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REVERSE MORTGAGES: POLISHING NOT TARNISHING THE GOLDEN YEARS

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REVERSE MORTGAGES: POLISHING NOT TARNISHING THE GOLDEN YEARS

WEDNESDAY, DECEMBER 12, 2007

U.S. SENATE,
SPECIAL COMMITTEE ON AGING,
Washington, DC.

The Committee met, pursuant to notice, at 10:39 a.m., in room SD–628, Dirksen Senate Office Building, Hon. Claire McCaskill, presiding.

Present: Senators Kohl, Carper, Salazar, McCaskill, Smith, and Martinez.

OPENING STATEMENT OF SENATOR HERB KOHL, CHAIRMAN

The CHAIRMAN [presiding]. I would like to call the hearing to order at this time, and recognize our witnesses, and express our appreciation to all of you for being here, for what will be I am sure a very insightful hearing. I would like particularly to thank Senator Claire McCaskill, who has put together this hearing and will for the most part Chair it.

In 1987, the Department of Housing and Urban Development created the Federal Home Equity Conversion Mortgage program. Known as HECM, the program was charged with reviewing the use of reverse mortgages. Twenty years later, we have seen the number of reverse mortgages skyrocket. In fact, HECM reverse mortgage loans increased by 41 percent from fiscal year 2006 to fiscal year 2007. In my State of Wisconsin, there has been a 97 percent increase in HECM reverse mortgages during the same time period.

American consumers see and hear advertisements for reverse mortgages all the time. Agents are targeting seniors aggressively in ways that this Committee has seen before, like through direct mail, celebrity endorsements, and free lunch seminars. Marketers often gloss over the risks of a reverse mortgage, but they convey the payoff quite clearly.

Now, when used properly, reverse mortgages can be an effective way for seniors to tap into the equity in their house as a means to bolster their retirement security. But too often these products are not used effectively and seniors end up losing their homes. Some salesmen are also convincing seniors to swallow this double-dose of bad financial advice, namely to take the cash from a reverse mortgage and use it to fund an unsuitable annuity. As this Committee determined at our September 5 hearing, long-term annuities are almost always inappropriate for seniors, as they can tie up retirement savings far beyond one's life expectancy.

Both Senator McCaskill and I would like to see the rights and interests of senior homeowners protected. I am happy to be working with Senator McCaskill on legislation that she is crafting that would strengthen consumer protection, fund independent financial counseling, and institute regulations to safeguard seniors from predatory lending tactics.

So we thank you all for being here today. Before the gavel is turned over to Senator McCaskill, I would like to turn to the Ranking Member on this Committee, Senator Gordon Smith.

OPENING STATEMENT OF SENATOR GORDON SMITH, RANKING MEMBER

Senator SMITH. Thank you, Senator Kohl and Senator McCaskill for organizing this hearing. This is a very important one. We do need to do our best to ensure that the integrity of reverse mortgages is sustained throughout the very sizable growth in the industry.

Reverse mortgages are becoming an increasingly popular option for seniors to supplement their income, meet unexpected medical expenses and many other kinds. The advantage of a reverse mortgage is that it allows seniors to remain in their home, retain ownership of their home, and on top of all that, to receive cash payments.

Although reverse mortgages became available in the United States 20 years ago, this loan market only recently has seen very rapid growth. From 1990 to 2002, FHA-insured loans grew from 157 to 13,000. In 2007, FHA issued over 107,000 reverse mortgage loans. That is a 68,000 percent increase in just 17 years.

However, as this rapid growth continues, so grows our responsibility to properly inform and prepare senior homeowners for what could potentially be a marketplace ripe for inappropriate products and downright fraudulent brokers. Increasing emphasis on the continued need for well-trained FHA-approved senior mortgage counselors, targeting and eliminating inappropriate products and brokers, and enhancing overall consumer education are all areas that we need to improve in.

The Department of Housing and Urban Development and private lenders have an ever-increasing level of responsibility. With proper preparation and planning, the industry stands to provide seniors with much-needed income and stability, while without it seniors stand to lose their home, their lifestyle and their peace of mind.

HUD's Home Equity Conversion Mortgage program has proven successful thus far. Since its inception, the cap on the number of mortgages allowed in the program has been increased a number of times. The elimination of the cap can benefit more elderly citizens who have the vast majority of their wealth tied up in their homes and need cash to pay for expenses in their golden years. I support legislative efforts to remove this cap.

We hear a lot about the concept of aging in place, and with strong consumer protections, the reverse mortgage industry has the chance to provide seniors the opportunity to do just that—to grow old in a comfortable, secure home environment.

So thank you, Senator Kohl and Senator McCaskill for this important hearing.

OPENING STATEMENT OF SENATOR CLAIRE MCCASKILL

Senator MCCASKILL [presiding]. Thank you.

Thank you, The Chairman. I am grateful for the opportunity to work on this issue with both you and with Senator Smith, the ranking on this Committee. I think it is important that we look at this issue.

I want to welcome everyone to today's hearing. In particular, I want to thank our witnesses for taking time to appear here today. Obviously, it is an honor to be given this opportunity to work on this issue and to Chair this hearing.

Today, we will discuss the rapidly increasing market of reverse mortgages. We will examine how reverse mortgages have helped seniors use their home equity to meet their needs during retirement, but more importantly how reverse mortgages can and do become a tool for predatory lending that strip seniors of their home equity and puts them in financial trouble.

According to the American Housing Survey, there are more than 12.5 million people aged 65 or older with no mortgage debt, representing over $4 trillion in home equity. These numbers will undoubtedly increase with the looming retirement of the baby boom generation.

In addition, there has been incredible growth of companies marketing reverse mortgages, rising from a few hundred a couple of years ago to over 1,400 different companies today. This is on top of over 20 different proprietary, privately insured products currently being marketed to seniors. There are numerous concerns which we need to address regarding this product, including the risks to the Federal Government in insuring these mortgages.

Since the Federal Government insures the vast majority of these loans, there are very real liabilities. As we have recently witnesses in the subprime debacle, real estate is no sure bet. There are numerous scenarios where the loan balance will exceed the home value. In these instances, the collateral risk falls to HUD and the American taxpayer, because lenders can currently assign these loans to the Federal Government, thus leaving the taxpayer on the hook for the fees charged on the loan and the unpredictable and sometimes unrealistic expectations of always-increasing home values and low interest rates.

We have gone through a saving and loan collapse, a stock market bubble, and are currently in the middle of a lending mess. Our goal is to make sure that the reverse mortgages don't become the scandal of the next decade. We are aware of reports of unscrupulous and predatory activities of some of the companies that are marketing reverse mortgages, as well as excessive fees to service the loans. It seems obvious that one of the reasons for the unprecedented growth of this market is due to the fact that there is a lot of money to be made.

I will point your attention to one such pitch, trying to lure salesmen into this line of work. It begins with, "This will be the easiest sale you have ever made. The market for reverse mortgages is exploding and fortunes are being made as you read this. Here is your opportunity to get in on the ground floor of a business that could make you incredibly rich. All that is required is your ability to follow directions so that you, too, can cash in on this once-in-a-lifetime boom."

I will not go any further on this since we have invited witnesses to provide testimony on some of these practices. We must make sure protections are offered to the elderly to help them avoid programs that are not financially beneficial to them and may actually be harmful. As a condition of receiving a reverse mortgage, the borrower must receive counseling by a HUD-certified counselor. Unfortunately in this multi-billion dollar industry, HUD has only set aside $3 million to help ensure that our elderly are not taken advantage of by predatory lenders.

You may say to yourself, it is not possible to employ enough counselors to service all these loans for $3 million, and you would be exactly correct. One of the largest counseling agencies reported providing over 100,000 counseling sessions this year and expects to conduct 240,000 counseling sessions next year. At $100 per session, that is a $24 million shortfall over what HUD is spending.

Who fills in the shortfall in the government-approved counselors? The mortgage lenders themselves are in fact funding some of the counselors. These counselors are able to become HUD-qualified and are then paid for by the very people they are supposed to be scrutinizing. Most counseling does not occur face to face, but rather over the phone, and we have heard troubling reports of the development of online counseling.

Although the operative word is "independent," it is concerning that the very people that are supposed to be protecting a vulnerable population are actually receiving payment from those they are supposed to be protecting them from. This is also used as marketing ploy where the salesman uses the fact that a "HUD counselor" will make sure everything is on the up and up, when this may be one of the furthest things from the truth. In fact, in one company commercial, they state that reverse mortgages are in fact an important government benefit that you should take advantage of.

Finally, I have concerns about referral relationships between lenders, agents and annuity sales, as you can see in just two of the documents that we have brought to the hearing today. Clearly, annuity sales have become part of the pitch by some agents selling reverse mortgages. All you have to do is look at this advertisement for agents: "Join our winning team and receive these benefits." You notice, it says "We will teach you. Learn how our producers use annuities to double their commissions by providing their clients a guaranteed monthly income they can't outlive."

The other document, "What is the bottom line? A loan officer in our program earns an average of $5,000-plus when you include the product sale of life, annuity or LTC." Clearly, this is a troubling development in this program and one that we must act to prevent. As the Chairman said, it is wildly inappropriate to be selling an annuity to an elderly person combined with a reverse mortgage. I don't know how these people could look themselves in the mirror because the fundamentals of the financial reality of that transaction is terribly unfair to the elderly person who is being duped by people anxious to double their commissions.

I want to emphasize that this is not a hearing to condemn reverse mortgages. They are a valuable tool to many seniors and we have made a great effort to make sure we bring a company to this hearing to talk about reputable practices that provide this important financial tool to seniors appropriately. But clearly, there is trouble on the horizon. This is a growth industry. There is big money to be made, with very little risk to the people who are making the money. The American taxpayer is in fact at risk and the elderly people that this Committee wants to protect.

I want to thank again all of the witnesses who are here, and ask Senator Martinez, would you like to make an opening statement?

OPENING STATEMENT OF SENATOR MEL MARTINEZ

Senator MARTINEZ. I surely would. Thank you very much.

Thank you, Mr. Chairman and Ranking Member Smith.

Good morning to all of you. I believe it is important that we discuss this important issue of reverse mortgages. They are unique financial instruments that have really exploded in popularity over the last many years. Although they have been around since the 1970's, they are really little understood by the general public.

I hope that we can use today's hearing to shine some light on the reverse mortgages and the positive effect that they can have on our aging population. According to the American Housing Survey, nearly 25 million American homeowners have no mortgage debt, and more than 12.5 million of them are 65 or order. For many elderly homeowners, the equity in their homes represents their largest assets.

Reverse mortgages offer unique financial flexibility for America's fast-growing aging population. While traditionally reverse mortgages have been used to provide for the most basic living expenses such as food, medicine or home repairs, today's retirement-age population is seeking more creative financial planning tools to help guide them through their golden years I would like to welcome all of the witnesses today, but especially Meg Burns from the Department of Housing and Urban Development. HUD facilitates the largest reverse mortgage program through the Federal Housing Administration. FHA's Home Equity Conversion Mortgage program is an industry leader, accounting for 90 percent of all reverse mortgages. FHA has run an exemplary program that provides a safe and sound product option for consumers, as well as a model for the private market.

I understand that there have been instances of predatory practices involving reverse mortgage products, and I have absolutely no tolerance for the unscrupulous actions of individual companies. However, we should keep in mind that this is a valuable tool, and just because some have abused it doesn't mean that it is not something worth doing.

The ongoing subprime crisis has shed light upon the fact that many consumers entered into complex financial arrangements that they did not fully understand. It is important to recognize that consumers are only able to make sound decisions when armed with good information. Instead of limiting financial options, we should ensure transparency, availability, and accuracy of financial information.

Earlier this year, the Banking Committee reported an FHA modernization bill that addresses the Home Equity Conversion Mortgage program. We are seeking to make positive changes that will enhance product availability, lower fees and costs going forward, and help us to better understand the evolving financial needs of seniors. I am proud of this bipartisan legislation and I hope that the Senate is able to act upon it even before we leave for the upcoming holidays.

Reverse mortgage programs are an important tool used by many of my constituents. In fact, in the last fiscal year alone, Florida witnesses a 116 percent increase in the number of HECM loans. As these products continue to increase in popularity, Congress has a responsibility to ensure that our elderly are properly protected, but still given every opportunity to make the personal financial decisions that are right for them.

I look forward to the testimony from the witnesses and thank the Chairman for holding this important hearing.

Senator MCCASKILL. Thank you, Senator Martinez.

Senator Salazar, do you have an opening statement?

OPENING STATEMENT OF SENATOR KEN SALAZAR

Senator SALAZAR. I do.

Thank you very much, Senator McCaskill, for chairing this hearing on reverse mortgages. I want to thank Chairman Kohl and Ranking Member Smith for their leadership on this Committee and for giving us time to address this important issue.

Several of our seniors rely on these products as a safety net. The monthly payments help to supplement their income and cover the costs of unexpected circumstances such as medical expenses. We all, I think, are familiar with circumstances where that has occurred.

The Department of Housing and Urban Development has provided reverse mortgages through its Home Equity Conversion Mortgage program. To be eligible under that program, you must be 62 years of age or older, own the property, occupy the property as a primary residence, and participate in consumer information counseling. The timing of this hearing is perfect. With the 20-year anniversary of the program fast approaching, it is critical to examine the growth of reverse mortgages, identify gaps in consumer protection, and address predatory practices related to reverse mortgages that effectively strip seniors of their home equity.

I am concerned about recent reports that show that many seniors are being heavily targeted to purchase reverse mortgages even though it may not be in their best interest. At the very minimum, elder Americans should have access to quality housing counseling services for advice and information. Additionally, we must ensure that there are adequate protections in place to help seniors avoid bad actors in the market.

I want to just conclude by making a comment about some efforts that are not too distant in my mind. That is, as attorney general of Colorado a few years ago, I started a program that was called AARP Elder Watch. It was a joint effort with AARP to try to make sure that we were protecting seniors from financial exploitation. Financial exploitation comes in many ways and many forms, but it tends to target our senior population because there are unscrupulous actors out there who know that seniors have assets and that seniors, for a number of different reasons, may be more vulnerable than others.

I think it is important for all of us who care about our families, who care about elder Americans, who are watchful about the incoming growth in the baby boomer population, that we get ahead of this issue. While we allow reverse mortgages to continue as a useful tool, as some of my colleagues have addressed, that we also stand up for a value which I think is not only an American value, but a human value that is priceless and timeless, and that is respecting our elders.

I grew up in an environment where if you lifted your hand against an elder, your hand was going to fall off. Of if you spoke in a way that was disrespectful to your elders, your tongue was going to fall out of your mouth. That was tough. [Laughter.]

I think when we talk about making sure that we are protecting our elders against the predatory practices that may occur with reverse mortgages, what we are really talking about is upholding one of the most fundamental values that make us the human beings that we are.

So I thank you again, Chairman Kohl and Senator Smith and Senator McCaskill, for shedding a spotlight on this issue.

Senator MCCASKILL. Senator Smith, would you want to introduce our first witness?

Senator SMITH. Yes, thank you.

Meg Burns is with us today. She is director of the Federal Housing Administration's Single Family Program Development. She is with, obviously, the Department of Housing and Urban Development, to discuss the growing reverse mortgage market and areas in which the Federal Government can properly monitor the overall increase in federally insured home equity conversion mortgages.

Margaret Burns, take it away.

STATEMENT OF MARGARET BURNS, DIRECTOR, FHA SINGLE FAMILY PROGRAM DEVELOPMENT, US DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, WASHINGTON, DC

Ms. BURNS. Thank you.

Chairman Kohl, Ranking Member Smith, and distinguished members of the Committee, thank you for the opportunity to testify on the Federal Housing Administration's Home Equity Conversation Mortgage program.

I also want to thank Senator Martinez for his leadership on the FHA modernization bill, which would lift the cap on the number of reverse mortgages that FHA can insure.

FHA's reverse mortgage program reflects the very best of FHA. Launched in 1989, HECMs were designed to be an innovative new mortgage product, a product that would allow seniors to tap into their home equity in a safe and affordable manner, and a product that would serve as a model for the private sector. As Secretary Jackson and Commissioner Montgomery have noted many times, the FHA was established to operate in exactly this manner, supporting and complementing the private sector with products that meet a public purpose.

HECMs continue to be at the forefront of the reverse mortgage industry, representing approximately 90 percent of the business today. The FHA HECM is less expensive than other reverse mortgage products, provides higher cash proceeds to borrowers, and offers unique consumer protections. All seniors contemplating a HECM receive counseling from a qualified HECM counselor to ensure they understand the product's complexities and costs, and are aware of alternatives to a HECM before making a financial commitment.

Further, FHA's HECM program is extremely flexible, offering seniors five payment plan options that permit the borrowers to draw funds on a monthly basis, in a single lump sum, through a line of credit that can tap funds as needed, or through a combination of these methods. Seniors can easily change payment plans at any point in time.

Additionally, because HECMs are non-recourse loans, when the borrower's heirs sell the house, they will not owe more than the value of the property, even if the local real estate market has declined and the loan balance is greater than the home's appraised value. If, however, the property's value has increased, the heirs will inherit the full amount of the appreciation above the loan balance. Neither the lender nor FHA will receive a share of that equity.

Further, FHA regulates the lenders who participate in FHA's reverse mortgage program. Lenders who originate and underwrite HECMs must meet basic net worth and audit requirements that demonstrate their capacity to operate in a safe and sound manner. Before a lender can close its first five HECM loans, FHA carefully reviews each loan package in its entirety, re-underwriting the mortgage to verify that the lender understands and complies with all of FHA's guidelines.

As a result of conscientious oversight, the FHA program has helped close to 400,000 seniors live more comfortably in their retirement years. Over the last 4 years, HECM volume has increased steadily from 37,000 loans in 2004 to 107,000 loans in 2007. The marked success of FHA's HECM has demonstrated the value of the product and the private sector is now ready to carry it to the next level. Consumers are now in a position to benefit from the improved efficiency, lower pricing, and innovation that results from the type of growth and expansion that is finally beginning to occur in the reverse mortgage market.

In spite of the program's success, we at FHA recognize there are areas for improvement. We have worked with the industry, including the National Reverse Mortgage Lenders Association and the AARP Foundation to address some areas of concern. For example, we are working together to reduce the transaction costs and to improve the availability of quality counseling across the nation. Over the last year, we have been assessing the up-front fees such as the origination charge and the mortgage insurance premium to determine whether any costs can be eliminated or reconfigured to make the product more affordable and appealing to consumers.

On the counseling side, AARP has played an instrumental role training HECM counselors and providing them with tools and information to improve their efficiency and effectiveness. In addition, FHA has been conducting its own training for lenders and counselors nationwide. Last year alone, we performed 68 HECM-specific training sessions reaching almost 25,000 lenders and counselors.

The recent trends indicate this product will only continue to grow, and we at FHA want to do everything we can to ensure that reverse mortgages are used wisely. Educated consumers, ethical lenders and experienced counselors are all critical to this program's success, and we support any efforts to achieve these goals.

In closing, all of us at FHA appreciate the bipartisan congressional interest in the HECM program and thank you for the opportunity to testify. Meeting the housing needs of seniors is a critical mission that requires focus and dedication. I look forward to your questions.

Senator MCCASKILL. Thank you, Ms. Burns. We will have questions now. We are going to try to do 5 minutes. If we can come close to that, that would be great.

Let me start out by asking you, what is required for a counselor to be able to give counseling? What does FHA require them to do?

Ms. BURNS. Right. We have requirements for HUD-approved counseling agencies nationwide. They must be nonprofit organizations. They must be independent, objective organizations, separate and apart from lending institutions, for example. They must have one-year experience providing counseling services in the area in which they are seeking HUD approval to provide those services. For HECM specifically, we require them to have some additional training.

We have a regulation that is in the works that will make this requirement enforceable. This spring the regulation should be published. So this spring, all HECM counselors will have to be trained and will be tested. They will have to pass an exam to provide HECM counseling services, and they will have to follow a specific protocol to provide counseling services. So they will have to follow a set of instructions that leads them through all of the topics that must be covered.

Senator MCCASKILL. But right now, I could be hired to be a counselor by one of these agencies, and I could be counseling someone tomorrow legally with literally no requirement of any kind of training or oversight by FHA. Is that correct?

Ms. BURNS. The way the program works today, the HUD-approved agencies who have approval and have one year experience could hire a new counselor who could provide services immediately. It is true that the regulation will come out in the spring that will dictate that these counselors must be tested.

Senator MCCASKILL. This is dicey, this part.

Ms. BURNS. Right.

Senator MCCASKILL. We are calling them, and by the way they are marketed as independent HUD counselors. Right now at this moment, they have no requirement of any training whatsoever, the individual counselors. It is unclear where the money is coming from, to these people who are getting the counseling. I think they think that you are paying for it, but in reality in many of these instances the lending institutions are paying these agencies, aren't they?

Ms. BURNS. That is correct. The funding is severely inadequate. You mentioned earlier that $3 million has been devoted to HECM counseling services. With a limited pot of $40 million in total, HUD struggles to provide counseling services across the board. We have to provide foreclosure prevention counseling, pre-purchase counseling, rental counseling to people who are evicted.

Senator MCCASKILL. There is no question you don't have enough money to do the job. By the way, though, we are marketing these loans and telling people, and giving them the sense that these are in fact somehow HUD-trained or HUD-certified, and that somehow HUD, the government, is in fact giving their blessing to whatever advice this counselor is giving. In reality, the people they are supposed to be independent of are actually paying their salaries.

Ms. BURNS. Well, while it is true that the lenders make contributions to the counseling organizations, the organizations are themselves independent. We do go out and monitor all these organizations. When we approve them to participate in our program, we make sure that they are separate entities. If we hear a complaint, we will go out and immediately investigate. We will remove the approval status from organizations if we have a consistent—.

Senator MCCASKILL. How often have you done that?

Ms. BURNS. I don't have the stats in front of me, but I can assure you that we absolutely have done that.

Senator MCCASKILL. I think that would be something that we would want to have for the record. How many times has FHA taken action against a counseling agency as a result of this?

Isn't it true that a convicted felon can be one of these counselors right now?

Ms. BURNS. We don't have a requirement that somebody do a screening for——

Senator MCCASKILL. There is no background check required?

Ms. BURNS [continuing.] For previous——

Senator MCCASKILL. Someone could be convicted in a con scheme in a retirement community down in Florida and they could walk in and get hired as a counselor. The agency would be paid by the lender and be telling people the next day a reverse mortgage is a great thing for you—and by the way, I have also got an annuity I want to sell you. Is that an absolute possible scenario under the current regulation and oversight?

Ms. BURNS. They couldn't also sell them an annuity, but it is true that they could—we do not do a background——

Senator MCCASKILL. How do you explain this marketing then—that they are telling agents you can double your commission if you sell an annuity at the same time.

Ms. BURNS. Wasn't that mortgage brokers, not counselors?

Senator MCCASKILL. I am talking about that the people that are selling these are allowed to sell both at the same time. HUD does not prohibit that?

Ms. BURNS. No, we do not permit mortgage brokers or counseling organizations to be employed with another company that also is engaged in a real estate-related activity. We do not permit that. We would absolutely remove the approved status of either a lender, a broker or a counseling agency that was engaged in both activities.

Senator MCCASKILL. So if their marketing people—come be one of these brokers, so that you can make $5,000 per sale by selling a reverse mortgage and an annuity at the same time, that is prohibited?

Ms. BURNS. That is absolutely prohibited. If I knew the companies——

Senator MCCASKILL. We can provide you that.

Ms. BURNS. Yes, that would be——

Senator MCCASKILL. By the way, this wasn't hard to find. We have more examples. We have a number of examples of this, where people are being told to come join these companies and sell both. How many administrative actions has FHA taken against brokers for this kind of activity—selling annuities and reverse mortgages at the same time?

Ms. BURNS. I don't actually know the numbers, but I do know——

Senator MCCASKILL. Would it surprise you if it was none?

Ms. BURNS. No. I know for sure that we have been engaged in some monitoring and enforcement activities over organizations.

Senator MCCASKILL. That is something I think it is really important for us to know, if there has been any enforcement, if there is any sense out there in the community that you are going to be held accountable for these kinds of practices.

Senator Smith.

Oh, excuse me. I am sorry. Senator Carper has joined us.

OPENING STATEMENT OF SENATOR THOMAS CARPER

Senator CARPER. Thanks, Senator McCaskill.

We are joined this morning by a bunch of students. It is standing room only. They are a part of the delegation that is here from the Charter School of Wilmington, 1 of 17 charter schools that we have in our State. We have some wonderful public schools, traditional public schools, and we have a number of excellent charter schools. This is a school that was started about 12 years ago when I was Governor. It is a math-science academy.

Last week's issue of US News and World Report listed the top 100 public high schools in America, and Charter School of Wilmington was number 41. There are 18,000 public high schools in America and these young people, their school is in the top 50. So we are very proud of them.

Today, they are being led down here by the president of the Young Democrats Club. They have Young Democrats and Young Republicans. If one of these kids looks a little bit like me it is because he is my youngest son. [Laughter.]

Senator MCCASKILL. Now I know why you get to talk about this school for so long. [Laughter.]

Senator CARPER. That is right. We are just real happy that they are here. They are going to be meeting with some of our senators here shortly, so they are here a few minutes as part of Capitol Hill 101 to get a sense of what we do here. I just want to say a special welcome to them and thank you for letting them join us for a few minutes. Thank you.

Senator MCCASKILL. Welcome to all of you.

Senator Smith.

Senator SMITH. Let me join in welcoming them as well. Thank you, Senator Carper, for bringing them here.

Meg, obviously, the whole point of this hearing is to, I think we all agree that reverse mortgages are a legitimate product and they can do an awful lot of good. But I think because it is such a growing category, we are very anxious that government do its part to make sure that there aren't unscrupulous players in it.

Obviously, with the bubble popping on the subprime mortgages, there is going to be a lot of brokers out there who may well be looking for a job, and may be attracted to a growth category. Some of them may be entirely appropriate to participate in this, but I wonder if, following on Senator McCaskill's point, if there is sufficient screening to make sure that what happened in subprime doesn't happen in reverse mortgages.

I know they are different products, but I do think that what we are all saying is that the quality of the standard that brokers meet needs to go up, and our citizens be protected. Are you aware of any flow into this market from the subprime brokers?

Ms. BURNS. We actually have not seen that to date, but I am very glad you asked me that question because one of the things that you will note with the FHA product in general is that we actually haven't had that problem because we do have standards for brokers. Normally, the states regulate the brokers, but for FHA-specific lending, we have our own set of requirements. As a result, we have not seen the kinds of problems that you have seen in the subprime market today. We are very proud of that.

On the HECM side specifically, we for the last 2 years have engaged in extensive monitoring of HECM lenders specifically, and we have done it in part with an educational approach to that monitoring. We went out and we saw what was happening, and we said this is where you are doing something wrong.

Now we are going back out and we are imposing what our monitors would call remedies. In cases where we find a problem, where we find a deficiency, we are going to be imposing remedies. So we actually are very conscious that this is our growth product and that we want to make sure that lenders do it right.

Senator SMITH. Great, great. You probably heard in my opening statement that I do support raising or eliminating the Federal cap on reverse mortgages. Obviously, that needs to be done in tandem with proper procedure and oversight. I wonder if, in your view, we do eliminate this cap, what that means to HUD? What steps will you take to guard against what will likely be a tremendous additional escalation in these? Because the cap was reached earlier this year, so——

Ms. BURNS. Right. Right. Exactly. Well, we believe actually that elimination of the cap will really help the product. One of the problems with having a cap on a program is that lenders really can't devote the resources and invest in the infrastructure the way they might if they thought there was no cap. They can't devote the money to the human resources or their systems.

So we think that once that cap is lifted, the lenders will devote the resources necessary to their infrastructure that will improve the efficiency of the product, that will lower the cost of the product, and it actually will help us overall create a better product for consumers.

Senator SMITH. Good. You are aware that in 2000, Congress enacted legislation in which HUD is required to waive up-front costs, providing the proceeds to go toward long-term care. Since the law was enacted, it is my understanding—correct me if I am wrong—that HUD has not followed through with implementing a policy to waive these costs. Is that correct?

Ms. BURNS. That is correct. We went through the motions. We published an advance notice of proposed rulemaking and we published a proposed rule. Based on the public comments, which were very negative, and lots of discussion with organizations like the AARP Foundation, we determined it was not in the consumer's best interest to implement that piece of legislation. That is correct.

Senator SMITH. Very good. Thank you.

Senator MCCASKILL. Senator Kohl.

The CHAIRMAN. Ms. Burns, do you think that the recent dramatic increase in reverse mortgages is a good thing? Do you think we ought to continue with that? Do you think we ought to try to put some brakes on that? What is your judgment?

Ms. BURNS. I do think it is a good thing. I think one of the confusions about the dramatic increase is that relative to the forward mortgage market, it actually is still a very, very small presence. So in 2006, there were approximately 14 million forward mortgages made. In 2006, we had less than 100,000 reverse mortgages made.

So even though the number is growing exponentially, it is growing exponentially because the base is so small. So this growth actually has been steady and gradual relative to the base. I think it is a good thing because I do believe it is a good product for seniors. I think, as all of you have mentioned today, used wisely, this makes a big difference in seniors' lives. Even the AARP report points out that 90-something percent of the seniors who took out a reverse mortgage were very satisfied. It helped them live more comfortably, and that is really our goal here.

The CHAIRMAN. In light of the recent expansion in reverse mortgages that are guaranteed by HUD, many of us are concerned about the increased financial risk as a result to taxpayers. What safeguards has HUD put in place to protect taxpayer liability, especially in this declining real estate market?

Ms. BURNS. Yes, I am so glad you asked me that question. Senator McCaskill mentioned it, and I wanted to respond.

We as a mortgage insurance company do risk analysis on a regular basis. We absolutely do it on an annual basis. We need to make sure that the premium income that is generated from the borrowers covers potential losses. We do projections every year looking at the projected conditions in the market. So we recognize that the real estate market is not doing well, and that the values of homes are dropping. We do an annual assessment to determine what that mean for our portfolio of loans. How much premium income do we need coming in to cover potential losses?

We will do this kind of analysis for the entire portfolio. So we look at the loans that are already on the books. So we will never be in a position where as a mortgage insurance company that premium income can't cover those potential losses. That is our sole function, frankly, as a mortgage insurance company.

So I am glad you asked the question. We would never put the taxpayer in a position of actually paying for this type of service. We would make underwriting changes. We would make programmatic changes. We would do whatever it took to make sure that the insurance funds themselves were always solvent and able to support the business.

The CHAIRMAN. Thank you.

Senator MCCASKILL. Thank you, Mr. Chairman.

I want to thank you, Ms. Burns, for being here this morning.

Oh, I am sorry. I forgot Senator Martinez. Sorry.

Senator MARTINEZ. Thank you.

Let me just proceed on that same question of the potential liability to the government. The FHA HECM program has operated for how many years?

Ms. BURNS. Approximately 20 years.

Senator MARTINEZ. During that 20-year period, has there ever been a period of time where it was not actuarially sound?

Ms. BURNS. No.

Senator MARTINEZ. In other words, that premiums charged were always in excess of any losses that occurred?

Ms. BURNS. Yes.

Senator MARTINEZ. During that 20-year period of history, that is a little longer timeframe than the recent housing bubble, if you would call it that, and there have been periods of housing market downturns and devaluations along the way, have there not?

Ms. BURNS. Yes.

Senator MARTINEZ. The whole FHA program, which began in 1934, has in its entirety always operated in the black. Correct?

Ms. BURNS. Absolutely.

Senator MARTINEZ. It has always been an insurance program that has helped in fact some 34 million Americans either get into homeownership or, in these instances, somehow utilize mortgage products to the benefit of their financial lives. In all of that time, the FHA has never lost a dime.

Ms. BURNS. Exactly.

Senator MARTINEZ. Has always operated financially actuarially sound by collecting premiums in excess of losses or potential losses.

Ms. BURNS. Correct.

Senator MARTINEZ. Now, in order for us to improve the product and create a situation where the premium might be lower and the costs might be lower, you mentioned that you were hoping to reduce the transactional cost, as well as the premium cost. In order to reduce the premium cost, you believe that raising the limit or the cap on the product would enable you to lower the premium costs. Is that correct?

Ms. BURNS. Well, to tell you the truth, we do a cash-flow analysis that looks at not just the premium income generated in any given book of business, but potential losses for the loans that are already on the books. So it is a sort of very comprehensive holistic look at the books of business. We are not considering lowering the premium just as a result of increasing the loan limit.

Senator MARTINEZ. OK. It is an ongoing process.

Ms. BURNS. The origination fee actually is what I think people have been talking about lowering as a result of the increase.

Senator MARTINEZ. What would be the——

Ms. BURNS. The origination fee is what the lender is charging, and would be lowered as a result of the loan limit. For us, the mortgage insurance premium, we are looking in part at reconfiguring it so that there is a lower up-front premium so it reduces those up-front costs to the borrower.

Senator MARTINEZ. But in any event, you are not a profit-making entity. In other words, your premium costs are as low as you need to make them to remain actuarially sound.

Ms. BURNS. Right. Our goal is to be profit-neutral, to just collect enough to cover the losses. Exactly.

Senator MARTINEZ. Would you explain to the Committee the limits that you have on loan-to-value ratios and why those are important?

Ms. BURNS. Yes, that is an excellent question. Under the HECM program, the determination of how much equity can be drawn out of the home is a proportion of the value of the home. It is based on the borrower's age. The highest LTV, for lack of a better term—we don't normally use that term really with reverse—but the highest LTV for a reverse mortgage today is for a 95-year-old borrower. The most they could draw out would be 85 percent of the value of the property. So that is a very big cushion between the amount of the loan and the value of the property, which again is another protective measure for FHA, who would pay in the event of a shortfall—the difference between the loan balance and the value of the property.

Senator MARTINEZ. Thank you very much.

Ms. BURNS. Thank you.

Senator MCCASKILL. If I could ask one follow-up question on the risk. Is there another program within FHA where you have to not only consider the value of the property in terms of the analysis of how the debt is collateralized, but also the life expectancy on people? Isn't the risk to HUD much greater for those loans that are being written for people ages 62 to 65 than, say, the loans that are being written for people that are later in their lives?

Ms. BURNS. Interestingly enough, we have found that the loans to the younger borrowers are terminating faster than we would have expected based on life expectancy rates. So that is a great question. The risk actually isn't as high as we had originally predicted. Again, as a mortgage insurance company, we really do use those actuarial tables and try to figure out how long we think these loans will stay on the books. For the younger borrowers, they were terminating at a much faster rate, within 7 years.

Senator MCCASKILL. They are dying?

Ms. BURNS. They were dying or they were moving from the home, moving to another home or moving to assisted living, moving out. Yes.

But the calculation of the original principal limit is based on the borrower's age, so the highest LTV is for the oldest borrowers. The younger borrowers would have a lower LTV, so the amount of equity they could draw is much smaller so that as it grows over time, you are getting closer and closer to that value. But it starts out much lower. Again, risk protection measures a big cushion between the value of the property and the actual amount of the loan.

Senator MCCASKILL. Are you familiar with the CRS report that talks about the risk to the government in terms of the actuarial tables of life expectancy?

Ms. BURNS. No. I am not familiar with it.

Senator MCCASKILL. I would love for you to take a look at that and then give a written response to the Committee as to how you would refute some of the things that they found in their research that ended up convincing some of the researchers there that there was in fact real risk, particularly for those reverse mortgages that are being written for the younger population within the allowable age limits.

Ms. BURNS. OK. I would love to do that.

Senator MCCASKILL. Does anybody else have a follow-up? Sure.

Senator MARTINEZ. Just one more question. You mentioned earlier about a 100,000 figure, and I couldn't quite understand. You meant that there were 100,000 HECM loans or all the reverse mortgages?

Ms. BURNS. Oh, in 2006, the last set of figures I had for forward mortgages was 2006, so in 2006, there were 14 million forward mortgages that were originated. There were approximately 100,000 reverse.

Senator MARTINEZ. Our of 14 million total mortgage loans, 100,000 were reverse mortgages?

Ms. BURNS. Reverse, right.

Senator MARTINEZ. The totality of reverse, not just HECM?

Ms. BURNS. Right, exactly. I added the figures together.

Senator MARTINEZ. So we are talking about 100,000-mortgage world, if you will.

Ms. BURNS. Yes, exactly. I just wanted to put it in perspective. We always say——

Senator MARTINEZ. If the cap were raised as the FHA modernization bill proposes, do you have any projections of what that number would go to?

Ms. BURNS. We do have projections, although I don't have them here with me. We could certainly follow up with you.

Senator MARTINEZ. Would you mind doing that? That would be great. Thank you.

Senator MCCASKILL. Any other follow-up questions for Ms. Burns?

Senator MARTINEZ. Thank you, Madam Chair.

Senator MCCASKILL. Thank you so much for being here today. We appreciate it.

Ms. BURNS. Thank you.

[The prepared statement of Ms. Burns follows:]

STATEMENT OF MEG BURNS

Director, FHA Single Family Program Development
U.S. Department of Housing and Urban Development

Hearing before the Special Committee on Aging
United States Senate

"Reverse Mortgages: Polishing not Tarnishing the Golden Years"

December 12, 2007

Chairman Kohl, Ranking Member Smith, and distinguished members of the Committee, thank you for the opportunity to testify on the Federal Housing Administration's Home Equity Conversion Mortgage (HECM) program.

FHA's reverse mortgage program reflects the very best of FHA. Launched in 1989, HECMs were designed to be an innovative new mortgage product, a product that would allow seniors to tap into their home equity in a safe and affordable manner, and a product that would serve as a model for the private sector. As Secretary Jackson and Commissioner Montgomery have noted many times, the FHA was established to operate in exactly this manner – supporting and complementing the private sector with products that meet a public purpose.

HECMs continue to be at the forefront of the reverse mortgage industry, representing approximately 90 percent of the business today. The product is less expensive than other reverse mortgage products, provides higher cash proceeds to borrowers, and offers unique consumer protections.

All seniors contemplating a HECM receive counseling from a qualified HECM counselor to ensure they understand the product's complexities and costs and are aware of alternatives to a HECM before making a financial commitment. Further, FHA's HECM program is extremely flexible, offering seniors five payment plan options that permit the borrowers to draw funds on a monthly basis, in a single lump sum, through a line of credit that lets them tap funds as needed, or through a combination of these methods. Seniors can easily change payment plans at any point in time. Additionally, because HECMs are non-recourse loans, when the borrower's heirs sell the property, they will not owe more than the value of the property, even if the local real estate market has declined and the loan balance is greater than the home's appraised value. If, however, the property's value has increased, the heirs will inherit the full amount of that appreciation; neither the lender nor FHA will receive a share of that equity.

In addition, the FHA regulates the lenders who participate in FHA's reverse mortgage program. Lenders who originate and underwrite HECMs must meet basic net worth and audit requirements that demonstrate their capacity to operate in a safe and sound manner. Further, before a lender can close its first five HECM loans, FHA carefully reviews each loan package in its entirety, re-underwriting the mortgage to verify that the lender understands and complies with all of FHA's guidelines.

As a result of conscientious oversight, the FHA program has helped close to 400,000 seniors live more comfortably in their Golden Years. Over the last four years, HECM volume has increased steadily, from 37,000 loans in 2004 to 107,000 in 2007. The marked success of FHA's HECM has resulted in the entrance of a number of private-sector, non-insured reverse mortgage products into the market. FHA demonstrated the value of the product and the private sector is ready to carry it to the next level. Consumers are now in a position to benefit from the improved efficiency, low pricing, and innovation that results from the type of growth and expansion that is finally beginning to occur in the reverse mortgage market.

Given the program's growth and the level of confidence the lending and investing communities now have with the product, the Administration has requested a number of appropriate programmatic changes, all incorporated into the FHA Modernization bills passed by the House (H.R. 1852) and pending in the Senate (S. 2338).

Both bills propose elimination of the program's volume cap, which was originally established in 1989, when the program was being piloted. Such a cap is no longer appropriate or necessary, now that the program has been tested for 18 years and has proven to be a real success story – a model for the entire industry.

Both bills also propose to increase the loan limits for HECMs to a single national loan limit, set at the conforming limit. Currently, the HECM program is tied to the FHA 203(b) loan limits, which have the effect of limiting the home equity seniors can tap. For example, for an elderly couple living in a $500,000 home located in Jefferson County, Missouri, near St. Louis, the calculation of the principal limit for a HECM loan is based on the current FHA loan limit of $213,750. A HECM borrower will not be able to access more than a portion of this amount, regardless of the value of the home.

Finally, both bills are also proposing to expand the program to permit seniors to purchase a home with a HECM. The existing program permits seniors to take out a HECM loan only for the home in which they are currently living. A HECM is not an option for seniors who are interested in selling the family home, which may be too big to maintain or too difficult for less-mobile seniors to navigate, to move to a senior community where senior services are readily available. Today, these seniors must purchase a new home and then take out a HECM in two distinct mortgage transactions with two distinct sets of costs.

Passage of an FHA Modernization bill would permit FHA to offer a HECM product to purchase a home and tap into the home equity with a reverse mortgage in a single transaction. This statutory change would help seniors move to housing better suited to meet their needs and would help free up housing stock for young families seeking homeownership opportunities.

In spite of the program's success, we at FHA recognize there are areas for improvement. We have worked with the industry – including the National Reverse Mortgage Lenders Association (NRMLA) and the American Association of Retired Persons (AARP) Foundation – to address some areas of concern. For example, we are working together to reduce the transaction costs and to improve the availability of quality counseling across the nation. Over the last year, we have been assessing the upfront fees, such as the origination charge and the mortgage insurance premium, to determine whether any costs can be eliminated or reconfigured to make the product more affordable and appealing to consumers while maintaining actuarial soundness of the premium. On the counseling side, AARP has played a critical programmatic role, training HECM counselors and providing them with tools and information to improve their efficiency and effectiveness.

I have one last comment on HECMs: we at FHA are trying to change the public perception about this product. While HECMs have often been viewed as a means for "house-rich, but cash-poor" seniors to meet their most basic living expenses, we are trying to move the public away from that perception and toward a recognition that this program could be utilized as a financial planning tool – as a way to help seniors move into their golden years with a sensible and clear strategy for funding household and personal expenses.

HECMs can benefit many homeowners over the age of 62 who have adequate home equity, even if it's simply enough to pay off an existing forward mortgage. In other words, depending on a senior's financial circumstances, a minimal amount of cash drawn from the home may still be very beneficial; eliminating a monthly mortgage payment may be all a homeowner is seeking. For example, 65-year old Mary Jones still owes $30,000 on her $100,000 home. A HECM would permit her to eliminate her $400 monthly mortgage payment, making it possible to cover her basic living expenses with her Social Security benefits and pension income.

Some seniors are looking for a specific amount of money to cover the costs of home repair or to cover ongoing medical expenses. My point is simply that the program has the potential to benefit seniors with a wide variety of financial needs and, as such, should be thoughtfully considered by all seniors making financial planning decisions.

In closing, all of us at FHA appreciate the bipartisan congressional interest in the HECM program and thank you for the opportunity to testify on the program. Meeting the housing needs of seniors is a critical mission that requires focus and dedication.

I look forward to your questions.

Senator McCASKILL. We will take this opportunity to welcome our second panel. We want to thank all of you for being here today. Let me briefly introduce our panel, and then we will ask you to make your presentations and look forward to an opportunity to ask questions.

Our first witness, Prescott Cole, is a senior attorney at the California Advocates for Nursing Home Reform, where he has been working for the past 13 years. He received his bachelor's degree in broadcast communication arts from San Francisco State University and his law degree from JFK University. He is a member of the California Bar Association.

Our second witness is Carol Anthony, who grew up in Salinas, CA and graduated from Fresno State College with a degree in speech therapy. After graduation, she kept herself busy raising her family and being involved in the family farm and cattle ranch. After her two sons graduated from Cal Poly San Luis Obispo, she returned to teaching. She currently teaches a special education class for children with severe delays of language, hearing impairment and autism for the Monterey County Office of Education.

Our next witness is Don Redfoot. He has worked for 12 years as a strategic policy advisor in AARP's Public Policy Institute. He conducts and supervises public policy research on domestic and international issues related to assisted living, long-term care options, and reverse mortgages. He earned his PhD in sociology from Rutgers in 1981, a master's in social sciences from the University of Chicago, and a bachelor's in sociology from Westminster College in Pennsylvania.

Our fourth witness is George Lopez. He is vice president of James B. Nutter and Company, a mortgage company, where he has worked since 1988. He is responsible for the reverse mortgage compliance and State licensing at his company. He received his bachelor's degree in communication studies and political science from—I regret to inform the hearing—the University of Kansas. Big problem. [Laughter.]

It is a good thing he works for a fine Kansas City company, or we would have to penalize you even further for your unfortunate association with the land of Jayhawks.

But we welcome all of you here today, and look forward to your testimony.

Mr. Cole.

STATEMENT OF PRESCOTT COLE, SENIOR STAFF ATTORNEY, CALIFORNIA ADVOCATES FOR NURSING HOME REFORM, ON BEHALF OF COALITION TO END ELDER FINANCIAL ABUSE, SAN FRANCISCO, CA

Mr. COLE. Thank you, Senator McCaskill.

Senator McCaskill and Committee members, I am Prescott Cole. On behalf of CEASE, a national Coalition to End Elder Financial Abuse, I would like to express our appreciation for this opportunity to testify about some of the problems we are encountering in the emerging reverse mortgage market, and request your consideration of the recommendations we bring forth.

While reverse mortgages and certain annuity products may be advantageous for some seniors in certain circumstances, they are inappropriate in others. Our concern today is about the seniors who are being pressured by unscrupulous sales people whose only goal is to sell products—products that are generally inappropriate for seniors and sold under false pretenses and through fear tactics.

In this testimony, I will cover three specific reverse mortgage problem areas: first, the problem of reverse mortgages being used to finance deferred annuities; second, problems in reverse mortgage counseling; and third, CEASE's concern with the impact of the Deficit Reduction Act of 2005 on low-wealth seniors.

The first problem, insurance agents in the reverse mortgage market. CEASE has major concerns about unscrupulous sales agents promoting reverse mortgages in order to generate funding for annuities. It is irresponsible and it is an economic absurdity to use a reverse mortgage loan to finance a deferred annuity. Reverse mortgages are very expensive loans, they have to be because the lender doesn't get anything back until the elder has died or moved out of the house.

A deferred annuity will tie up a senior's assets for years or sometimes for the rest of the senior's life. The deferred annuity will never generate enough interest to offset the money that is owed on a reverse mortgage loan. We are now seeing insurance brokers actively recruiting insurance agents to promote reverse mortgage senior seminars. Some brokers are even offering to help insurance agents become HUD-certified counselors. These brokers are telling insurance agents that it is ethical to advise seniors to remove tens of thousands of dollars from their home equity in order to buy annuities.

We are now seeing insurance agents who used to be putting on living trust seminars switching over to doing reverse mortgage seminars. These are the same agents who have been using misleading titles and designations to pass themselves off as financial experts or as trusted advisors. These insurance agents like to play on the senior's fears of going in to nursing homes or outliving their assets.

A typical deceptive technique is to say to the senior, "Seniors have a 50 percent chance of going into a nursing home and the average stay is 2½ years." This is a very frightening statement and is also a very false statement. But fear is the greatest sales tool, and fear is what is driving the deferred annuity market.

The second problem—reverse mortgage counseling. There is a misconception about the adequacy of reverse mortgage counseling.

Counseling really isn't about working with a senior to determine whether or not the reverse mortgage is actually something suitable for the senior. Reverse mortgage counseling is really only about making sure that the senior understands the terms of the loan contract. This is counseling in name only and we think that it is inadequate.

Our third area of concern is about reverse mortgages and the Deficit Reduction Act. One of the greatest impacts of the DRA was the treatment of the Medicaid Recipient's home. The DRA emphasizes reverse mortgages as a means to qualify for Medicaid. This is an unwarranted commercial endorsement for reverse mortgages. Having language in a Federal statute wrongfully encourages elders to encumber their homes with progressively expensive and unnecessary loans.

In addition, the DRA's treatment of the home has given insurance agents a powerful sales hammer that they can use to promote their products. The DRA puts the insurance agent in a position where they can say, "I am going to help protect you and your house from the Federal Government."

Our recommendations: first, to prohibit the predatory practice of using reverse mortgage funds to finance deferred annuities; second, require reverse mortgage counseling to include a suitability criteria; and third, to remove references to reverse mortgages from the Deficit Reduction Act.

In closing, simply stated, home equity is the senior's nest egg and we need to do all that we can to preserve it.

Thank you very much.

[The prepared statement of Mr. Cole follows:]

CEASE **Coalition to End Elder Financial Abuse**

AAIA
American Association for International Aging
505.875.0875

CANHR
California Advocates for Nursing Home Reform
www.canhr.org

NAPSA
National Adult Protective Services Association
www.apsnetwork.org

WISER
Women's Institute for a Secure Retirement
www.wiserwomen.org

December 12, 2007

The Honorable Senator Claire McCaskill, Chair
Senate Special Committee on Aging
Dirksen Senate Office Building, Room 628
United States Senate
Washington, D.C. 20510

Dear Senator McCaskill and Committee Members:

On behalf of CEASE, a national Coalition to End Elder Financial Abuse, I would like to express our appreciation for this opportunity to testify on some of the problems we are encountering in the emerging reverse mortgage market and request your consideration of the recommendations we put forth.

About the Coalition

The Coalition is composed of the American Association for International Aging, the California Advocates for Nursing Home Reform (CANHR), the National Adult Protective Services Association (NAPSA), and Women's Institute for a Secure Retirement (WISER). CANHR has 25 years of experience in elder abuse issues; is the sponsor of groundbreaking legislation on consumer protections and elder abuse; and received the California Attorney General's 2005 Distinguished Service Award for Elder Abuse Prevention by a Community-Based Organization. NAPSA is the national coordinating organization for state Adult Protective Service Agencies, the front line professionals preventing and protecting elder abuse. WISER is a nationally recognized leader in developing and disseminating information on a wide range of financial issues for women. The American Association for International Aging (AAIA) is a key networking and research organization in aging and long-term care circles.

Our concern today is to represent seniors who are being pressured by unscrupulous financial salespeople whose only goal is to sell products-products that are generally inappropriate for seniors and sold under false pretenses. These seniors are not receiving information about what may be suitable for their particular needs. While reverse mortgages and certain annuity products may be advantageous for some seniors in certain circumstances, they are very complicated and should be purchased with careful consideration.

In this testimony, I will cover three specific reverse mortgage problem areas. First, CEASE is concerned with the impact of the Deficit Reduction Act of 2005 on low wealth seniors; second, the problem of reverse mortgages being used to finance deferred annuities, and third; the problem of ineffective reverse mortgage counseling.

1. Reverse Mortgages and the Deficit Reductions Act – Deceptive Advice

On January 8, 2006 President Bush signed into law the Deficit Reduction Act of 2005, or DRA. This Act dramatically changed many of the rules for qualifying for long-term care Medicaid benefits. One of the greatest impacts was the treatment of the prospective beneficiary's home. The DRA limits the level of equity an individual can have in his or her home and still qualify for Medicaid. The DRA specifically suggests that seniors take out reverse mortgages in order to deplete their excess home equity. It is a form of unwarranted commercial endorsement for reverse mortgages. Having this language in a federal law is unprecedented, and wrongfully encourages elders to encumber their homes with progressively expensive and unnecessary loans.

Encouraging Elder Financial Abuse

Section 6014 of the DRA tells seniors to reduce the equity level in their homes by using a reverse mortgage if they want to qualify for Medicaid. This statement is deceptive and misleading. In California, there are 3.6 million seniors, according to the Office of Statewide Health Planning and Development less than 11% of seniors who enter nursing homes stay for more than two years. Contrary to the DRA's suggestion that seniors take reverse mortgages to help them qualify for Medicaid, the reality is that most seniors won't be staying in nursing homes long enough to exhaust their equity and therefore, will never qualify for long-term care Medicaid. Because reverse mortgages are generally unsuitable for long-term care estate planning, the federal government should not be recommending them. This recommendation by the federal government has lead to another problem. Financial predators are using the government's endorsement of reverse mortgages as a means to promote unsuitable financial products. Ironically, the DRA is encouraging more elder financial abuse scams:

Reverse Mortgage Trap for Unmarried Seniors

Reverse mortgages are the wrong financial choice for any unmarried senior who may be bound for a nursing home – these are usually older women. Pulling out equity will not always qualify a senior for Medicaid. Equity removed from the home converts to assets that will be used to pay for the senior's stay in a nursing home. As long as the senior has assets that exceed the Medicaid limit, that senior will not qualify for Medicaid.

Once that senior has been in the facility for twelve months, the reverse mortgage loan will be due. Once the loan is due the senior will have to sell the house in order to pay off the lender. After the house is sold, the senior will receive the residue equity and the residue equity will be used to continue paying for the senior's stay in the nursing home.

In all likelihood, the senior will not outlive the residue, and therefore will never get onto the Medicaid program. This means that the whole reverse mortgage exercise was a waste of money. The senior would have been better off financially if she had never taken a reverse mortgage since these products chew up so much of the seniors' equity in interest and fee transaction costs. Seniors and their families need to be informed that it is unlikely that taking a reverse mortgage will ever lead to qualifying for Medicaid.

2. Deferred Annuities and Reverses Mortgages – Unsuitable Products

CEASE has major concerns about unscrupulous sales agents promoting reverse mortgages in order to generate funding to purchase annuity products. We are seeing an increase in sales agents who had been presenting "living trust seminars" now switching to "reverse mortgage seminars". These are the same agents who have perfected the technique of selling annuities by playing on the seniors' fears of going into nursing homes or outliving their assets. The DRA's treatment of the home has given these agents a hook to convince seniors that the government will force them to strip the equity out of their house if they go into nursing homes.

These are the same sales people who use misleading titles and designations to pass themselves off as financial experts or as trusted advisors. These agents are experts at using the seniors' lack of knowledge and fear of the Medicaid Program to double talk the senior into buying deferred annuities.

These sales agents present seminars and tell a room full of seniors that 50% of them will go into a nursing home and their average stay will be two and a half years. This is a false statement. Again, California's Office of

Statewide Health Planning and Development reports that within 90 days after admission, 70% of seniors who go into nursing homes will be discharged either because they go home, are sent to an assisted living facility, or die.

Fear is the financial predator's greatest tool. Misleading seniors or misrepresenting the facts is a way to panic them into purchasing unsuitable financial products such as annuities with funds from reverse mortgages. We have seen an increase in insurance brokers who are now actively seeking agents to promote reverse mortgages. Some brokers are even offering to help insurance agents become HUD certified counselors. They are instructing the insurance agents that they can "ethically" get the senior to pull out home equity in order to buy insurance products.

CEASE believes that it is always inappropriate to use proceeds from home equity to fund deferred annuities. Funds from reverse mortgages are very expensive due to loan fees and insurance requirements.

We provide an example that highlights the shortcomings of using home equity to purchase deferred annuities:

> Imagine a senior taking out a reverse mortgage on her home to finance a $100,000 ten-year deferred annuity. The real question is: What will the cost be for financing the deferred annuity through a reverse mortgage?
>
> Reverse mortgages now cost about 6%. Because of compounding, in ten years at 6% the senior will owe $183,000 on the $100,000 reverse mortgage loan. There will also be an additional $20,000 to $30,000 for the other fees and charges associated with the reverse mortgage loan. In ten years, the senior will have spent about $200,000 to purchase a $100,000 ten year deferred annuity. Ten year deferred annuities are currently only averaging 3%.

It is impossible for a deferred annuity to generate interest that would offset the true costs of the reverse mortgage. Furthermore, the deferred annuity places the senior's assets out of the senior's control for years with substantial penalties and feesfor early withdrawals.

There is no financial justification to use a reverse mortgage to fund a deferred annuity. This predatory practice must be stopped immediately!

3. Reverse Mortgage Counseling - Inadequate & Misleading

There is a misconception about the adequacy of reverse mortgage counseling. Currently, counseling is not focused on helping the senior to understand whether the loan may be a bad deal or totally inappropriate. Reverse mortgage counseling is only required to making sure the senior understands the terms of the loan contract. It is inadequate and "counseling" in name only.

Further, reverse mortgage counseling does not provide assistance with financial decision-making. The counselor does not ask what the senior intends to do with the money, nor do they work with the senior to explore any options to taking a reverse mortgage. Currently, such "counseling" is simply a procedure that must be completed before the senior is given the money.

Face to face "counseling" is not required. "Counseling" can be done over the phone. Sometimes the counselor will be in another state. The Fair Lending Project in Santa Clara, California is working with a client that was phone "counseled" by someone in Florida. The reason the Fair Lending Project happened to be working with this particular client in the first place was because that client had previously gotten into trouble with a series of predatory loans. A phone interviewer has only the briefest contact with the senior and has only a limited ability to assess the senior's ability to understand the gravity of the transaction. The phone counselor never really knows whom they are talking to.

CEASE recommends that the counseling system be expanded to include a suitability component whereby the counselor asks the senior a series of questions to learn why they are taking the loan. Just as it has been determined to be good public policy to have a suitability requirement for financial investors, so should there be a suitability standard set up for reverse mortgage counselors. It is more important for the government to act as a gatekeeper for low wealth seniors than to have the government promoting reverse mortgages. It is extremely important to prevent predatory practices rather than to indirectly encourage flawed financial products and decisions. The reverse "counselors" should be sufficiently qualified and knowledgeable to suggest alternatives; and a counselor should have the authority to recommend disapproving the loan if not satisfied with the responses.

Recommendations:

It is important for policymakers to take steps that will help prevent low wealth senior citizens from losing their home equity to financial predators. We hope that the Senate Special Committee on Aging would adopt the following three recommendations:

1. Remove the language from the Deficit Reduction Act recommending reverse mortgages for seniors.

2. Prohibit the predatory practice of using reverse mortgage equity to fund deferred annuities.

3. Require the reverse mortgage-counseling program to include suitability criteria. Counselors should be able to suggest alternatives to reverse mortgages, and to inquire as to what the senior intends to do with the funds. The suitability criteria should contain a set of inquiries whose responses would lead the counselor to disapprove a loan where appropriate.

Conclusion

Clearly, much needs to be done to protect seniors from financial abuse. The government should be urging caution and not be in the position of promoting the use of inappropriate reverse mortgages. Reverse mortgages are meant to be the seniors' lifeline, not a financial marketer's source of fees. Reverse mortgages are expensive loans and should only be used as a last resort. Where appropriate, counselors should help seniors find more suitable alternatives. Home equity truly is the seniors' nest egg and needs to be protected.
Thank you.

Prescott Cole, Esq.
CEASE, Coalition to End Elder Financial Abuse
(415) 974-5171 or prescott@canhr.org

Senator McCASKILL. Thank you, Mr. Cole, for being here.
Ms. Anthony.

STATEMENT OF CAROL ANTHONY, DAUGHTER OF A RECIPIENT OF A REVERSE MORTGAGE TIED TO AN ANNUITY, KING CITY, CA

Ms. ANTHONY. Senators McCaskill and Ranking Member Smith and members of the Committee, my father John Adcock, was a member of the greatest generation. During World War II, he served proudly with the United States Marines in the South Pacific. When the war was over, he returned to his home town of Salinas, CA, grateful to be able to get a good job and in his own words "marry the prettiest girl in town." Mom and dad built a home, lived their lives modestly, and made sure their daughters were provided the opportunity of higher education.

When Dad died in 2000, he left Mom with a comfortable estate so she would be provided for safely the rest of her life. What he didn't provide, what he never even anticipated, was the need and knowledge to protect her from predatory lenders, con-men, and the new California gold rush, also known as reverse mortgages.

That is why I am here today. In April, 2006, my 80-year-old mother, Betty, was sold a reverse mortgage by Senior Freedom. At the time of the sale, she was in very poor health, frail and not at all capable of entering into or understanding even the simplest financial dealings. Most importantly, Mom didn't need a reverse mortgage. She had substantial money in different accounts and investments, and besides, I had already helped her establish a $150,000 home equity line of credit in case of any unforeseen emergency. The closing costs for the home equity line were zero.

In the 3 years she had access to the credit line, she had only borrowed $19,000. She was paying very, very little per month to service this line. But in April, 2006, a salesman entered the picture, introduced to my mother by her 86-year-old girlfriend, also a widow. The salesman and the lending institution, Financial Freedom, promised the following: there would be no risk of losing her home—but there was; she would receive independent credit counseling—but she didn't; all loan options available to her would be reviewed—but they weren't; she would never be rushed into signing anything she didn't fully understand or was not ready to sign—but she was; she would never be pressured into borrowing or applying for more money than she needed—but she was; she would not be incurring a mortgage—but she did; all loan terms would be carefully explained—but they weren't.

When mom signed on the dotted line, she felt the salesman was her new best friend, but he wasn't. In place of the no-fee home equity line, she now had a reverse mortgage that charged 18 separate closing fees, depleting the equity in her home—the equity that had been saved by my mom and dad one buck at a time over the many years. The 18 closing fees totaled a staggering $16,791. Next, she was forced to make home repairs of about $5,000—repairs that were never mandated by the equity line, but are all too common with Financial Freedom mortgages.

Now, instead of paying interest only on the $19,000 equity line, she received her first statement showing a principle balance of almost $37,000 with interest compounded daily. She would also be charged a monthly finance charged called an "MIP," and another monthly finance charged called a "finance charge." To compound the financial damages, the salesman then converted $125,000 from one of mom's municipal bond funds into a 20-year annuity. The municipal bonds had been paying mom a nice monthly income. Now, she would have to wait until her 100th birthday to see a cent of her money.

Even though the salesman, working for Senior Freedom/Financial Freedom for the reverse mortgage, and Standard Life of Indiana for the annuity, had no real estate or securities license, the harm was done. On the day she signed the loan and the insurance documents, close to $165,000 had been effectively lifted right from her estate.

Should you get involved? I believe the current housing crisis and the explosion of reverse mortgages have some similarities and connections. Both entities have at least insinuated, if not promised, home prices were going to continue to rise at about 4 percent forever. Both sets of lenders have demonstrated they are more than willing to sell loans to people who can't afford them, or to the elderly with home equity lines that don't need them. Lenders are no longer dealing in subprime loans and people without money are unable to qualify for those loans.

So where do you think the thousands of real estate and insurance salesmen and saleswomen are headed? I think to the reverse home mortgages market. It is the new California gold rush coming to your area faster than a California wildfire, thanks to aggressive DVD marketing, featuring such trusted celebrities like James Garner and Robert Wagner. Over 86,000 seniors purchased reverse mortgages just last year. Sales seminars are seeing 10 times the number of participants as they were seeing just a year ago. Financial Freedom is offering careers in what they are calling the "explosive market" of reverse mortgages.

I have a couple of suggestions on how to put a damper on the reverse mortgage market. First, and more important, I think reverse mortgage lenders should compare their product with other conventional home mortgage products—just not Fannie Mae's—such as what my mother had, the home equity line of credit. This one act would reduce the future number of reverse mortgages and all of the problems associated with them. The current system of letting the lending institutions provide their own sales pitches and calling it "independent credit counseling" should be stopped.

Second, I think there should be a substantially reduced loan fee system for the elderly for the privilege of tapping into the equity of their own homes. When mom realized what the salesman had done, she became very depressed and all but stopped eating. The rage that I felt seeing her cry and hearing her call herself a fool was very profound. She was lucky. I was able to buy back her house and settle the annuity issue.

But what about the other victims—the aged, the elderly, the members of the greatest generation? They are part of that trusting generation now so susceptible to predators—predators whose only appreciation for them is appreciation of their money. I appreciate these members of the greatest generation and will be forever thankful and in awe of their sacrifices. They put their lives on hold, went to war, and saved the free world. Now, I am asking you to save them.

Thank you very much for hearing my story. I want to say special thanks to my son, Matt Anthony, who chaperoned me all across the United States. My mother wishes you Godspeed in your good work.

Thank you very much.

[The prepared statement of Ms. Anthony follows:]

Statement of Carol Anthony

Before the Senate Special Committee on Aging

December 12, 2007

Senators Kohl and McCaskill, thank you for shining a light on this important issue.

My father, John Adcock, was a member of the greatest generation. During WW2 he served proudly with the United States Marines in the South Pacific. When the war was over, he returned to his home town, Salinas California, Grateful to be able to get a good job and in his words "marry the prettiest girl in town." Mom and Dad built a home, lived their lives modestly *and made sure their 2 daughters were provided the opportunity of higher education.*

When dad died in 2000, he left mom with a comfortable estate so she would be provided for safely the rest of her life.

What he didn't provide, what he never even anticipated, was the need and knowledge to protect her from **Predatory Lenders, Con-Men** and the **"new California Gold Rush"** also known as the reverse mortgage.

That's why I'm here today. In April 2006 my 80 year old mother (Betty) was sold a reverse mortgage. At the time of the sale, she was in poor health, frail and not at al capable of entering or understanding even the simplest financial dealings. And, most importantly, mom didn't need a reverse mortgage. She had substantial money in different accounts and investments and beside, I had already helped her establish a $150,000 home equity line of credit in her name for any unforeseen emergency. The closing cost for the home equity line was zero.

In the 3 years she had access to the credit line, she had only borrowed $19,000. She was paying very little per month to service this line.

But in April 2006, a salesman entered the picture, introduced to my mother by her 86 year old friend (by the way, also a widow). The salesman and the lending institution promised:

- "There would be no risk of losing her home." But there was.
- "She would receive independent credit counseling." But she did not.
- "All loan options available to her would be reviewed". But they were not.
- "She would never be rushed into signing anything she did not fully understand or was not ready to sign." But she was.
- "She would never be pressured into applying for more money than she needed." But she was.
- "She would not be incurring a mortgage." But she did.
- "All loan terms would be carefully explained." But they were not.

When mom signed on the dotted line, she felt the salesman was a good friend. But he was not.

In place of the no fee home equity line, she now had a reverse mortgage that charged 18 closing fees depleting the equity in her home: **The equity that had been saved over the years .... one buck at a time.**

The 18 closing fees totaled a staggering $16,791.23. Next, she was forced to make home repairs of about $5000. Repairs not mandated with the equity line, *but are all to common with financial freedom.* Now, instead of paying interest only on the $19,000 equity line, she received her first statement showing a principle balance of almost $37,000 with interest compounded daily. She would also be charged a monthly finance charge called an **"MIP"** and another monthly finance charge called a **"Finance Charge"** to compound the financial damages, the salesman converted $125,000 from one of mom's municipal bond funds into a 20 year annuity. The municipal bonds had been paying mom a nice monthly income, now, she would have to wait until her 100th birthday to see a cent of her money.

Even though the salesman, working for Senior Financial Freedom (for the reverse mortgage) and Standard Life of Indiana (for the annuity) had no real estate or securities license, the harm was done. On the day she signed the loan and insurance documents, close to $165,000 had been effectively lifted from her estate.

Why Should You Get Involved?

I believe the current housing crisis and the explosion of reverse mortgages have some similarities and connections. Both entities have at least insinuated, if not promised home values would continue to rise at about 4% **forever**. Both sets of lenders have demonstrated they are more than willing to sell loans to people who can't afford them, or to the elderly with home equity lines that don't need them. Lenders are no longer dealing in subprime loans and people without money are unable to qualify for loans.

So where do you think the thousands of real estate and insurance salesmen and women are headed? To the reverse home mortgages market!

It is the new **California Gold Rush** coming to your area faster than a California wild fire. Thanks to aggressive DVD marketing, featuring such trusted celebrities like James Garner and Robert Wagner. Over 86,000 seniors purchased reverse mortgages just last year. Sales seminars are seeing 10 times the number of participant as they were seeing just a year ago. Senior Financial Freedom is offering careers in what they are calling the **explosive market** of reverse mortgages.

I have some suggestions on how to put a damper on the reverse mortgage market.

First make reverse mortgage lenders compare their product with other conventional home mortgage products – such as the home equity line of credit. This one act would reduce the future number of reverse mortgages and the problems associated with them. The current system of letting the lending institutions provide their own sales pitch and calling it "independent credit counseling" should be stopped.

And second, substantially reduce loan fees the elderly must pay for the privilege of tapping into the equity of their own homes.

When mom realized what the salesman had done, she became very depressed and all but stopped eating. The rage that I felt seeing her cry and hearing her call herself a fool was profound. She was lucky, I was able to buy back her house and amicably settle the annuity issue.

But what about the other victims, the aged, the elderly, the members of the greatest generation. They are part of that trusting generation now so susceptible to predators, predators whose only appreciation for the elderly is appreciation of their money. I appreciate these members of the greatest generation and will be forever thankful and in awe of their sacrifices. They put their lives on hold, went to war and saved the free world. Now I am asking you to save them.

Senator McCASKILL. Mr. Redfoot.

STATEMENT OF DONALD REDFOOT, STRATEGIC POLICY ADVISOR, AARP PUBLIC POLICY INSTITUTE, BILLINGS, MT

Mr. REDFOOT. Good morning, Senator McCaskill and Senator Smith, Senator Martinez. Thank you for the opportunity to testify and present information this morning from an AARP report on reverse mortgages that we are releasing today.

This hearing provides the opportunity to take stock of the progress made over 20 years since the enactment of the Home Equity Conversation Mortgage program, or HECM. It is also a time to identify important issues that will affect the future of reverse mortgages for older homeowners.

The HECM program has been a public policy success story in many respects. It created an insurance model to cover the risks of reverse mortgages. It developed flexible payment options for consumers. It established a consumer counseling program. It produced model disclosures for consumers, and it laid the foundation for funding by investors. Moreover, respondents to AARP's survey were largely positive with respect to their experiences of the loan process and in meeting a wide range of needs, at least in the short run.

However, despite recent growth, only 1 percent of older households have ever taken out a reverse mortgage, and public attitudes still reflect a lack of knowledge about and wariness toward such loans. Both borrowers and nonborrowers in AARP's survey report that costs are too high, and 9 percent of borrowers reported that their lenders had recommended purchasing an annuity, long-term care insurance or an investment—uses that are generally not in the consumer's interest.

Additional research is needed about the long-term impact of tapping into home equity on the ability to address needs later in life. Put directly, are some reverse mortgage borrowers trading their lifetime of savings in home equity for short-term consumption in ways that will jeopardize their future financial security and ability to pay for future needs like long-term care services?

If reverse mortgages are to move from a rather exotic niche in the mortgage market to a more mainstream financial option for greater numbers of older homeowners, policymakers, lenders and consumer advocates must work together to lay the foundation for the next generation of reverse mortgage products, services and regulations. Moving from a low-volume, high-cost market to one characterized by higher volume and more competitive pricing will require reducing costs and building consumer confidence.

The recent collapse of the subprime mortgage market provides some sobering lessons on problems that can occur if high fees and inappropriate marketing practices are allowed to continue. The AARP report suggests ways that HUD and the lending industry can reduce costs, improve products to meet diverse needs, strengthen consumer information and protections, and build consumer confidence in reverse mortgages.

AARP has called upon the Senate to pass the FHA modernization bill that is pending, which contains many important changes to the HECM program. This legislation would remove the limit on the number of reverse mortgages that FHA can insure to foster greater competition and lower costs for consumers. The legislation would also reduce origination fees and require HUD to explore lowering mortgage insurance premiums consistent with maintaining the actuarial soundness of the HECM program.

AARP also urges HUD and proprietary lenders to develop new products such as loans with lower loan limits and lower costs for borrowers who only need modest amounts of money. HUD and HHS should also create incentives for State-based demonstrations to lower the costs of reverse mortgages for homeowners who have long-term care needs.

To strengthen consumer information and protection, Congress should provide a sound basis for funding reverse mortgage counseling services and enact provisions to guarantee that such counseling remains independent of any financial interest in closing a loan or selling products to consumers. State and Federal agencies should develop new standards to deal with the marketing of investments, annuities and long-term care insurance to reverse mortgage borrowers.

These changes would lower costs and give consumers greater confidence as reverse mortgages move from a niche product to a more mainstream option for older homeowners.

Thank you, and I look forward to answering any questions.

[The prepared statement of Mr. Redfoot follows:]

AARP℠

STATEMENT

BEFORE THE

SPECIAL COMMITTEE ON AGING

OF THE

UNITED STATES SENATE

ON

"REVERSE MORTGAGES:
POLISHING, NOT TARNISHING, SENIORS' GOLDEN YEARS"

DECEMBER 12, 2007

WITNESS: Donald L. Redfoot, Ph.D.
Strategic Policy Advisor
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Federal Affairs Department

Thank you for the opportunity to testify on reverse mortgages AARP is releasing today in conjunction with this hearing, including data from the first national survey of reverse mortgage shoppers.

It is particularly fitting that the Special Committee on Aging is holding this hearing as we approach the 20th anniversary of the enactment of the federal Home Equity Conversion Mortgage (HECM) insurance program in February 2008. In 1982, this Committee held the first Congressional hearing on reverse mortgages and issued a report calling for the federal mortgage insurance program that was enacted nearly five years later. Today's hearing provides the opportunity to take stock of the progress made in the past 20 years to identify important issues that will affect the future of reverse mortgage options for older homeowners.

Entitled "Reverse Mortgages: Niche Product or Mainstream Solution? Report on the 2006 AARP National Survey of Reverse Mortgage Shoppers," AARP's report provides a comprehensive look at the trends and issues shaping the reverse mortgage industry and consumer experiences with such loans. The rhetorical question in the title summarizes the state of reverse mortgages in the United States today. After many years of very low volume and slow growth, the number of loans insured by the HECM program has increased substantially in recent years – from under 7,000 loans in FY 2000 to over 107,000 loans in FY 2007. Nonetheless, only one percent of older households have taken out a reverse mortgage, and public attitudes reflect a lack of knowledge about and wariness toward such loans.

The report we are releasing today includes the following sources of information:

- *The first ever survey of reverse mortgage shoppers* -- a national telephone survey of 1,509 reverse mortgage counseling recipients, including 1,309 homeowners, 807 of whom had decided to take out a reverse mortgage ("borrowers") and 502 of whom had not taken out a reverse mortgage at the time of the survey ("non-borrowers"). To focus on the needs of homeowners who are likely to have long-term care needs, 200 additional interviews were conducted with representatives of homeowners who had a power of attorney (POA), enabling them to make legal/financial decisions on behalf of a homeowner.
- *An additional national telephone survey* of 1,003 persons age 45 and older, replicating a 1999 survey on consumer awareness of and interest in reverse mortgages.
- *Analyses of U.S. Department of Housing and Urban Development (HUD) data* on characteristics of borrowers, use of loan types, and characteristics of HUD's loan portfolio.
- *Information from unpublished research* on a small Connecticut reverse mortgage program targeted to older homeowners with long-term care needs.

Findings from the Report
The report reaches five conclusions and offers 16 recommendations to deal with emerging issues facing both older homeowners and the reverse mortgage industry.

Conclusion 1: FHA's Home Equity Conversion Mortgage insurance program has successfully created the foundation for the financial infrastructure of the reverse mortgage industry.

The HECM program has been a public policy success story. In the 20 years since it was authorized, the program has proven to be essential in creating the foundation for the reverse mortgage industry. Among the important achievements of FHA's pioneering efforts are:

- an insurance model that pools the risks involved in open-ended loans that do not become due until the homeowner dies, sells the home, or moves permanently;
- flexible payment options that allow consumers to address a variety of needs through monthly payments for a specific term or for the borrower's tenure in the home, a lump sum, a line of credit, or combinations of these approaches;
- a line of credit payment option with a growing availability of loan funds over time that has become a model for the reverse mortgage industry;
- a total annual loan cost (TALC) disclosure that is more complete than the annual percentage rate (APR) disclosure required for other loans;
- mandatory counseling that educates consumers about reverse mortgages and alternative ways to address their needs;
- the backing of the federal government, which has resulted in secondary market funding of these loans, first from Fannie Mae and more recently from Wall Street investors, who are beginning to establish more competitive interest rates; and
- collection and publication of data on loan risks and performance, with the most comprehensive and significant data being published this year on the program's financial performance from its beginnings in 1990 to 2006.

Conclusion 2: Reverse mortgages have enabled older homeowners to address a range of needs and desires with a high level of initial satisfaction.

AARP's survey found that older homeowners were able to address a wide range of needs and desires with reverse mortgages. When borrowers were asked about the main use to which they had put their loan proceeds, the most frequent responses were retiring an existing mortgage (19 percent), home repairs and improvements (18 percent), improving the quality of their lives with extras (14 percent), and paying for everyday expenses (10 percent). 5 percent of borrowers said that addressing health and long-term care needs was the main use for their loans, most frequently to pay for prescription drugs. Borrowers in fair or poor health, especially those for whom a family member was acting with a power of attorney, were much more likely to report using their loans to pay for home care services and home modifications to remain independent.

Though relatively small percentages of borrowers used their loans to make investments or purchase annuities and/or long-term care insurance products, these uses are generally not in the interests of consumers. The involvement of some lenders in marketing such financial products requires more consumer protections, improved consumer education and greater emphasis on ethical marketing practices.

The survey found high levels of initial borrower satisfaction with HECM loans—83 percent reported that their loans had completely or mostly met their financial needs, and 93 percent reported that their reverse mortgages had had a mostly positive effect on their lives. These findings reflect short-term assessments because more than 9 in 10 borrowers had obtained their loans within the past 3 years, so we do not know the long-term satisfaction rate with reverse mortgages. (Indeed, more research is needed in precisely this area.) Consumers reported high levels of satisfaction with reverse mortgage lenders (90 percent satisfied) and counselors (95 percent satisfied), though non-borrowers were four times more likely than borrowers (23 to 6 percent) to report that they were not satisfied with their lender experience.

Conclusion 3: Loan costs are too high.

Consumer concerns about high costs, as reflected in the AARP Survey and other research, most likely represent the single greatest impediment to greater acceptance of reverse mortgages. When asked to identify the main reason they decided against a reverse mortgage, high costs were the leading reason by a 3-to-1 margin over the next most frequently cited main reason—that borrowers decided a reverse mortgage was not necessary given their financial circumstances. Even two-thirds (69 percent) of borrowers deemed the costs high.

To illustrate the costs associated with these loans, during the month in which the AARP Survey was conducted, the total lifetime transaction costs on a fairly typical federally insured HECM reverse mortgage for a borrower age 74 living in a $300,000 home could have been about $30,000—about half of which comes from upfront fees and the other half from ongoing monthly fees over the life of the loan. These cost estimates do not include any loan proceeds to meet the borrower's needs or any interest charges. Origination fees charged by lenders have risen dramatically, with the maximum allowable fee rising 303 percent between 2000 and 2006.

Conclusion 4: Consumer knowledge about and confidence in reverse mortgages is low.

Consumer impressions of and attitudes toward reverse mortgages are still in the formative stages. According to surveys conducted by AARP, consumer awareness among individuals ages 45 and older increased from 51 percent who had heard of reverse mortgages in 1999 to 70 percent in 2007. But the share of respondents who indicated a willingness to consider a reverse mortgage in the future declined from 19 percent to 14 percent. Perhaps more ominous for future growth of the reverse mortgage industry, interest in using a reverse mortgage in the future remained constant between 1999 and 2007 at 10 percent among respondents age 65 and older but declined sharply from 24 percent to 16 percent among respondents age 45–64.

Most consumers admit that they do not know much about these loans, and misunderstandings about reverse mortgages are still common. Data from research cited above indicate that many consumers are still wary of such loans. A 2007 Harris survey found that reverse mortgages ranked last among various mortgage products in terms of respondents' understanding of the product. Only 25 percent said they had favorable impressions of reverse mortgages, compared to 71 percent who reported favorable impressions of fixed-rate forward mortgages.

A small market in its formative stages, like the reverse mortgage market, can be particularly susceptible to bad press and the resulting negative impact on consumer confidence. It is prudent to take steps now to build consumer confidence with measures that improve consumer information and prohibit unethical marketing practices.

Conclusion 5: More research is needed on how consumer uses of reverse mortgages change over the course of their loans as well as on the long-term impact of these loans on their financial well-being.

One consequence of the sampling limitations of the AARP Survey is that the results focus on the short-term experiences of HECM borrowers. Future research should focus on the longer-term effects of having a reverse mortgage, such as changing health and disability needs over time as borrowers encounter age-related disabilities or long-term care needs later in life. Another aspect of the long-term effects of reverse mortgages deserving of future research is the impact of such loans on asset divestiture and the ability to address needs in late life. Put directly, are some reverse mortgage borrowers trading their long-term savings in home equity for short-term consumption in ways that will jeopardize their future financial security and ability to pay for long-term care services?

Future research should also focus on the reasons why the average duration of HECM loans (6 years) is so short in relation to the median remaining life expectancy of the average HECM borrower assumed by HUD, which is 12 years (Szymanoski et al, 2007). Why are these loans being repaid so soon? How do these borrowers and their heirs assess their experiences with these loans? Since over 9 in 10 borrowers in our survey had obtained their loans within the past three years, these are key questions that our survey results cannot answer. The unique qualities of reverse mortgages call for a unique kind of financial literacy as older homeowners explore the best ways to manage this asset in a manner that will address their needs over the remainder of their lives.

Policy Recommendations

The 16 recommendations in the concluding section of the AARP report suggest ways that HUD and the lending industry can reduce costs, improve products to meet diverse needs, strengthen consumer information and protections, and build consumer confidence in reverse mortgages to make them a more mainstream financial instrument for older homeowners.

1. Changes to the HECM Program to Reduce Costs and Build Consumer Confidence

The AARP Survey found that high loan costs are clearly leading some homeowners who might otherwise benefit from reverse mortgages to forgo these loans. Congress and HUD could take several steps to reduce the cost of the program and build consumer confidence in reverse mortgages.

Recommendation 1: Remove the limit on the number of reverse mortgages that FHA can insure to promote higher volume and more competitive pricing. Note that this provision is included in the AARP-supported FHA Modernization Act (H.R. 1852/S. 2338), which has passed the full House and the Senate Banking Committee and awaits action by the full Senate.

Recommendation 2: Establish a single national limit on home values in the HECM program only if *the cap on allowable origination fees is reduced substantially.* This pair of provisions is also included in the FHA Modernization Act.

Recommendation 3: Reduce the mortgage insurance premiums charged to consumers under the HECM program consistent with the actuarial soundness of the program.

Recommendation 4: Develop policies to avoid foreclosing on consumers who run out of funds to pay property taxes and homeowners insurance.

Recommendation 5: Clarify that the HECM non-recourse limit means that borrowers or their estates will never *owe more than the value of the home.*

2. Product Innovations to Reduce Costs and Meet the Growing Diversity of Consumer Needs

Most prospective borrowers are interested in a line of credit, but some do not want or need the full credit lines they are eligible for under the HECM program. They would prefer much smaller credit lines with lower costs but do not have that option. Because "lite" products would involve smaller loan amounts, they would be less costly to consumers because the risk to lenders and the FHA would be lower. Other innovations could include low-cost public reverse mortgages or publicly subsidized loans to meet specific needs such as home repairs, taxes, and long-term care needs.

Recommendation 6: HUD and proprietary reverse mortgage programs should develop reverse mortgages with reduced costs for those who want to borrow small amounts.

Recommendation 7: HUD and proprietary reverse mortgage programs should develop reverse mortgages that permit borrowers to increase their available loan funds in the future without all the costs of a formal refinance.

Recommendation 8: HUD and proprietary reverse mortgage programs should develop "reversible mortgages" that can shift from forward to reverse mortgages as homeowners age and their ability to make mortgage payments decreases.

Recommendation 9: States and localities should initiate low-cost public reverse mortgages to defer payment of property taxes and finance home repairs and modifications for older homeowners.

Recommendation 10: HUD and the U.S. Department of Health and Human Services (HHS) should create incentives for state-based demonstrations to lower the cost of reverse mortgages used to support the independence of older persons with disabilities or long-term care needs.

Recommendation 11: Congress should repeal provisions in the 2000 American Home Ownership and Economic Opportunity Act that authorize forgiving the upfront mortgage insurance premiums on HECM loans whose proceeds are used entirely to pay for long-term care insurance.

3. Improvements to Consumer Counseling and Information

The AARP Survey found that significant percentages of respondents answered "don't know" when asked to assess reverse mortgage costs. Most respondents indicated that they had not received information on alternatives to reverse mortgages. These findings suggest that individuals and entities providing information to prospective borrowers and counseling clients should take more time and care to make certain consumers understand the costs and potential alternatives to meet their needs. As the market grows and the products become more diverse, special efforts will be required to establish and enforce high standards for individual counselors and the information they give consumers. Counselors should serve as an independent source of unbiased information for consumers and should not have conflicts of interest; for example, reverse mortgage lenders or agents marketing investment or insurance products should not be able to provide counseling or decide which counseling agencies they will pay for this service.

Recommendation 12: HUD should improve the kinds of information it gives to consumers to enable them to understand potential alternatives to reverse mortgages.

Recommendation 13: Sufficiently fund reverse mortgage counseling services. One way to do so is by using some of the mortgage insurance premium collected by HUD to fund HECM counseling.

Recommendation 14: Provide earlier and more complete counseling on the "rising debt, falling equity" nature of reverse mortgages as well as the effects of interest rate or home value changes.

4. Improvements in the Marketing Practices of Lenders

A recent newsletter from the National Reverse Mortgage Lenders Association (NRMLA) stated, "As more companies enter the reverse mortgage business, the need for higher educational and ethical standards becomes critically important" (NRMLA, 2007). The following recommendations are designed to elevate the marketing practices used by companies and individuals who originate reverse mortgages, especially related to the marketing of financial products paid for with reverse mortgages that may not be in the interests of consumers.

Recommendation 15: Lenders should participate in education and accreditation programs that promote the ethical marketing of reverse mortgages.

Recommendation 16: State and federal agencies should develop new cost disclosures and suitability standards for reverse mortgages that are used to purchase investments, annuities, and long-term care insurance.

Final Word

The reverse mortgage industry is at a critical juncture in its development. After many years of low volume, the number of HECM loans made in fiscal year 2007 exceeded 100,000 for the first time. The infrastructure of mortgage insurance, originators, servicers, and investors has been developed, and enough performance data have been collected to evaluate the risks associated with such loans over time. In addition, tools have been developed to counsel consumers about reverse mortgages and alternatives. The initial response from consumers who participated in this survey has largely been positive with respect to their experiences with the loan process and in meeting their needs.

However, if reverse mortgages are to move from a rather exotic niche of the mortgage market to a more mainstream financial option for greater numbers of older homeowners, government agencies, lenders, and consumer advocates must work together to lay the foundation of the next generation of reverse mortgage products, services, and regulations. Moving from a low-volume, high-cost market to one characterized by higher volume and more competitive pricing will require reducing costs and building consumer confidence. Recent industry and public policy developments create the conditions for addressing these problems, but the recent collapse of the subprime mortgage market provides some sobering lessons on problems that can occur if high fees and inappropriate marketing practices are allowed to continue.

Senator MCCASKILL. Thank you, Mr. Redfoot.
Mr. Lopez.

STATEMENT OF GEORGE LOPEZ, VICE PRESIDENT, JAMES B. NUTTER AND COMPANY, KANSAS CITY, MO

Mr. LOPEZ. Thank you, Chairman Kohl, Ranking Member Smith, Senators McCaskill and Martinez, and other distinguished members of the Special Committee on Aging, for allowing me the opportunity to speak to you about the most remarkable home loan program with which our firm has ever been associated—the FHA HECM reverse mortgage program.

I am George Lopez, vice president of James B. Nutter and Company, a privately owned national mortgage banking firm headquartered in Kansas City, MO. Founded in 1951, James B. Nutter and Company has a proud home lending tradition dating back to the Truman administration. This year, we celebrated our 50th anniversary of FHA mortgage lending, and it is this FHA pedigree which enabled James B. Nutter and Company to close the first FHA HECM reverse mortgage in the Nation for Ms. Marjorie Mason of Fairway, KS in November, 1989.

Currently, we are the No. 2 wholesale reverse mortgage lender in the Nation, processing over 1,000 transactions each month and serving over 10,000 senior clients and 450 correspondent lenders in 50 states and the District of Columbia.

During the course of these hearings, you will no doubt hear about the phenomenal growth of the reverse mortgage product in the past decade, as well as its projected growth to come. The challenge for lenders like James B. Nutter and Company, as well as this special Committee, is to ensure that we work together to preserve the integrity and purpose of this unique program.

In my remarks today, I will focus on the life-changing impact of a reverse mortgage, the integrity and superior execution of the product, and some modest policy recommendations.

A reverse mortgage allows homeowners over the age of 62 to tap into their home equity and access funds that are tax-free and can be used for any purpose. The reverse mortgage is extremely flexible. Senior clients can obtain their money in a lump-sum at closing or on a monthly basis, establish a line of credit or utilize a combination of these options. Best of all, there are no monthly payments that the senior client has to make to the mortgage company.

There is no doubt that a reverse mortgage can dramatically improve the quality of life of a senior citizen in a variety of ways, and the financial and emotional impacts cannot be overstated. In the past year alone, we have seen reverse mortgages prevent dozens of foreclosures. In many cases, the closing occurred the day or week before the subject property was to be auctioned. The reverse mortgage was the miraculous solution to an otherwise hopeless and tragic situation.

We have seen reverse mortgages enable seniors to pay for costly medical treatments, to avoid entering a nursing home prematurely, or to pay for medical equipment and prescription medications that they could otherwise not afford. We have witnessed hundreds of reverse mortgages that have helped seniors cover the cost of critical home repairs—a growing problem in our senior community.

But most importantly, we have seen reverse mortgages provide peace of mind by giving seniors the ability to fend off the rising tide of higher living expenses. Seniors can thus remain in their homes, self-sufficient and independent, with dignity and peace of mind.

I would like to share a few thoughts about the integrity of the reverse mortgage program, for thankfully, the HECM program was designed by FHA with an eye toward sound lending principles and strong consumer safeguards. It is a potent product combination that many lenders in the forward mortgage world would be wise to imitate. It is safe to say if subprime lenders and Wall Street investors had followed the same formula when designing many of their risky subprime products, we wouldn't be in the mess we are in today.

Most reassuring is the fact that the evils of mortgage fraud and deceptive advertising have not yet crept into the mainstream of the reverse mortgage industry. I am pleased to report that our firm has received no complaints of any kind related to unscrupulous third parties taking advantage of our seniors. Although our guard is up, there are unique consumer protections that inhere in the reverse mortgage product.

Consider first the strong counseling protocols. Before formal application can be made, the senior client must attend mandatory counseling by an FHA-approved third party. Family members are encouraged to participate, which is a vital part of the process. Second, closing costs are heavily regulated. FHA mandates a list of allowable reverse mortgage costs that cannot be modified. There are no markups or junk fees which plague the forward mortgage world.

Third, lenders must be FHA-approved. A qualified lender must meet a sizable net worth requirement and submit annual audited financials. Fly by-night brokers are effectively prevented from entering the market. Finally, fourth, lenders adhere to a strong industry-wide best practices agreement which precludes the funding of third parties—an important check.

In the final analysis, no loan program is perfect, but the strong consumer safeguards built into the FHA reverse mortgage program provide an excellent deterrent to those who would seek to take advantage of our seniors. In our opinion, major changes do not need to be made. However, here are two modest policy recommendations to consider.

First, augment HUD counseling protocols. We recommend that HUD augment existing counseling protocols to include questions that probe more deeply into whether individuals other than the lender have approached the senior client to do a reverse mortgage or purchase an exotic financial product. These additional questions would help smoke out any unsavory actors and would particularly help protect those seniors who are single, widowed or have no family to advise them.

Second, monitor loan closing documents. At closing, senior clients are already required to disclose whether or not they will be using the loan proceeds to purchase an annuity either voluntarily or involuntarily. FHA thus has the means to monitor the situation and, if necessary, formulate an appropriate response.

In conclusion, the Senate Special Committee on Aging is to be commended for bringing all of us together today to discuss these issues, for only through informed discussion and debate can consensus be reached and solutions found.

Thank you again for allowing me to testify, and I would be happy to respond to any questions you may have.

[The prepared statement of Mr. Lopez follows:]

Testimony of

George B. Lopez
Vice President
James B. Nutter & Company

Before the
Special Committee on Aging
United States Senate

"Reverse Mortgages: Polishing, Not Tarnishing The Golden Years"

December 12, 2007

Thank you, Chairman Kohl, Ranking Member Smith, and other distinguished members of the Special Committee on Aging, for allowing me the opportunity to speak to you about the most remarkable home loan program with which our firm has ever been associated—the FHA HECM reverse mortgage program.

I am George Lopez, Vice President of James B. Nutter & Company, a privately owned national mortgage banking firm headquartered in Kansas City, Missouri.

Founded in 1951, James B. Nutter & Company has a proud home lending tradition dating back to the Truman administration. I am pleased to report that this year James B. Nutter & Company celebrated its 50th anniversary of FHA mortgage lending. This well-established FHA lending pedigree enabled our selection to pilot the FHA HECM program in 1988. Subsequently, in November 1989, James B. Nutter & Company closed the first FHA HECM reverse mortgage in the nation for Ms. Marjorie Mason of Fairway, Kansas.

The length of our firm's experience with the reverse mortgage product is exceeded only by the depth of our experience. Currently, James B. Nutter & Company is the #2 wholesale reverse mortgage lender in the nation, processing over 1,000 transactions each month and serving over 10,000 customers and 450 correspondent lenders in 47 states and the District of Columbia. We also originate forward mortgages in 50 states and the District of Columbia.

James B. Nutter & Company has always participated in loan programs that benefit both the borrower and the lender. Despite the large profits that a subprime lending program would have garnered for our firm, we chose not to engage in this deleterious lending practice that has wreaked havoc on the mortgage industry.

During the course of these hearings, you will no doubt hear about the phenomenal growth of the reverse mortgage product in the past decade as well as its projected growth to come. On January 1, 2008, just three weeks from today, the first of America's baby boomers will enter retirement age and effectively usher in a new era of reverse mortgage lending. Millions of baby boomers will soon be able to take advantage of the life-changing benefits of a reverse mortgage.

The challenge for lenders like James B. Nutter & Company as well as this Special Committee is to ensure that we work together to preserve the integrity and purpose of this unique program. For the reverse mortgage product is a very fragile product—it's poorly understood by the media and even less so by many retirees. Misconceptions abound. Even the investor community is now only beginning to comprehend the vast complexities of the reverse mortgage instrument.

There is broad consensus within the mortgage lending industry that the FHA reverse mortgage program has been a resounding success. Thanks to the efforts of FHA, Fannie Mae and the National Reverse Mortgage Lenders Association, the reverse mortgage program is well-positioned to enhance the retirement security of millions of Americans in the years to come.

Nevertheless, it is important to look for ways to protect the program and ensure that no aspect of the program can be corrupted by those who would seek to manipulate our senior citizens for their own gain. Needless to say, any negative publicity about the FHA reverse mortgage program could do incalculable damage.

In my remarks today I will focus on the life-changing impact of a reverse mortgage, the integrity and superior execution of the reverse mortgage product (especially when compared to that of a forward mortgage), and some modest policy recommendations.

The Impact of the FHA Reverse Mortgage Program

To understand the positive effect that a reverse mortgage can have on the life of a senior citizen, one must listen to the voices of those who have already been helped.

In our experience, the abstract concepts of exorbitant health care costs, escalating living expenses and the looming threat of losing one's home are transmuted into a harsh reality that millions of senior citizens face each day. In many instances, the reverse mortgage is literally the only option to which our clients can turn for help. Consider the following advantages of a reverse mortgage:

- <u>Reverse mortgages prevent foreclosures</u>. In the past year alone, our firm has handled reverse mortgage transactions that have prevented dozens of home foreclosures. In many cases, the reverse mortgage closing occurred the day or week before the subject property was to be auctioned. The emotional and financial benefits in this context cannot be overstated. The reverse mortgage was the miraculous solution to an otherwise hopeless and tragic situation.

- <u>Reverse mortgages offset higher medical costs</u>. Our firm has handled many reverse mortgage transactions that have enabled seniors to pay for costly medical treatments, to avoid entering a nursing home prematurely and to pay for medical equipment and/or prescription drug medications that they otherwise could not afford. In one memorable example, a Southern California couple was able to access their home equity to pay for a daughter's organ transplant operation--a procedure that, we have been told, will add years to her life.

- <u>Reverse mortgages help seniors fix their homes</u>. In the past year, our firm has closed hundreds of reverse mortgage loans that have covered the costs of critical home repairs, a common problem plaguing our senior community. Again, these repairs would not otherwise have been made but for the reverse mortgage.

- <u>Reverse mortgages provide peace of mind</u>. Countless reverse mortgage transactions have given seniors the ability to fend off the rising tide of higher living expenses. Whether escalating credit card debt or utility bills, increased property taxes or homeowners insurance premiums, or the loss of income from the death of a loved one, the funds made available from a reverse mortgage address these needs. Reverse mortgages thus provide a unique peace of mind and dignity that every senior citizen deserves.

It's important to note that these are not isolated instances. The examples I've cited take place each and every day. I'm certain that every reverse mortgage lender in America could come before this body and relate similar stories.

The bottom line is this—too many of our seniors who are rapidly approaching retirement age have not saved enough to meet their needs. Even those seniors with a higher equity position and/or higher net worth can enter their retirement years ill-prepared to deal with the financial realities to come. The reverse mortgage program can thus play a vital role in securing a rich and rewarding retirement for seniors of all income brackets.

The Integrity of the FHA HECM Reverse Mortgage Program

Thanks to the efforts of FHA and Fannie Mae, the FHA HECM reverse mortgage program was designed with an eye towards sound lending principles and strong consumer safeguards. It's a potent product combination that many lenders in the forward mortgage world would be wise to imitate. It's safe to say that if subprime lenders and Wall Street investors had followed the same formula when designing many of their risky subprime products, we wouldn't be in the mess we're in today.

Owing in large part to these sound lending principles, the evils of mortgage fraud and deceptive advertising practices have not yet crept into the mainstream of the reverse mortgage industry. In fact, I am happy to report that in the past year our firm has received no complaints of any kind related to unscrupulous 3rd parties taking advantage of our seniors. According to the National Reverse Mortgage Lenders Association, there have been very few reported incidents related to these issues and what complaints they have received were related to the marketing of loan products that were ***not*** reverse mortgages.

Our guard is up, but it's important for this Special Committee to recognize the unique protections that inhere in the reverse mortgage product:

- Strong counseling protocols. Before formal application can be made and the loan process started, the senior client must attend mandatory reverse mortgage counseling by a FHA-approved third party. Not only do these counselors do a good job of educating the senior client about the loan terms and closing costs, but they operate entirely independent of the mortgage lender. There is no fiduciary connection between the two.

- Family members and advisors are encouraged to participate. In the counseling and application process, family members of the senior client are encouraged to participate. In this way, the senior client receives valuable advice from a diversity of sources that have their best interest in mind.

- Closing costs are heavily regulated. Unlike the forward mortgage world in which RESPA allows a lender to charge almost anything, FHA mandates a set list of allowable reverse mortgage closing costs that cannot be modified. In other words, there are no "junk fees" or "mark-ups" which are so prevalent in the forward mortgage world.

- Lenders must be FHA-approved. In order to originate a FHA HECM reverse mortgage, lenders must be FHA-approved. To obtain this approval, a lender must meet a sizeable net worth requirement, agree to submit annual audited financial statements and must not appear on any watch lists. These are but a few of the FHA requirements but the point is clear—not every lender can originate a reverse mortgage and, best of all, the "fly by night" broker is effectively prevented from entering the market.

- Lenders adhere to a strong, industry-wide best practices agreement. Under the auspices of the National Reverse Mortgage Lenders Association, reverse mortgage lenders sign a strict "Code of Ethics & Professional Responsibility" that covers employer-employee standards, loan disclosure, proper execution of the loan application and closing process, privacy standards and acceptable compensation practices.

- Lenders cannot fund third parties. With only a few exceptions, all proceeds from a reverse mortgage go directly to the senior client and not someone else. Exceptions include proceeds used to pay off an existing mortgage balance, to pay for home repairs mandated by the appraiser, to pay the client's property taxes or homeowners insurance, or to satisfy liens encumbering the title to the property.

In the final analysis, no loan program is perfect. But the strong consumer safeguards built into the FHA reverse mortgage program provide an excellent deterrent to those who would seek to take advantage of our seniors. In our opinion, major changes do not need to be made.

Modest Policy Recommendations

I would leave you today with a few reverse mortgage policy recommendations that we feel would enhance an already successful loan program. I would urge members of this Special Committee to consider the following:

- Endorse passage of the FHA Modernization Act. There appears to be widespread bipartisan support for passage of this Act. We feel passage would markedly improve the FHA reverse mortgage program and help a larger percentage of retirees benefit from the lower rates and higher loan proceeds that the FHA HECM affords.

- Augment HUD counseling protocols. We recommend that HUD augment existing counseling protocols to include questions that probe more deeply into whether individuals other than the lender have approached the senior client to do a reverse mortgage—i.e., who these individuals are and if they are marketing any exotic financial products. These additional questions would help "smoke out" any unsavory actors, and would particularly help protect those seniors who are single, widowed or who have no family to advise them.

- Monitor loan closing documents. At closing, senior clients are required to disclose whether or not they will be using the loan proceeds to purchase an annuity either voluntarily or involuntarily. If so, they are required to disclose the name and contact information of the annuity provider as well as the financial details of the product. FHA thus has the means to monitor the situation for potential problems and, if necessary, formulate an appropriate response.

- Educate counselors about new proprietary reverse mortgage products. There are more than 20 relatively new reverse mortgage products currently on the market that contain a plethora of new loan features, new indices and loan terms. The counselors do a remarkable job and the more informed they are, the more effective the counseling.

Conclusion

We owe an enormous debt to the senior citizens of our country. They've raised our families, fought our wars, put a man on the moon, cured diseases and moved us into the Computer Age.

Unfortunately, life has increasingly become more difficult for our seniors. While many of our seniors are living longer and leading more productive lives, their financial resources aren't keeping pace.

Thankfully, policymakers can point to the FHA HECM Reverse Mortgage Program as a viable solution to this alarming trend. The Senate Special Committee on Aging is to be commended for bringing all of us together to discuss these issues today. For only through informed discussion and debate can consensus be reached and solutions found.

Thank you again for allowing me to testify and I would be happy to respond to any questions you may have.

Senator MCCASKILL. Thank you, Mr. Lopez.

Let me start with you, and ask, obviously you think it would be wildly inappropriate for someone who was working on your company's behalf to sell an annuity at the same time that sold a reverse mortgage.

Mr. LOPEZ. Absolutely true. Yes. We don't sell any sort of insurance products, annuities. We are not aligned with financial planners who would sell these products to senior citizens. In listening to Ms. Anthony's testimony, frankly I am outraged, and I am angry to hear stories like that because we service currently about 10,000 senior clients, and news of these practices has not reached our ears yet.

It is safe to say that we would not do business with such a firm that was going to sell us a reverse mortgage, and there would be a lot of things that we could do on the back end, including undoing the HECM loan and reinstating the original loan, to try to repair some of that damage.

The bottom line is this, and that is that the reverse mortgage industry is a fragile industry. It is a poorly understood product, both by the media and retirees and the public at large. Any negative publicity that is generated from one of these incidents can do incalculable damage. I think the overwhelming majority of lenders that are out there don't engage in these types of deleterious practices. I do think that the system is constructed with enough safeguards that the bulk of the problems can be prevented, but we do see areas where fine-tuning can be done to fix these things.

Senator MCCASKILL. The unfortunate reality of our line of work is that a lot of the time we spend is trying to address problems that bad guys do, not good guys. If everyone was a good guy, we would have a lot less work. What we are trying to get to the bottom of here is how do we, without damaging a valuable product to many seniors, how do we provide government with the right resources and oversight to make sure what you talked about in terms of the consumer being educated and the consumer understanding and making sure that we are not cross-pollinating inappropriate financial products with a reverse mortgage. Clearly, that is occurring. Ms. Anthony's testimony is powerful and emotional and it should be.

So what would your recommendations be? I know you said maybe additional protocols. Do you all pay any money to these counseling agencies that are providing the counseling?

Mr. LOPEZ. Typically, the way the counseling works is depending on what city the senior citizen is in, a list is generated off of the HUD Web site of counselors in the area. We are supposed to provide a pretty substantial list of those. We are not to steer the client to any particular one. We are not to fund those or have any sort of fiduciary relationship with those parties on the back end.

So the counseling process, the way it is designed, there is integrity to that process. Counseling is required. I mean, a product of the counseling session is a counseling certificate that has to be executed by the borrower. It has to be a wet signature and the lender is supposed to obtain a copy of that counseling certificate.

So in listening to Ms. Anthony's testimony, that was one of the things that jumped out at me. It does not seem that correct counseling procedures were followed. That means, to answer your question, I do think that we could augment existing counseling protocols to have a series of questions, particularly for those seniors that don't have what I would describe as a safety net of either family members or personal advisors that could help ask the tough questions: Hey mom, dad, how is this money going to be spent? Why do you need this? What are you going to do with the money? Has anybody approached you unrelated to the lender to buy something? That would filter out some of this riff-raff that you are referring to.

Senator MCCASKILL. Well, aren't you surprised at these come-ons for agents that you are going to be able to make a lot more money if you sell an annuity at the same time you sell a reverse mortgage? Does that surprise you?

Mr. LOPEZ. It does. Obviously, you have bad actors out there, and no system is going to be perfect, but there is temptation to sell products like this. I mean, they are taking an incredible risk because they are going to appear on the radar of entities like FHA and wholesale lenders like ours. We can just refuse to buy the loans, and we would if an incident like this came to our attention.

But it also would draw the attention of other regulatory bodies. As reverse mortgage lenders, we are not empowered to determine suitability of annuities and financial products. That is drilled into our heads at an early stage, that we are not supposed to provide tax advice or financial planning advice. But certainly State insurance regulators and the FTC and other entities that regulate this sort of investment activity, they certainly would have a lot more to say about the suitability of these products, which in this case was clearly unwarranted.

Senator MCCASKILL. Well, first I want to make a comment for the record and make sure that you understand that we invited Financial Freedom to testify today. They declined to testify. I know that they are a big player. I know they are one of the largest. One of these documents actually refers to Financial Freedom—"we can close your reverse mortgage with Financial Freedom or Seattle Mortgage, and many of our loans close in less than 30 days." Let me ask you, Ms. Anthony, was there a wet signature on a counseling form for your mother?

Ms. ANTHONY. No, there was not.

Senator MCCASKILL. There was not.

Ms. ANTHONY. There was not.

Senator MCCASKILL. Did she even receive any kind of counseling that you are aware of, even if it did not involve her executing a signature on a document?

Ms. ANTHONY. No, she didn't receive any outside counseling. The counseling she got was from the salesman, and the sales pitch was printed on documents that were clearly using the software, of Financial Freedom Senior Funding trademarked and bar-coded, specifically "printed by Financial Freedom Senior Funding Corporation's Reserve Mortgage Analyzer" copyright 1999–2005.

Senator MCCASKILL. You need to turn on your microphone and lean up, if you would.

Ms. ANTHONY. OK. What didn't you get?

Senator McCASKILL. I think I heard. It was hard for others in the room to hear.

So if she didn't get the counseling, were you able to get the loan reversed because she hadn't received the counseling?

Ms. ANTHONY. No. I wasn't able to get the loan reversed. I simply purchased it back from HUD and from the lending institution. That was the fastest way to stop the bleeding, the every month of all the extra fees. She didn't want it. She had no idea she had even mortgaged her house, and that there were two deeds of trust on it.

I did have some dealings with Financial Freedom. They didn't go very far. It was a time when they were selling their product to another entity that they owned, and they were saying, Senior Freedom became U.S. Financial Mortgage and U.S. Financial mortgage as an "approved correspondent" of Financial Freedom would sell the loan to Financial Freedom. So it was very hard to deal with them at all Financial Freedom put the blame on U.S. Financial mortgage, formerly known as Senior Freedom. It just became a straight sale—find the papers, tell them I wanted to buy the house back for my mother. Even that took about 6 to 9 months.

Senator McCASKILL. So the record is clear, the agent who sold the reverse mortgage was the same agent that sold the annuity? It was the same person?

Ms. ANTHONY. The same person.

Senator McCASKILL. Are you aware if there has been any action taken against that individual for that?

Ms. ANTHONY. There has not been any action, but there is a case pending at Salinas District Attorney's office, but it is pending. No action has been taken.

Senator McCASKILL. Are you aware whether or not the regulatory environment in California and the insurance regulation in the State of California, are you aware of any actions they have taken as it surrounds the case involving your mother?

Ms. ANTHONY. They have taken none, in regards to the reverse mortgage. However, the California Department of Insurance did intervene in the annuity issue.

Senator McCASKILL. The attorney general?

Ms. ANTHONY. No.

Senator McCASKILL. Are you aware of whether FHA and HUD have taken any action toward the lender, any administrative action toward the lender?

Ms. ANTHONY. They have not.

Senator McCASKILL. OK. I assume you didn't find out about this until after the fact?

Ms. ANTHONY. I found out after the fact. My mother became very ill and she thought she was dying. Then she told me, but she was embarrassed and ashamed. It was about 5 months after the fact that she finally told me that she had done something horrible. She couldn't believe what she had done, and she was afraid she was going to die, and that would mean that she would really lose her home, because if you don't die and you have to go to an old folks home or a nursing home, if you are out of your home for over a year, the process can start to sell that home.

Senator McCASKILL. I think that is something we haven't talked about on the record and we need to. If you are in a nursing home and you are there for more than 12 months, and you are no longer living in your home, that triggers in fact an acceleration of the money being due.

Ms. ANTHONY. Yes. That is one thing that really upset me on the DVDs with James Garner, even though I just love James Garner. He is a paid salesperson. But at the beginning of the DVD, it says you cannot lose your home. There is no risk of losing your home with the reverse home mortgage. If you read the disclosures, there are many, many ways you can lose your home.

For instance, if you don't keep it repaired up to their standards, if someone puts a lien against your home, even if it has no merit, that can be something that would trigger you losing your home. If you run out of your equity line, if you get a reverse mortgage when you are 62 and go through too much equity, and find yourself unable to borrow from other sources; if you don't pay your property taxes; if you don't pay your insurance, that is another trigger that can start the sale of your home.

There are very many.

Senator MCCASKILL. Let me ask you, Mr. Redfoot, on the counseling front. The thing that is a curiosity to me, I absolutely understand that there are reputable companies like James B. Nutter that actually are trying very hard to make sure everything is done correctly, and don't want to take advantage of any senior.

On the other hand, I am very troubled at this notion that this counseling is independent because it is clear to me no one is stepping up and saying, "I am paying for it." I can't figure out. It is like almost magic fairy dust is being spread throughout the country, and these counselors are appearing.

Would you explain for the record how these counselors are actually getting paid for the work they are doing? Where is this money coming from?

Mr. REDFOOT. Well, AARP shares your concern, to be sure, because this program has never been adequately funded. So as a result of that, some are getting some HUD funds, but when you have a requirement for counseling, and you don't adequately fund it, then, as you say, the money has to come from somewhere. It is not just fairy dust.

In many cases, that money is coming from lenders today. On the one hand, the lenders are stepping up and paying for that which government is not paying, but that troubles us in terms of the independence of the counseling and it should be troubling to people.

So what we have proposed is we need a more assured financing system. Whether that comes as a portion of the mortgage insurance premium, that is one of the proposals that we have made, or whether it comes from borrower fees to some extent. To give you an example, as Ms. Anthony indicated, the up-front costs of the loan can be as much as $16,000. The cost of the counseling is maybe $150 or $200. It would be the best investment we could make in assuring that people get good information, independent information, rather than relying on a system that has inherent conflicts, potentially.

Senator MCCASKILL. The legislation that we are going to be proposing would in fact propose to pay for it using the MIP, the fee, which we think would be the appropriate way to do this to ensure that we know where the money is coming from to pay counselors and there is not the possibility of—you know, we don't need to worry about whether the good companies would do this.

I know the rules are you can't steer, but frankly the rules are that you are supposed to have counseling, and clearly that did not happen in the case we have heard about today. I know that Ms. Anthony's example is not an isolated example. I don't think it is the mainstream conduct of this industry, but clearly there are people that are taking advantage of this. All you have to do is look at some of the advertising for the agents and see it.

Obviously, there was a great deal of pressure because it is my understanding that in 2005, HUD lifted the requirement for counseling because of the shortage of counselors. Then they reinstated it. There was a rule that was proposed to lift it for awhile, and then it went back in.

Oh, the requirement that you had to do it before your application was lifted. Right. That was because of the shortage of counselors. The requirement wasn't lifted. You had to have it before you applied was changed. Now that has gone back because we have more counselors, and obviously there is a flow of money here somewhere that is going on that we can't really get our hands on as to where this money is flowing from.

At Nutter, do you write a check to these not-for-profits on some kind of global basis to help pay for counseling?

Mr. LOPEZ. Well, you have to remember our primary footprint is a wholesale lending footprint, so we are buying loans from mortgage lenders around the country. They are the ones that are responsible to see that the counseling is being done properly. Within our retail space, no, we don't subsidize that sort of thing. We have a much smaller retail footprint than a wholesale footprint.

I am sure that some lenders probably use counseling services that would provide counseling on a much more timely basis. One of the problems, as you mentioned, not only was there a shortage of funds, there was also a shortage of counselors to keep pace with the growth of the product. So counseling delays were taking weeks and weeks and so forth. The people from FHA could speak to this much more on-point than I can, but the point is that some lenders do engage the services of companies that can help get them counseling a little bit more quickly. But as far as our company's involvement, no.

Senator MCCASKILL. Mr. Redfoot, I know that AARP does a counseling certification program for counselors, and that you are kind of the gold standard. I am correct, am I not, right now that anyone could counsel anyone in America on one of these mortgages without anyone requiring that they receive any training on the details of the instrument.

Mr. REDFOOT. As Ms. Burns explained earlier, the certification goes to the agencies rather than the individuals. So you are correct that in terms of individuals that might be hired, that they would not have the training and would not have the adequate certification. We are working with HUD to try to improve that. We have developed testing mechanisms to test knowledge, worked with them on counseling protocols that they are about to issue that would deal with some of these troubling areas.

Yet as you say, unless you have an adequately funded, adequate numbers, and adequately trained system out there to accommodate this growth, you are going to have a lot of people getting counseling that is inadequate.

Senator MCCASKILL. Is there any prohibition now that you are aware of on gifts? We have a lot of rules around here about who we can take a cup of coffee from. Are there any rules that you are aware of right now as to the relationships, the prohibitions on giving trips or getting gifts or anything of that nature, between the lender and any of these counselors?

Mr. REDFOOT. I might have to defer to Meg Burns from HUD to answer that one.

Senator MCCASKILL. Ms. Burns, is there any prohibition on gifts or gratuities?

Ms. BURNS. There are prohibitions on the relationships between the lenders and the counseling organizations. The lenders can provide lump-sum contributions to counseling organizations. However, they cannot in any way intervene or interfere with the services.

Senator MCCASKILL. Can they give them gifts?

Ms. BURNS. No. Gifts in the form of like a car or a truck? No.

Senator MCCASKILL. Anything?

Ms. BURNS. No, no.

Senator MCCASKILL. Are they expressly prohibited?

Ms. BURNS. I am not exactly sure how our regulation reads on that, but I am sure that there is some language that gets at that issue, and I actually haven't heard of that as even being a problem in the counseling arena. It really is more that the lenders are willing to step up and pay for the counseling services, and that calls into question, is there a conflict of interest.

Senator MCCASKILL. Right.

Ms. BURNS. So, yes.

Senator MCCASKILL. Thank you for going out of turn there. I was interested in getting that on the record. I would like to, if you would, this whole area of the regulation that FHA has I think is important. We will follow up and make sure we get on the record what the specifics are about prohibition of gifts or gratuities or anything of that nature between the lender and the actual counselors.

Mr. Cole, let me ask you this. How difficult is it legally to unravel any of this after it has been done?

Mr. COLE. Well, our experience really comes in around the annuities. It is a very, very difficult process. In California, we do not have a suitability standard for the sale of annuities. That is a big battle and unfortunately we are not making much progress. Some states have adopted a model standard from the NAIC. The problem with the NAIC standards adopted, is insurance agents can actually set up their own suitability standard.

We find when a senior has purchased an annuity, it is virtually impossible to break it without suffering all of the costs. The worst case we have seen is a case where a 92-year-old had purchased a deferred annuity that matures the year 2063. The sum he put in was $650,000. Within 2 years after the purchase, he died, and the relatives who weren't going to wait around until 2063 suffered about $100,000 penalty to get out of that annuity.

We are seeing a two part problem, when seniors are in a reverse mortgage and they are using the money of the reverse mortgage to finance a deferred annuity. First, they have their obligations to the reverse mortgage lender to pay off the loan. As was mentioned, to start a loan, you may have something like $16,000 in fees and costs right out of the box, and then every year there is interest on the loan that is compounding on top of that. Second, if you get into the annuity, then getting out of that annuity becomes a financial train wreck.

What we are finding when seniors get into these situations is that they give up. They will just take their loss and they will accept the 17 percent immediate penalty that they suffer by canceling that annuity, along with any other cost. Seniors don't like to fight. They are from the greatest generation, but their fight is over. They are not going to spend their last 2, 3 or 4 years of their life working their way through some civil litigation.

What we are finding, unfortunately with our situation in California is that the Department of Insurance does not have the resources to go after unsuitable annuity sales. We have 225,000 people who are licensed to sell annuities in California. There is no way that we can keep track of those through our Department of Insurance or our attorney general. We have very few resources to fight every battle. Financial abuse cases are complicated. You get into "who said what—he said, she said". Again, the seniors are not going into that battle.

The agents have extraordinary power. In some instances they are thugs because they win the senior over, and after they do that, they abuse the senior. It is not just about the money. There is power involved. They use fear tactics to cripple the seniors and then they rescue the seniors. They scare them and they say, "Now, I can help you."

This business about the Deficit Reduction Act, it is incredible. The Deficit Reduction Act highlighting reverse mortgages for going into a nursing home is absurd. The Deficit Reduction Act actually has a provision within it, section 6014, that states that if you are married, you don't have to worry about your equity. Well, if you are single going into the nursing home, as Ms. Anthony pointed out, and are in the nursing home for 12 months, that house is going to be sold and the reverse mortgage won't do you any good.

Senator MCCASKILL. Right.

Mr. COLE. I believe also with the HECM loans, you cannot get a reverse mortgage if you don't live in the house. Why are reverse mortgages mentioned in the DRA? Agents are using the DRA to promote their products. I just came across something again Friday—this is something out of Florida—where an individual is offering to make insurance agents "professors of reverse mortgages". Agents are going to go out and talk to viable seniors, get them all worked up, then tell them they have to have a reverse mortgage otherwise the government will strip out their equity.

That is the problem for somebody going to the nursing home.

Senator MCCASKILL. Right.

Mr. COLE. What is the problem for people who are going to stay at home? This is being sold as the pot of gold. This is the vacation they never had. This is everything except the reality that this is the last resource for the low-wealth seniors. Rich people don't get reverse mortgages because it is expensive. Reverse mortgages are very, very expensive loans.

Senator MCCASKILL. Right.

Mr. COLE. Reverse mortgages target low-wealth seniors. When you take a low-wealth senior and invite them to do something capricious its wrong. Loans are being pitched for anything that a senior wants. I had a call from a son-in-law to get money whose mother-in-law, a recent widow, took out a reverse mortgage and put $14,000 into draperies. This is something that is going to come back to haunt her at the end of the game. That reverse mortgage is like a rope. There is only so much equity you can pull out of your house, and after you have reached the end of the rope what is going to happen? Your house is at risk. There are many ways you can to lose your house.

Reverse mortgages have wonderful, wonderful things to offer, but we have to be very, very, very careful. Mr. Lopez had some great recommendations. When I was hearing what he was saying, I was feeling that he was moving toward a suitability standard. You need to have somebody in there to say, "Let's settle down." That person that talked to you about the reverse mortgage—a celebrity? Where will the celebrity be when the seniors finances go overboard?

Senator MCCASKILL. Right.

Mr. COLE. Thank you very much.

Senator MCCASKILL. Yes, absolutely.

I want to thank all of you for being here. I want to reiterate that I think we are supportive of this tool. We want this tool to work. But if we are going to lift the cap, it is incredibly important we fix these problems before we do, because there is money to be made and there will be unscrupulous people that will take advantage.

That is why we have to make sure that you have the resources in government, the FHA has the resources to make sure the counseling is done right, that we are doing suitability, that there is oversight, and there are consequences to this kind of stuff, where people are told you sell them both at the same time, which on its face should offend anyone.

I think the legislation we are proposing will do those things, and at the same time protect this tool for many seniors who need it.

I want to read one of the commercials, the text part of it. This is where I really get nervous. It says his name and what company he is with. "If you are a homeowner aged 62 or over, I have an important message for you. Here is a great government benefit now available. You may qualify to pay off your existing mortgage and access tax-free money from your home to use for whatever you wish without ever having to make a loan payment. With the HUD-regulated, government-insured reverse mortgage, you can convert the equity of your home into financial solutions without ever having to make a monthly payment."

Now, I have to tell you, that sounds really good. If I don't have one of those, I am missing out on something that my government is providing me. Well, that is not what this is. We know that the fact that they are calling it HUD-regulated and we are using that kind of terminology reassures this vulnerable population that we have put our stamp of approval on whatever it is they are being sold. That stamp of approval is precious.

I think we have to make it not just be law that we write, but that we are willing to implement with the resources to allow government to do this right. I think that the testimony from FHA was good this morning, but I think frankly it is obvious they do not have the resources to oversee this and do it right at this point. It is essential that before we grow this program, that we fix this.

I know we have a vote that has been called, so I will have to adjourn the hearing now. I want to welcome any additional testimony that anyone wants to give to the Committee. That includes any of the lenders, any of the advocacy groups, any of individuals that have had the kind of abuses go on like Ms. Anthony's family has. We welcome that to the Committee. Hopefully all of us will come together and support the legislation that will be introduced by myself and Senator Kohl within the coming days.

Thank you very much for being here.

[Whereupon, at 12:17 p.m., the Committee was adjourned.]

Testimony of

Peter H. Bell, President
National Reverse Mortgage Lenders Association

Submitted to
The Special Committee on Aging
U.S. Senate

December 12, 2007

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December 12, 2007

National Reverse Mortgage Lenders Association (NRMLA) is pleased to submit the following written testimony to the Senate Special Committee on Aging. We applaud Sen. McCaskill for organizing this hearing and look forward to assisting in any way possible.

As you know, reverse mortgages enable senior homeowners 62 or older to convert part of the equity in their homes into tax-free cash without having to sell, move, give up title, or take on new monthly mortgage payments. Borrowers are never, under any circumstances, forced to leave their homes providing they make their real estate property tax and insurance payments. Borrowers can choose to receive reverse mortgage funds as a lump sum, fixed monthly payments (for up to life), line of credit, or as a combination of these. No mortgage payments are due during the life of the loan. Borrowers can use the funds anyway they wish. The loan is repaid when the last surviving borrower (in the case of a couple) sells the home or permanently moves out.

The amount of funds a borrower is eligible to receive depends on the person's age (or the age of the youngest spouse on title in the case of couples), the appraised home value, interest rates, and in the case of the FHA-insured Home Equity Conversion Mortgage program, the county lending limit. In general, older borrowers and/or those with more equity accumulated in the home can get more money than younger borrowers and/or those with home encumbered with other debt.

Consumer demand for reverse mortgages has increased dramatically over the past three years. The most widely used reverse mortgage, accounting for an estimated 90 percent of all loans, is the Federal Housing Administration-insured Home Equity Conversion Mortgage, or "HECM." Since its adoption in 1990, FHA (part of the U.S. Department of Housing and Urban Development) has insured 346,212 HECMs. During the most recent federal fiscal year (ending September 30), approximately 107,558 seniors (compared to 76,351 in 2006) obtained HECMs to pay off existing debts, fund health care expenses, pay for modifications to make their homes safer and more comfortable, or simply to create an income stream that provides additional cash and peace of mind.

California is the largest market for FHA-insured reverse mortgages, even though production declined slightly to 17,642 loans in 2007 from 20,320 loans in 2006 due to increased competition from conventional products that offer higher lending limits and lower upfront fees. But in most other parts of the country, FHA volume increased substantially. For example, FHA insured 1,872 reverse mortgages in Missouri (compared to 849 in 2006) and 934 loans in Wisconsin (compared to 473 in 2006).

Consumer Protections

Several factors are fueling this growth. Increased awareness and consumer acceptance of reverse mortgages are two key factors. Our industry receives mostly positive press coverage from major media outlets, including the *Wall Street Journal*, *The New York Times*, *Chicago Tribune*, *LA Times*, CNN, NBC News, and other daily news sources.

Much of the press coverage focuses on the important consumer protections built into the HECM program. Over the past decade, all of the stakeholders in the reverse mortgage business -- AARP, National Council on Aging, counseling organizations, and NRMLA have worked collaboratively to refine our product offerings and enhance consumer protection. We have all worked towards a shared goal of making sure each and every person who applies for a reverse mortgage is adequately protected.

Arguably, the most important consumer protection is mandatory counseling. Before a reverse mortgage application can be processed, the prospective borrower must first meet with an independent counselor. Counseling is required by law under the HECM program and required by industry best practice for all other reverse mortgage products. HUD, in conjunction with AARP, National Foundation for Credit Counseling and Money Management International, oversees a network of counselors whose job is to review the transaction, answer any questions the borrower may have about reverse mortgages and suggest alternative options.

Among HECM's other consumer safeguards are several important features:

- **Standard & Capped Interest Rates.** Interest rates are calculated from one of two indexes, either the 1-year U.S. Treasury Constant Maturity Rate or the London Interbank Offered Rate (LIBOR) depending on the consumer's preference, and priced at a set margin above the index. Historically, interest rates were variable only, but now fixed rate HECMs are becoming available. On variable rate loans, there are caps on interest rate increases.

- **Limitation on Fees.** Origination fees are limited by HUD regulations and may be financed as part of the reverse mortgage. This means a senior incurs very little out-of-pocket expense to get a reverse mortgage HUD currently has an administratively-imposed origination fee limitation and the pending FHA Modernization bills would establish a limit by statute.

- **Advance Disclosure.** The Total Annual Loan Cost, or "TALC" disclosure, required by the Federal Reserve Board, is provided to the prospective reverse mortgage borrower and displays the total transaction costs over the projected life of the loan. This way, a senior is made fully aware of the costs incurred in obtaining the reverse mortgage. If a prospective borrower indicates that an annuity is to be purchased with the reverse mortgage proceeds, that transaction is reflected in the TALC disclosure.

- **No Maturity Date.** A reverse mortgage cannot become due during the homeowner's lifetime. It is a permanent tool. The fact that there are no required payments and there is a lifetime right to occupy the home provides great protection against unforeseen or unanticipated future circumstances, rendering reverse mortgages vastly safer than other loan alternatives.

- **No Prepayment Penalty.** Although the loan is not due and payable until the senior permanently moves out of the home, it can be paid-off at any point prior with no additional fees or costs.

- **No Penalty for Canceling the Loan.** After the loan closes, a senior has up to three days to cancel the transaction, the so-called "right of rescission," for any reason whatsoever.

- **Asset Protection.** The HECM is a "non-recourse" loan. This means that the amount due can never exceed what the home is worth. Title to the home always remains with the borrower. When the loan becomes due, the lender is repaid the sum of funds advanced plus the accrued interest, but never more than the value of the house. If there is remaining value, it belongs to the homeowner or the estate.

- **No Shared Appreciation.** No reverse mortgage product in the marketplace has "equity-sharing" or "shared appreciation" features. In some earlier reverse mortgage products, the senior could obtain more money in exchange for giving up a percentage of the future value of the home. Such products are no longer offered.

All of these protections are required by law, regulation or FHA Mortgagee Letter for the HECM program. All sponsors of proprietary reverse mortgage products have emulated HECMs safeguards and adopted similar protections for all other conventional reverse mortgages.

NRMLA's Code of Conduct

In addition to these protections, NRMLA members subscribe to a Code of Conduct and Best Practices that assures American's demand for reverse mortgages can be fully met by companies committed to standards that emphasize the highest ethical integrity, place fulfilling the clients true needs beyond all else, and have a commitment to the communities they serve.

Standard industry practices include: (1.) informing all borrowers that they have no obligation to purchase any product or service as a condition of getting their reverse mortgage; and (2.) only disbursing funds directly to the borrower(s), with the exception of funds disbursed for required repairs, to settle existing liens on the property, or at the borrower's specific direction. Furthermore, as part of the loan origination process, loan officers inquire if an annuity is being purchased with the loan proceeds. If the prospective borrower answers affirmatively, additional disclosures incorporating costs associated with the annuity are provided with the TALC disclosure.

These factors combined have resulted in a high degree of satisfaction among homeowners who have gotten a reverse mortgage. According to AARP's newly published reverse mortgage study, nine out of ten homeowners said that they were satisfied with their lenders. Another 93 percent of borrowers survey reported that their reverse mortgages had a mostly positive effect on their lives.

Conventional Reverse Mortgages

Historically, three products were available to consumers: FHA HECM, the Fannie Mae Home Keeper, and the Cash Account, a "jumbo" reverse mortgage created by Financial Freedom Senior Funding Corporation, Irvine, CA. One investor, Fannie Mae, purchased all HECMs and Home Keeper loans. With a single investor, consumer choices and product options were limited. For example, interest rates were variable; fixed-rate options were not available. Interest rate margins were the same no matter which lender a consumer chose, restricting the flexibility for lenders to tailor loans to fit consumers' needs.

In recent months, more investors have entered the marketplace, which has led to several new conventional reverse mortgage products being introduced offering fixed interest rate options, higher lending limits and lower upfront fees. The end benefit to consumers is greater choice, lower costs and more flexibility. Newer, more flexible options are also becoming available on the FHA-insured HECM product, which still retains over an 85% market share.

Growth in Reverse Mortgage Participants & Product Innovation

More and more major financial institutions are exploring opportunities in the reverse mortgage market and choosing to enter this business. This increasing competition brings down costs to consumers and provides more product options.

Much creative thinking is beginning to get underway at life insurance companies, banks and other financial services entities. Many are thinking through ways to more effectively convert an asset (home equity) into a stream of income that can cover home upkeep, day-to-day living expenses and long-term care costs. Some of the solutions might utilize combinations of various products, for example, pairing a reverse mortgage with an immediate annuity and/or with home care coverage policy. If such products "dovetail" properly and provide a bona fide benefit to the borrower, there is nothing inherently wrong with the concept.

There have been some annuities sold to reverse mortgage recipients that are ill-advised. Responsible members of the industry and NRMLA stand ready to work with Congress and other reverse mortgage stakeholders to figure out how we can make sure this doesn't happen. Among steps we are exploring are developing industry standards and guidelines for acceptable companion products; or establishing a product review process through which acceptable products can be identified.

We believe that the excellent work that AARP has done in joining with insurance companies to come up with an approved, consumer-friendly annuity product that is sold with the AARP name, provides an example of how an organization can help influence a market to better serve consumers.

It is important to keep in mind, as creative thinking begins to emerge in this sector, that broad-brushed restrictions such as outlawing the purchase of any annuity with a reverse mortgage under any circumstances whatsoever might be overly restrictive and stifle product innovation. Deferred annuities are probably inappropriate for seniors in most situations; although there are some financial planning scenarios in which they might make sense. On the other hand, we have seen examples of single-premium immediate annuities from top-rated insurance companies that can be purchased with HECM proceeds, in which the borrower would receive a higher monthly payment from the annuity than from the HECM – plus the payments would continue after the borrower moves out of the home.

Critical Role of Reverse Mortgages

Today over 34 million Americans are over age 65.[1] This is expected to double in the next 30 years to almost 70 million.[2] By 2030, 20 percent of Americans will be over age 65.[3] Almost four out of five seniors own their own homes, meaning there are about 27 million senior homeowners today, and that number will rise in the future. Seniors of all races have the highest rates of homeownership compared to other age groups.[4]

Even so, seniors have a lower median income than any other demographic group ($23,311 for seniors, and $43,581 for all homeowners nationwide). Yet seniors have the *highest* median home equity ($80,000 for seniors, compared to $57,000 for all homeowners and only $19,000 for homeowners under age 35).[5] This indicates that conversion of home equity into income could significantly increase the relatively low incomes of senior homeowners.

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[1] U.S. Bureau of the Census, Current Population Reports.

[2] Ibid.

[3] Ibid.

[4] "Housing Our Elders: A Report Card on the Housing Conditions and Needs of Older Americans," HUD, November 1999.

[5] The State of the Nation's Housing 2000, Harvard University Joint Center for Housing Studies.

This is important from a public policy perspective. Seniors are a large and growing segment of the population. As seniors age, their incomes do not generally increase, while their needs do. Homes need repairs and accessibility improvements, chronic illnesses require ongoing treatment and expensive prescription drugs, cars wear out and must be replaced with more expensive ones, and people with declining mobility may need more daily help with household tasks. Seniors who cannot afford these growing expenses either forego them—thereby, sacrificing quality of life, independence, and even their health—turn to families, who are often hard pressed to help; take out expensive home equity loans, which must be repaid on a current basis; seek government assistance; or sell their homes in order to access their home equity. Studies by AARP have shown that seniors will sacrifice considerable quality of life in order to remain in their homes for as long as possible.[6]

Reverse mortgages offer an ideal way to avoid these dire consequences while maintaining seniors' desired independence in their own homes.

Reverse Mortgage Alternatives

It's worth noting alternative sources of income available to seniors, particularly home equity loans or trading down to smaller homes.

Home equity loans are often problematic for seniors on fixed incomes because homeowners are obligated to make monthly payments that their cash flow prohibits. In fact, many seniors could not qualify for loans that require current payments because they just do not have the income to qualify. The beauty of the reverse mortgage is that there are no monthly payments. Instead of the homeowner paying the lender, the lender pays the homeowner.

As far as the option of selling and moving is concerned, this can be problematic from both a financial and emotional perspective. It is important to recognize that a home, in many circumstances, is much more than merely an economic asset. I have visited seniors in homes with gardens nurtured for decades, woodshops, art studios, handmade built-in furniture and other irreplaceable features. Whether it is due to the physical attributes of the home, a sense of community, or the numerous memories contained therein, many seniors simply do not want to move.

From a financial perspective, if the costs of selling, including a typical broker's commission (6-7%), closing costs on the new home, and moving expenses (not to mention the inconvenience of packing up 15-55 years of accumulated belongings) are calculated, a reverse mortgage might very well prove to be the more cost-effective solution. Furthermore, it would be quite possible for someone to outlive the "net

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[6] Fixing to Stay, AARP, May 2000.

proceeds" obtained from selling and moving—unless those funds are used to purchase an annuity or some other financial instrument providing lifelong income.

With the reverse mortgage, on the other hand, lifetime income can be guaranteed, as long as the home is occupied, even if the amount provided eventually exceeds the value of the house.

Conclusion

In conclusion, a healthy, active reverse mortgage program could be a key component for helping seniors take control over their financial situation. Reverse mortgages are a promising way to unlock billions of dollars in home equity, providing financial security, independence, and great improvement in the quality of life for thousands of senior homeowners. Wider acceptance of reverse mortgages can mean reducing the need for costly increases in federal spending on health care and other benefits for seniors in the future.

It is important that all stakeholders in the reverse mortgage sector – government, elderly advocates, lenders, insurers and investors – continually work together to advance products options and availability, and assure that proper standards and safeguards are in place. We should not stand in the way of innovation, but we must stand together to make sure that our nations seniors are only offered products that offer true peace of mind and financial security.

We appreciate the opportunity to provide these comments. If you have any questions or would like any additional information, I would be happy to respond.

Respectfully Submitted,
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