclosure that a home equity conversion mortgage may have tax consequences, affect eligibility for assistance under Federal and State programs, and have an impact on the estate and heirs of the homeowner."

- The law also required that the mortgage contract contain a provision that borrowers need not repay the balance of the loan until death or sale of the home.

The HECM program continued as a demonstration for about 10 years. During that period, the program was extended three times, through September 30, 2000, and the maximum number of mortgages that HUD could insure was increased to 25,000 in 1990 (P.L. 101-508), to 30,000 in 1996 (P.L. 104-99), and shortly thereafter to 50,000 (P.L. 104-120). HUD also released three reports during this time evaluating the HECM demonstration program, as required by the statute.[104]

The only substantive change to the HECM program during the demonstration period was made as part of the Housing Opportunity Program Extension Act of 1996 (P.L. 104-120). The law expanded the program to allow FHA insurance to cover 1-4 family residences.

The FY1999 Departments of Veterans Affairs and Housing and Urban Development, and Independent Agencies Appropriations Act (P.L. 105-276) removed the demonstration status from the HECM program and increased the number of mortgages that could be insured to 150,000. The law also

- directed the HUD Secretary to consult with consumer groups, industry representatives, and representatives from counseling organizations to "identify alternative approaches to providing consumer information" to potential HECM borrowers;
- authorized (from FY2000-FY2003) up to $1 million of the amount appropriated for HUD's Housing Counseling program to be used for HECM counseling and consumer education;
- expanded disclosure requirements, requiring that borrowers know all charges involved in the mortgage, including those for estate planning and financial advice, and which charges are required for obtaining the mortgage and which are not; and
- gave the HUD Secretary the authority to put in place restrictions to ensure that a borrower "does not fund any unnecessary or excessive costs for obtaining the mortgage, including any costs of estate planning, financial advice, or other related services."

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[104] See U.S. Department of Housing and Urban Development, *The FHA Home Equity Mortgage Insurance Demonstration: A Model to Calculate Borrower Payments and Insurance Risk*, October 1990, http://www.huduser.org/Publications/pdf/HUD%20-%205802.pdf; *Preliminary Evaluation of the Home Equity Conversion Mortgage Insurance Demonstration: Report to Congress*, December 1992, http://www.huduser.org/Publications/pdf/HUD%20-%206094.pdf; and *Evaluation of the Home Equity Conversion Mortgage Insurance Demonstration: Report to Congress*, March 15, 1995, http://www.huduser.org/Publications/pdf/HUD%20-%206606.pdf.

Changes to the HECM Program Since 2000

The American Homeownership and Economic Opportunity Act of 2000 (P.L. 106-569):

- The law provided that borrowers could refinance existing HECMs. As part of the refinancing, they could receive credit for the up-front premium paid on the previous HECM, as well as waive counseling if the previous HECM had been made within the last five years. The law also gave the HUD Secretary the authority to set limits on the origination fee for the subsequent HECM.
- Owners of units in housing cooperatives were made eligible for HECMs.
- The law allowed the up-front mortgage insurance premium to be waived in instances where borrowers used the amount borrowed from the reverse mortgage to purchase long-term care insurance.

The Housing and Economic Recovery Act of 2008 (P.L. 110-289):

- The law strengthened the counseling requirement for HECM borrowers. Third party housing counselors cannot be associated (directly or indirectly) with the loan originator or servicer, or with an entity involved in selling annuities, long-term care insurance, or other financial or insurance products.
- The HUD Secretary was given authority to use a portion of mortgage insurance premiums to fund housing counseling.
- Mortgage originators were prevented from participating in the sale of insurance or financial products, or to establish firewalls within the company to ensure that there is no incentive to sell insurance or financial products to borrowers.
- Lenders were prohibited from requiring borrowers to purchase insurance and financial products as part of the reverse mortgage transaction.
- The provision that allowed the up-front mortgage insurance premium to be waived when borrowers purchased long-term care insurance (added as part of P.L. 106-569) was removed.
- The law limited the amount of origination fees that can be charged.
- HECMs were allowed to be used to purchase a 1- to 4-family home.

The Reverse Mortgage Stabilization Act of 2013 (P.L. 113-29):

- The law gave HUD the authority to establish requirements via notice or mortgagee letter (rather than regulation) regarding the fiscal safety and soundness of the HECM program.

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