Legal Problems of the Elderly (Reports No. 105)

Resolved, That the American Bar Association recognizes that home equity conversion offers older homeowners a viable option for accessing the equity in their homes;

Resolved, That the rapid growth of home equity conversion products reinforces the need for consumer education and safeguards, including full disclosure of the legal and financial consequences of these products, and counseling about other housing and service options that may be appropriate.

Further Resolved, That the American Bar Association supports the development and promulgation of local, state, federal and territorial policies ensuring that loan proceeds from home equity conversion products are disregarded in determining borrower eligibility for government benefits.
REPORT

I. BACKGROUND

For many older homeowners, maintaining a home can be a tremendous financial burden and, when coupled with health care and other daily living expenses, can deplete savings accumulated over a lifetime. While some people choose to sell their homes, the majority would prefer to stay. Many are generating additional income through home equity conversion. Several home equity conversion options exist, including sale-leaseback, sale of a remainder interest, government sponsored home repair loans, property tax credit or deferral programs, and the increasingly popular reverse mortgages.

Reverse mortgages are rising debt loans, usually paid out in a lump sum, monthly installments and/or a line of credit. Homeowners must be at least 62 years of age, and live in single family residences, usually with little or no outstanding liens or mortgages. Unlike traditional, or "forward" mortgages, borrowers need not meet minimum income requirements. The debt is secured by equity in the home, and is repaid with interest at the end of the loan term, which occurs when the owner sells or permanently vacates the house; or, less often, on a fixed repayment date; or, in the case of a reverse annuity mortgage, upon the death of the borrower. The size of the cash advances is determined by the age(s) of the homeowner(s), the value of the home, the interest rate, the loan term, the loan costs if financed, any outstanding liens that must be satisfied and the amount of the initial lump sum disbursed. The borrower retains title to the property during the loan term and remains responsible for taxes, repairs and maintenance. Reverse mortgages are non-recourse loans -- if the final mortgage balance exceeds the value of the property, the lender is limited to recovery of the appraised value of the home upon its sale. In addition to generating income to meet out of pocket expenses, reverse mortgages are being used to save homes from foreclosure, when all other avenues have been exhausted.

The most frequently utilized reverse mortgage product is the federally insured Home Equity Conversion Mortgage, (HECM) authorized by Congress in 1987 as a demonstration program. Borrowers may choose from among five payment plans, and may switch plans during the loan term. Payment on the loan is due in full upon one of several occurrences -- when the last borrower dies; when the borrower conveys title to the property and no other borrower retains title or a long-term leasehold; when the borrower fails to occupy the property for more than 12 consecutive months, and

1 AARP National Telephone Survey (1992).

2 For example, the American Association of Retired Persons receives more inquiries about reverse mortgages than any other issue.

the property is not the principal residence of another borrower; or when an obligation (such as maintenance of the property, or payment of taxes or insurance premiums) of the borrower is not performed.

While the federally-insured HECM dominates the market, other, lender-insured products are also available. Some offer monthly advances plus the option of an initial lump sum or line of credit, for as long as a person lives in the home. Others offer simply a line of credit. Still others involve an annuity purchase, which allows the homeowner to receive payments even after vacating the home. No matter what the plan, the costs are substantial when a borrower does not remain in the home for long, but decrease with each succeeding year of residence.

II. EXISTING ASSOCIATION POLICY

Recognizing the value of reverse mortgages as an option for older homeowners, particularly those who are "house rich and cash poor," and recognizing also the legal and financial complexity of these products, the Association has worked actively over the years to promote continuing legal education on the subject, and to educate counselors and other professionals about the legal issues. The Commission on Legal Problems of the Elderly, the Senior Lawyers Division and the Section on Real Property, Probate and Trust Law have all sponsored seminars and other programs, and have encouraged members of the bar to attend trainings for counselors, lawyers and financial advisors, among other groups, conducted by the American Association of Retired Persons (AARP).

In 1989, concerned that reverse mortgage proceeds would jeopardize eligibility of low-income homeowners for government benefits, the ABA voiced its support for "the development and promulgation of local, state and federal policies that ensure that loan proceeds from home equity conversion mechanisms are disregarded in determining the eligibility of elders for the benefits of public assistance programs." In 1990, the Association joined with AARP, the Federal National Mortgage Association (Fannie Mae), the Federal Reserve Board and the National Consumer Law Center, to produce a Model State Statute on Reverse Mortgages. The Model Statute contains a provision exempting loan proceeds from consideration in needs-based government benefit programs. The federal Supplemental Security income program contains such an exemption, as does Medicaid. A few states have adopted the Model Statute, and exempt reverse mortgage proceeds from consideration in state

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5 During the last decade, several lender-insured products have been introduced to the market and withdrawn.


If, however, Supplemental Security Income, Medicaid and other federal needs-based programs are converted to block grants to the states, there is a very real possibility that states will be free to establish their own eligibility rules, and could choose to count these proceeds as income. Hence, it is important for the Association to underscore its continued support for policies at the federal, state and local levels that protect low income older persons by ensuring that home equity conversion proceeds do not defeat eligibility for needed programs.

III. PROPOSED RESOLUTION

More than ten thousand federally-insured HECM loans have been closed, and new products are regularly introduced. Interestingly, HECM borrowers tend to be single women in their seventies, without children, whose median income is $10,400 per year -- people who are truly “house rich and cash poor.” The HECM program, however, remains a demonstration, and is due to expire in September, 1995.

Reverse mortgages offer older homeowners a viable option for accessing the equity in their homes, but the variety and complexity of these products raise a number of legal and financial issues. Homeowners contemplating a reverse mortgage transaction need to consider the basic real estate and contractual issues inherent in such an undertaking, and the options available under the “umbrella” of home equity conversion. Just as important are the array of issues which arise as a result of these programs and which can have far reaching impact on the borrower and his or her heirs. These issues include tax implications, eligibility for government benefits, planning for incapacity and the impact of the transaction on the borrower’s estate. Borrowers should also be aware of the alternatives to home equity conversion which may be available in the community, such as housing programs, government income and health benefits, or community support services.

The HECM program requires that prospective borrowers receive third-party counseling, performed by non-profit or public agencies approved by HUD. Counseling typically includes screening for eligibility and a discussion of alternatives, financial implications of the loan including the potential for tax consequences, effect on government benefits and impact on the borrower’s estate. Counselors have access to HUD’s computer software, which allows them to help homeowners analyze and compare different payment options. Homeowners considering a lender-insured or uninsured product are unlikely to receive even this level of counseling. Some products include a counseling component, but the service is likely to be performed by an employee of the lender or an individual who works on

Minnesota, Massachusetts, New York, Ohio and Utah are among the states with such laws. In other states, administrative agency decisions may guide program eligibility requirements.

commission for the lender. And, while some state laws require that all potential reverse mortgage borrowers have access to counseling, funding for independent counseling is virtually non-existent.

As noted earlier, at Page 2, the House of Delegates in August 1989 approved a resolution in support of local, federal and state policies that disregard home equity conversion proceeds from determinations of eligibility for need based programs. Beyond that, the Association has no comprehensive policy on the subject. The proposed resolution will serve three goals -- to place the Association firmly on record in support of home equity conversion as a serious option for older persons seeking to tap the equity in their homes; to reiterate support for state and federal laws and policies that permit low income older persons whose only resource is their home, to take advantage of that resource without jeopardizing their eligibility for government benefit programs; and to acknowledge that these products present complex legal and financial issues necessitating adequate consumer education and safeguards. Specifically, the proposed resolution would allow the Association to advocate for continuation of the Home Equity Conversion Mortgage Demonstration program and other useful products. Less directly, but no less significantly, the proposed resolution would place the Association firmly behind efforts to educate the legal profession about these important issues.

The proposed resolution poses no cost to the Association.

Respectfully submitted,

Alexander D. Forger
Chair
Commission on Legal Problems of the Elderly

Max Gutierrez, Jr.
Chair
Section of Real Property, Probate and Trust Law

1. **Summary of Recommendation(s).**
   Supports home equity conversion, including reverse mortgages, as an option for older homeowners; supports consumer safeguards, counseling and information about financial and legal consequences; reiterates existing Association support of laws and policies that disregard loan proceeds from consideration of eligibility for needs-based government programs.

2. **Approval by Submitting Entity.**
   The Commission on Legal Problems of the Elderly approved this recommendation at its May 12, 1995 meeting. At its May 6 meeting, the Section on Real Property, Probate and Trust Law voted to co-sponsor the recommendation.

3. **Has this or a similar recommendation been submitted to the House or Board previously?**
   In 1989, the House of Delegates approved a resolution supporting "local, state and federal policies that insure that loan proceeds from home equity conversion mechanisms are disregarded in determining the eligibility of elders for the benefits of public assistance programs."

4. **What existing Association policies are relevant to this recommendation and how would they be affected by its adoption?**
   The only existing Association policy on this issue is described at #3, above. This recommendation would complement that resolution, by broadening the Association's support for home equity conversion products, for consumer safeguards and for access for older persons to information and counseling about the legal and financial implications of these products.

5. **What urgency exists which requires action at this meeting of the House?**
   Legislation to extend Federal Home Equity Conversion Mortgage Insurance Demonstration is anticipated.

6. **Status of Legislation. (If applicable.)**
   The Home Equity Conversion Mortgage Insurance Demonstration program, through which lenders approved by the US Department of Housing and Urban Development offer FHA-Insured reverse mortgages, is due to expire in September 1995. There is no legislation pending that
would continue the program; however, it is anticipated that such legislation will be introduced in the near future.

7. Cost to the Association. (Both direct and indirect costs.)
   None.

8. Disclosure of Interest. (If applicable.)
   None.

9. Referrals.
   On or before June 7, 1995, copies of this recommendation and report were mailed to all ABA Sections and Divisions, as well as to all other entities considered to have a potential interest in it.

10. Contact Person. (Prior to the meeting.)
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11. Contact Person. (Who will present the report to the House.)
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12. Contact Person Regarding Amendments to This Recommendation. (Are there any known proposed amendments at this time? If so, please provide the name, address, telephone, fax and ABA/net number of the person to contact below.)
    There are no known proposed amendments at this time.