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"Oversight of the FHA Reverse Mortgage Program for Seniors"

Hearing before the Subcommittee on Insurance, Housing and Community Opportunity

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Chairwoman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee:

Thank you for the opportunity to testify on behalf of AARP on the oversight of the Federal Housing Administration's reverse mortgage program. I am Lori Trawinski, Senior Strategic Policy Advisor in AARP's Public Policy Institute.

As the largest nonprofit, nonpartisan membership organization representing people age 50 and older, AARP advocates for policies that enhance and protect the economic security of older individuals. AARP has a long history of involvement with the Home Equity Conversion Mortgage (HECM) program. In the mid1980's, AARP supported the creation of the HECM pilot program. We believed then, as we do now, that older Americans should have a means by which to access their home equity without having to sell their homes or take on loans that will stretch their already tight budgets. Recognizing the need to protect older, potentially vulnerable consumers from loss of home equity, AARP advocated for the requirement that HECM borrowers obtain housing counseling from HUD-certified providers prior to applying for a reverse mortgage loan. In addition, the AARP Foundation helped develop the original HECM housing counseling protocol and ran the housing counselor training program until transferring those responsibilities to NeighborWorks in 2008.

Throughout the life of the HECM program, AARP has continued to monitor developments, advocate for consumer protections, conduct research on reverse mortgage issues, and develop policy recommendations to address the changes in this market. We are honored to be here today to present our views.

HECM Program

The HECM program has changed over the past 23 years. Throughout the 1990's, HECM volume remained well below 10,000 loans per year. In the early 2000's volume picked up and accelerated strongly until 2009, when annual HECM volume reached a record level of 114,639 loans. By then, the housing market had collapsed and home prices continued to fall. The crisis took a toll on mortgage lending of all types, including reverse mortgages, as decreased home values kept many reverse mortgage borrowers on the sidelines. In response to the increased risk to the FHA insurance fund, FHA lowered the amount of money that could be borrowed in a reverse mortgage transaction in 2010, while also increasing the ongoing mortgage insurance premium. Loan volumes declined 30 percent in 2010 and declined further in 2011.

Also notable has been a decrease in the average age of borrowers from 76 years old in fiscal year 2000 to 72 years old as of February 2012, and the increasing use of lump-sum full-draw payouts at closing. These changes may indicate that people have a need for higher amounts of money earlier in retirement, or even prior to retirement. Some of this need derives from higher amounts of forward mortgage debt being carried longer than in the past, and an increase in the overall indebtedness of Americans in general. Increasing use of full-draw lump-sum payouts could also reflect a change in how reverse mortgages are marketed. Whatever the underlying reason, borrowers who take the full draw on day one of the reverse mortgage loan exhaust their borrowing capacity immediately and accrue interest on a large balance. Younger borrowers who take out reverse mortgages have access to a smaller percentage of their home's value, since the amount that can be borrowed is based on the life expectancy of the youngest borrower. The concern is that by drawing down home equity earlier, people will have no access to additional cash later in life when they may encounter major health problems or other emergencies that require financial resources. Also, had they waited until later to take out the reverse mortgage loan, they would have had access to a larger amount of funds.

Another recent development is the continuing exit of the largest reverse mortgage lenders from the market. Financial Freedom, Bank of America and Wells Fargo exited last year, and MetLife, the largest lender in 2011, recently announced its departure. While loans are still available to people across the country, processing efficiencies have been lost, and increased costs to borrowers are likely to result.

Proprietary Reverse Mortgages

Proprietary reverse mortgages are loans made by lenders and are not insured by FHA. They have been around in many forms and have been offered by over 150 different lenders. However, proprietary reverse mortgage loan volume has never approached the level of HECM issuance, nor have private lenders been able to offer competitive rates within the HECM loan limit space. Proprietary reverse volume peaked in 2007 at 2599 loans for a total of approximately $2.6 billion.[1] Proprietary loans have typically served the "jumbo" sector of the reverse mortgage market, which is the high home value sector where loans are made on homes that far exceed the FHA home value limit.

Proprietary loans have not been made within the range of home values served by HECM program, nor are they likely to be. Consumers seek the safety of the government guarantee, particularly in the case of reverse mortgages. The FHA insurance guarantees that payments will be made to the borrower in the event of the lender's demise. Lenders in the proprietary market take on the risk that the loan will exceed the value of the home at termination. Even when home prices were rising rapidly, few lenders were willing or able to take on that risk. Currently, there are very few proprietary reverse mortgage loans being made, as depressed home values and the recent recession have weighed heavily on this market. A major downside of proprietary loans is that they lack many of the consumer protections that are mandatory in the HECM market. Therefore, these loans are riskier to the consumer.

I would now like to offer AARP's views on several key issues relating to the HECM program.

[1] Source: Gerald C. Wagner, Ibis Software Corporation; Active loans as of March 31, 2011.

Housing Counseling

Housing counseling is a major component of the consumer protections for reverse mortgages. Reverse mortgages are complex financial loans and are not easily understood even by the most sophisticated borrowers; and they are not suitable for all homeowners age 62 and older. HUD has implemented changes to the HECM counseling program that are designed to improve the quality of HECM housing counseling, including: requiring HECM counselors to attend training courses every two years and to take a certification exam every three years; introduction of the Financial Interview Tool (FIT) which consists of ten questions designed to test a borrowers' comprehension of important aspects of a reverse mortgage loan; and the requirement that both spouses attend the counseling session—even if only one spouse is on the title and applying for the loan. In addition, counselors must offer clients the opportunity to go through a Benefits CheckUp to see if they are eligible for any public benefit programs; Benefits CheckUp is mandatory for clients who are below 200 percent of the federal poverty level or are disabled.

Despite these improvements, we believe that opportunities to improve HECM counseling remain. HECM counselors tell us that they often require two or more hours to cover all topics required by the HECM counseling protocol. In contrast, other counselors, and specifically many who conduct counseling via telephone, manage to conduct a session in less than one hour. We believe that this discrepancy may highlight a potential problem with the consistency and quality of counseling, and we urge HUD to investigate this difference.

The HECM housing counseling program should be fully funded by Congress, particularly since HECM housing counseling is required by law and lenders are prohibited from paying for counseling on behalf of borrowers. AARP was pleased to see some housing counseling funds restored for FY 2012, but believe the lower funding level is not adequate and may cause some counseling agencies to run out of funds before year-end, which will lead to a curtailment of services. When funding runs out, borrowers must pay the counseling fees themselves or defer their counseling sessions until funding is restored. High quality counseling is one of the strongest consumer protections available to potential borrowers, and grants to nonprofit housing counseling agencies are vital to the effective functioning of the HECM program.

Additional funds should be allocated to foreclosure mitigation counseling. Every effort must be made to assist borrowers who have the capacity to become current on their property taxes and homeowners insurance so that they will not lose their home to foreclosure. The current program has not reached the vast majority of borrowers who are in technical default for failure to pay property taxes, homeowners insurance premiums, or both. Attention must also be paid to borrowers who have failed to pay their homeowners association dues and assessments, as these payments are vital to the ongoing operation and maintenance of condominium associations.

Financial Assessments

One of the main features in the design of the HECM loan was that income and credit history were not part of the underwriting process. The thought was that older Americans who have accumulated equity in their homes over a period of many years should have access to that equity without having to sell their home or take out a home equity loan. Many older homeowners with limited incomes would not qualify for a traditional home equity loan, since it would require monthly payments. Since the HECM loan did not require repayment as long as the borrower lived in their home, the underwriting process was largely based on the life expectancy of the youngest borrower, existence of current liens on the property, and a verification that the borrower was not in default on any federal debt.

Reverse mortgages were often recommended as loans of last resort for use when there were no other options available. As a result, low income households who were facing financial difficulty—such as a foreclosure on a forward mortgage—used the reverse mortgage to stave off the foreclosure. With a forward mortgage, monthly payments often include escrows for property taxes and homeowners insurance, but with a reverse mortgage, the borrower is responsible for making those payments—as well as homeowners association dues and assessments. It appears, however, that many borrowers are having difficulty making those payments. According to data provided by HUD, 54,000—or 9.4 percent of active HECM loans—were in technical default for nonpayment of taxes and/or homeowners insurance as of February 2012.

HUD plans to propose a rule requiring financial assessments for HECM borrowers in the near future. AARP understands the need to examine a borrowers’ financial ability to pay property taxes, homeowners insurance, homeowners’ association dues and assessments, and to be able to maintain the property. However, we do not believe that credit scores, payment history, or the existence of a bankruptcy filing or foreclosure should be part of the financial assessment. Rather, the determination should be whether borrowers have the ability to meet their basic living expenses, financial obligations and property charges, and this should be determined after taking the cash flow from the potential reverse mortgage into consideration.

AARP believes that is important to make sure that following a reverse mortgage, a borrower will have the ability to maintain payments for their obligations; if not, the reverse mortgage should not be made. Denying a loan may enable some homeowners to retain any equity they may have, instead of merely staving off the inevitable loss of a home with a loan that is destined to fail. AARP also believes that older homeowners should have access to reverse mortgage loans when they make financial sense and the borrower can maintain payments on their financial obligations. Imposition of additional requirements that go beyond household budgeting should not be included in these assessments.

Consumer Disclosures

AARP looks forward to the Consumer Financial Protection Bureau's forthcoming redesign of consumer disclosures for reverse mortgages.

AARP recommends the following change regarding statements from mortgage servicers that are periodically provided to borrowers. For borrowers who choose the line-of-credit payout option and have a creditline that grows over time, servicers should be required to:

1. Disclose the rate at which the creditline will grow; and
2. Provide a monthly or quarterly statement specifying:
    a. Creditline amount available at the close of the previous period;
    b. Withdrawals from the creditline during the current period;
    c. Creditline growth during the period; and
    d. Creditline amount remaining at the end of the period.

Advertising

We have all seen the television commercials. It is unlikely that the designers of the HECM program ever envisioned that the "The Fonz" and "I Dream of Jeannie" would appear in American living rooms to enlighten the masses about the benefits of a reverse mortgage. Some advertisements may inadvertently create the impression that a reverse mortgage is a federal benefit rather than a financial product. The decision to tap home equity is not a decision to be taken lightly and it should not be presented as anything other than a loan. These loans are not risk free or cost free and should not be presented as such. While it is appropriate to inform and educate the public about the availability of reverse mortgage loans, mass marketing of reverse mortgage loans should not be misleading or deceptive. Reverse mortgages are not appropriate for every homeowner over the age of 62. At a minimum, it should be clear that celebrities are paid spokesmen. Despite guidance in this area from the Reverse Mortgage Lenders Association, that is not always clear in the advertisements.

Another possible area of concern is the 'free lunch" seminar. These seminars are often used to present sales pitches to audiences in exchange for a free meal. In the investment sales arena, this practice has garnered the attention of the Securities and Exchange Commission and the Financial Industry Regulatory Authority. AARP conducted a survey in 2009 that examined who was invited, who attended, and what the expectations were of those who attended a free lunch seminar.[2] The report also presented information obtained from seminar attendees regarding what types of information were discussed when attending these events. Reverse mortgages were mentioned in the presentation or in the marketing materials 24 percent of the time. It appears that the investment product sales people may be presenting reverse mortgages as a means of paying for their products. While cross-selling of a financial product as a condition of obtaining a reverse mortgage is prohibited for lenders, this practice by investment salespersons appears to be a different means of cross-selling products that may not be in the best interest of consumers.

AARP has also been contacted by several of our members who have expressed concern with reverse mortgage lunch seminars being offered in their retirement communities. AARP urges the Consumer Financial Protection Bureau and state financial regulators to monitor reverse mortgage advertising and the use of free lunch seminars to ensure that no inappropriate marketing, including no inappropriate cross-selling, is occurring.

Statutory Loan Limit

To guarantee continuity of the HECM program, AARP supports legislation that would remove the statutory limit on the number of loans that can be insured by HUD in a given year. Loan limits were imposed when the HECM program was a pilot program. The loan number cap has been raised several times over the years and has, at times, led to a halt in originations when the cap was reached. Lifting the statutory loan limit would be helpful in encouraging lenders to offer reverse mortgages and remain committed to this market.

Conclusion

AARP continues to believe that older Americans should have a means by which to access their home equity without having to sell their homes or take out a home equity loan, and that a reverse mortgage can be an appropriate financial product for some people. AARP urges HUD to act in a timely manner to provide guidance in areas where there is uncertainty, such as: promulgating rules that prohibit cross-selling; and promulgating rules for financial assessments of borrowers. In addition, we support the development of a wider reaching program to assist borrowers who are in default, before the loan reaches the foreclosure stage. AARP also urges the following statutory changes: removal of the statutory limit on the number of loans that can be insured by HUD; and appropriation of sufficient funds to make sure that borrowers have access to the housing counselors they require and to the capital they need. AARP supports the continuation of the HECM program and we look forward to working with you and other stakeholders to ensure that older Americans can tap their home equity with safe, affordable, government-insured reverse mortgage loans that enhance their financial security.

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[2] Lona Choi-Allum, "Protecting Older Investors: 2009 Free Lunch Seminar Report," AARP, Knowledge Management, November 2009.

Thank you for the opportunity to share AARP's views. I would be happy to answer any questions.