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HOW DO REVERSE MORTGAGES WORK

How do Reverse Mortgages Work?

When you have a regular mortgage, you pay the lender every month to buy your home over time. In a reverse mortgage, you get a loan in which the lender pays you. Reverse mortgages take part of the equity in your home and convert it into payments to you, a kind of advance payment on your home equity. The money you get usually is tax-free and it generally won't affect your Social Security or Medicare benefits. Generally, you don't have to pay back the money for as long as you live in your home as your primary residence. In addition, lenders do not establish escrow accounts, therefore you are responsible to pay your taxes and insurance, flood insurance, HOA/Condo fees and maintain the home in a reasonable fashion. Alternatively, a set aside account can be established to pay for these various fees and borrowers can fund this account from their reverse mortgage loan proceeds.

Not complying with all loan terms can result in defaulting on the loan and borrowers can be subject to foreclosure. The loan becomes due and payable when the last remaining spouse no longer occupies the home or you sell the home. You and your heirs are afforded an ample time period to repay the obligation.

Q: What if I have an existing mortgage?

You may qualify for a reverse mortgage even if you still owe money on an existing mortgage. However, the reverse mortgage must be in a first lien position, so any existing indebtedness must be paid off. You can pay off the existing mortgage with a reverse mortgage, money from your savings, or assistance from a family member or friend. For example, let's say you owe $100,000 on an existing mortgage. Based on your age, home value, and interest rates, you qualify for $125,000 under the reverse mortgage program. Under this scenario, you will be able to pay off ALL the existing mortgage and still have $25,000 left over to use as you wish.

Q: Does the bank own my home?

No. You and your heirs always own you home just like any other loan.

Q: Can I/we hold title in a trust?

Yes, as long as the trust meet HUD guidelines. Have your Reverse Mortgage Specialist know right away so they can have your trust reviewed and approved immediately so there are no surprises later.

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Q: What happens if we live a long time and we owe more than the house is worth when it is time to pay off the loan?

Part of the FHA insurance guarantees that you will never have to pay more than the property is worth in a bona-fide sale.

What are the differences between a reverse mortgage and a home equity loan?

With a second mortgage, or a home equity line of credit, borrowers must make monthly payments on the principal and interest. A reverse mortgage is different, because it pays you; there are no monthly principal and interest payments.

Q: Under what circumstances should I not consider a reverse mortgage?

Because of the upfront costs associated with a reverse mortgage, if you intend to leave your home within 2 to 3 years, there may be other less expensive options to consider, such as home equity loans, no-interest loans or grants that may be offered by your county government or a local non-profit to repair your home, or a tax deferral program, if you're having problems paying your property taxes. Also, if you want to leave your home to your children, then you should consider other options, because in many cases, the home is sold to pay back a reverse mortgage.

Q: How does the interest work on a reverse mortgage?

With a reverse mortgage, you are charged interest only on the proceeds that you receive. Both fixed and variable interest rates are available. Rates are tied to an index, such as the 1-Yr. Treasury Bill or the London Interbank Offered Rate (LIBOR), plus a margin that typically adds an additional one to three percentage points onto the rate you're charged. Interest is not paid out of your available loan proceeds, but instead compounds over the life of the loan until repayment occurs. A reverse mortgage is not free money. It is a loan that you, or your heirs, will eventually have to pay back, usually by selling your home.

Borrowed money + interest + fees each month = rising reverse mortgage loan balance.