Reverse Mortgages: A bright financial spot for boomers

BY GREG FROST | SPECIAL TO NMBW

This year, the leading edge baby boomers turn 62, the magic milestone age when many consider retirement. Many of them bought or refinanced their homes during their peak earning years and have accumulated significant equity.

These homeowners are entering retirement with a large financial asset. Unfortunately, many are still making hefty mortgage payments at a time when their income is actually going down.

To make matters worse, the financial security that baby boomers counted on during their early careers is suspect at best. Corporate retirement programs suffer from mismanagement or unrealistic promises. Social Security is in jeopardy, and no one really expects to live at his or her current lifestyle on the benefit.

Many baby boomers are asking whether they can realistically stay in their homes. Should they refinance to another 30-year loan to reduce the monthly payments? Should they sell the place where the kids and grandkids have come to expect holiday celebrations? Should they buy something smaller or rent an apartment?

At today's prices, would something smaller really be cheaper? Any of these choices terribly lowers the homeowners' standard of living and are dreadful to consider.

There is good news for these leading edge baby boomers. They have also now reached the age where they can qualify for reverse mortgages on their homes. Reverse mortgages — whether taken as a lump sum, a monthly payment or accessed via a home equity line of credit — allow homeowners to access from 50 to 100 percent of their accumulated equity, depending on their age. Homeowners can access this equity and eliminate their mortgage payment, with no income, credit or medical qualifications.

There are some stipulations of course. All owners on the title of the home must be at least 62 and must sign the loan agreement. Single-family residences are most commonly eligible, though some programs accept other types of property, like manufactured houses and condominiums. However, mobile homes and co-ops do not generally qualify. The home must be in good repair. Reverse mortgage proceeds can be used to make home improvements if necessary or desired.

There are no stipulations on what a homeowner can do with the reverse mortgage proceeds, either. Homeowners can finance everyday living expenses, vacations, even the grandkids' tuition, without having a monthly payment as long as they live in the house.

Here's how it works. Let's assume that the $125,000 house that John Doe bought 15 years ago is now worth $220,000. Mr. Doe, who just turned 62, still owes $75,000 on the mortgage, leaving him with $145,000 in accessible equity. Based on his age, Mr. Doe can access $35,000 in equity via a reverse mortgage (half of the appraised value of the home, minus the balance of the current mortgage).

Rather than refinance a mortgage to a new 30-year loan just to lower a monthly payment, Mr. Doe could eliminate the payment entirely by using the equity built up during his lifetime.

Misconceptions about reverse mortgages abound, though. No, the bank doesn't own your house — the homeowner(s) retains title. No, no re-payment is required on the reverse mortgage as long as one surviving borrower remains in the home. No, the loan proceeds are not taxable, no matter how one receives them (lump sum, monthly payment or equity line of credit). No, Social Security or Medicare benefits are not affected by a reverse mortgage.

Your heirs won't be forced to sell your home to pay off the loan, either (though many adult children sell their deceased parents' homes anyway). If the heirs want to keep the home, they can pay off the reverse mortgage balance or refinance the loan into a regular mortgage for themselves.

Another misconception is that the equity in the home decreases by taking a reverse mortgage. On the contrary, very close to the same equity remains in the house, and could even grow slightly. Why? Here's how: Jane Smith is lucky enough to own her home, worth $100,000, free and clear. She takes a $50,000 reverse mortgage with an interest rate of 6 percent. This means roughly $3,000 in interest in the first year. At end of the year, Ms. Smith's reverse mortgage balance increases to $53,000. But her home's market value has appreciated by 3 percent. Now the house is worth $103,000. She owes $53,000. She still has the same $50,000 equity in her home.

Over the past 20 years, home appreciation in the Albuquerque area has well exceeded 3 percent a year, with some neighborhoods appreciating even faster. A homeowner with a reverse mortgage usually can absorb an interest rate as much as twice that of the rate the market value of their home increases and still retain the same equity percentage.

How much better would your life be without a monthly mortgage payment? Could you use a lump sum, monthly income or line of credit that never had to be repaid as long as you lived in your home? Would you go out to dinner more? Travel more? Pay for the rising costs of prescriptions or other medical expenses? Replace the car? Assist the grandkids with college expenses? Update or improve the family homestead? Pay off your credit card debt and reduce your monthly outflow even more? Reverse mortgages are one of the few bright spots for aging boomers in a time when they are getting nothing but bad news from their traditionally expected retirement benefits.

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