Examining Faulty Foundations in Today's Reverse Mortgages

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Introduction

A reverse mortgage is a type of home loan that is available to borrowers 62 years of age or older whose homes are paid for or nearly paid off. A reverse mortgage enables a borrower to obtain income through cash payment or credit lines by tapping the equity in their home.

As a matter of public policy, reverse mortgages should be considered suitable only when a senior has no other viable option. Those considering a reverse mortgage should always consider less costly options first.

As a matter of public policy, reverse mortgages should be considered suitable only when a senior has no other viable option. Those considering a reverse mortgage should always consider less costly options first. Reverse mortgages come with high costs, can expose borrowers to potential abuse and can place non-borrowers who may share the dwelling at risk of displacement when the borrower dies or must leave the home. A 2009 *Consumer Reports*[1] investigation found more cause for concern: Loan bailouts have soared. The annual sum of reverse mortgages taken over by a federal insurance fund has more than quadrupled in four years, from $81.3 million in 2004 to $381.3 million in 2008, according to an analysis of more than 500,000 loans over two decades.[2]

Reverse mortgages are now a permanent part of the nation's financial landscape and the growth potential for this largely untapped market is astounding. The 2009 *Consumer Reports* investigation noted that "retiring baby boomers are turning 65 at the rate of about 10,000 per day. . . [and] by 2010, more than 50 million Americans will be 62 or older, and more than 80 percent own their homes, controlling an estimated $4 trillion in equity."[3]

While the baby boomer demographic has expanded, so has the volume of the most common type of reverse mortgage--Home Equity Conversion Mortgages, known as HECM loans. In fiscal year 2001, 7,781 HECM loans were originated.[4] By the end of fiscal year 2009, the

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[1] *Consumer Reports* is a publication of Consumers Union.

[2] *Reversals of Fortune*, CONSUMER REPORTS, Sep. 2009 ("The Next Financial Fiasco? It Could be Reverse Mortgages"), *available at* http://www.consumerreports.org/cro/magazine-archive/september-2009/personal-finance/reverse-mortgages/overview/reverse-mortgages-ov.htm.

[3] *Reversals of Fortune*, CONSUMER REPORTS, Sep. 2009 ("A Different Kind of Debt"), *available at* http://www.consumerreports.org/cro/magazine-archive/september-2009/personal-finance/reverse-mortgages/a-different-kind-of-debt/reverse-mortgages-different-kind-of-debt.htm.

[4] NAT'L CONSUMER LAW CTR., SUBPRIME REVISITED: HOW REVERSE MORTGAGE LENDERS PUT OLDER HOMEOWNERS' EQUITY AT RISK 4 (2009), *available at* http://www.nclc.org/images/pdf/foreclosure_mortgage/predatory_mortgage_lending/reverse-mortgages-report1009.pdf.

annual volume of HECM loans was 114,656,[5] representing a staggering 1,373 percent increase in loan volume in just eight years.

As for the future growth of the reverse mortgage market, Ginnie Mae, citing figures from the National Reverse Mortgage Lenders Association (NRMLA) wrote, “Some projections call for as much as $37 trillion in senior home value by 2030, from which home equity figures are derived, assuming historical appreciation and taking into account the demographic shift as baby boomers begin to turn 62.”[6] In 2007, the NRMLA noted that there had been “less than a 1% market penetration”[7] which points to huge market opportunities for the purveyors of reverse mortgages.

Examining Faulty Foundations in Today’s Reverse Mortgages is a continuation of Consumers Union’s examination into reverse mortgages and their impact on consumers. In 1999 we first studied the impact of the product on seniors in California, a state with a large potential market for reverse mortgage sales, and produced a report entitled, *There's No Place Like Home: The Implications of Reverse Mortgages on Seniors in California*.[8] At that time, one of our primary conclusions was that for seniors who need additional income, reverse mortgages could be an attractive option or may entail devastating financial hazards. We recommended that state and federal agencies increase their oversight of the reverse mortgage market and enact consumer protections to safeguard borrowers.

Our latest examination into today’s reverse mortgage market is a collaboration between Consumers Union of the U.S., Inc, the nonprofit publisher of *Consumer Reports*,[9] California

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[5] IBM GLOBAL BUSINESS SERVICES, AN ACTUARIAL ANALYSIS OF FHA HOME EQUITY CONVERSION MORTGAGE LOANS IN THE MUTUAL MORTGAGE INSURANCE FUND, FISCAL YEAR 2010 8 (2010) (prepared for Dep’t of Housing and Urb. Dev.), *available at* http://www.hud.gov/offices/hsg/rmra/oe/rpts/actr/2010actr_hecm.pdf.

[6] GINNIE MAE, U.S. DEP’T OF HOUSING AND URB. DEV., BRINGING WALL STREET TO MAIN STREET: 2007 ANNUAL REPORT 9 (2007), *available at* http://www.ginniemae.gov/about/ann_rep/annual_report07.pdf.

[7] Press Release, National Reverse Mortgage Lenders Association, Reverse Mortgage Market Currently at $4.3 Trillion, Less than 1% Penetrated, According to the NRMLA/Hollister Reverse Mortgage Market Index (June 28, 2007),

http://dev.nrmlaonline.org/rms/press.aspx?article_id=557.

[8] VICTORIA WONG & NORMA P. GARCIA, CONSUMERS UNION, THERE’S NO PLACE LIKE HOME: THE IMPLICATIONS OF REVERSE MORTGAGES ON SENIORS IN CALIFORNIA (1999), *available at* http://www.consumersunion.org/pdf/reverse.pdf.

[9] **Consumers Union of United States, Inc.**, publisher of Consumer Reports®, is a nonprofit membership organization chartered in 1936 to provide consumers with information, education, and counsel about goods, services, health and personal finance. Consumers Union’s publications and services have a combined paid circulation of approximately 8.3 million. These publications regularly carry articles on Consumers Union’s own product testing; on health, product safety, and marketplace economics; and on legislative, judicial, and regulatory actions that affect Consumer welfare. Consumers Union’s income is solely derived from the sale of Consumer Reports®, its other publications and services, fees, noncommercial contributions and grants. Consumers Union’s publications and services carry no outside advertising. Consumers Union does not accept donations from corporations or corporate foundations.

Advocates for Nursing Home Reform[10] and Council on Aging Silicon Valley.[11] Together we present our findings to inform the public, policymakers and legislators about reverse mortgages and the current consumer protection concerns for its borrowers.

We found that the use of reverse mortgage loans is exploding as lenders and brokers push them with more urgency while shouldering almost no responsibility for whether the loans are suitable for the borrowers. While the reverse mortgage market continues to grow, there are deep concerns about the suitability of the products for some borrowers, the aggressive marketing and misleading advertising of reverse mortgages to seniors, the susceptibility of vulnerable borrowers to deceptive marketing involving complicated financial products, and the inadequacy of consumer protections to prevent loan abuses that can hurt eligible borrowers.

Compounding our concern, reverse mortgage loan bailouts funded by taxpayer dollars have climbed as a result of lender claims against the Federal Housing Authority (FHA) insurance fund for HECM reverse mortgages.[12] This fund protects lenders who take back homes through foreclosure or a deed in lieu of foreclosure against losses when the borrower's outstanding debt exceeds the equity remaining when the home is sold.[13] As of March 2010 there were as many as 20,631 HECM loans in default and the subject of foreclosure representing a maximum claim amount of more than $3.68 billion.[14]

Recent investigations by the Government Accountability Office (GAO) found potentially misleading statements in reverse mortgage marketing materials produced by 26 entities and at

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[10] Since 1983, **California Advocates for Nursing Home Reform (CANHR)**, a statewide nonprofit 501(c)(3) advocacy organization, has been dedicated to improving the choices, care and quality of life for California's long term care consumers. Through direct advocacy, community education, legislation and litigation it has been CANHR's goal to educate and support long term care consumers and advocates regarding the rights and remedies under the law, and to create a united voice for long term care reform and humane alternatives to institutionalization.

[11] Since 1974, the non-profit **Council on Aging Silicon Valley (COA)** has served as the designated area agency on aging (AAA) for Santa Clara County. COA has contractual relationships with 26 public and non-profit agencies providing a broad spectrum of health and supportive services. In addition to its mandated AAA responsibilities of planning, coordination, and advocacy, COA is a large provider of direct services to older and younger disabled residents in Santa Clara County. One of COA's main missions is to help older adults remain in their chosen homes and communities. The Fair Lending Project for Seniors at COA achieves this goal for many by preventing the loss of homes and equity due to predatory lending practices.

[12] *Reversals of Fortune*, CONSUMER REPORTS, Sep. 2009, *available at* http://www.consumerreports.org/cro/magazine-archive/september-2009/personal-finance/reverse-mortgages/overview/reverse-mortgages-ov.htm?INTKEY=195BME0.

[13] U.S. Dep't of Housing and Urb. Dev., FHA's Home Equity Conversion Mortgage Program, http://www.hud.gov/offices/hsg/sfh/hecm/hecm--df.cfm.

[14] HUD reported a 173 percent increase in "deferred" loans - loans in default because of unpaid taxes or insurance - from March 2009 to March 2010. U.S. DEP'T OF HOUSING AND URB. DEV., AUDIT REPORT: HUD WAS NOT TRACKING ALMOST 13,000 HECM LOANS WITH MAXIMUM CLAIM AMOUNTS OF POTENTIALLY MORE THAN $2.5 BILLION 7 (2010), *available at* http://www.hud.gov/offices/oig/reports/files/ig1060003.pdf.

the same time noted that counseling provided to HECM borrowers was weak.[15] Financial predators abound ready to take advantage of potential borrowers in the exploding reverse market raising law enforcement concerns.[16] These developments signal a clarion call that significant systemic problems are beginning to surface in the reverse mortgage marketplace and that greater consumer protections to prevent abuses are needed.

At the same time, new opportunities have emerged for examining reverse mortgages and the need for increased protection of its borrowers. The recently passed Dodd-Frank Wall Street Reform and Consumer Protection Act[17] mandates a closer examination and potential new regulation of the reverse mortgage industry. This new law establishes the Consumer Financial Protection Bureau (CFPB) which is empowered to issue regulations, orders or guidance to ban abusive practices in reverse mortgages. The CFPB is also charged with examining the reverse mortgage marketplace and publishing a study to inform the creation of future consumer protections.[18]

We propose solutions to close the gaps in consumer protection. Most urgently, we recommend that the newly developing Consumer Financial Protection Bureau and other federal and state regulators consider our findings and include the following reforms in developing strong and comprehensive policies to protect the public against abuses in the reverse mortgage marketplace. These reforms include:

- Requiring lenders and brokers to ensure loans are suitable for borrowers
- Establishing a fiduciary responsibility to the potential borrower
- Outlawing deceptive marketing
- Adopting stronger prohibitions on cross promotions
- Strengthening the quality and content of counseling
- Protecting non-borrowing spouses and tenants

Finally, to assist potential reverse mortgage borrowers, we include a Tip Sheet offering practical advice for consumers considering reverse mortgages.

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[15] GOV'T ACCOUNTABILITY OFFICE, REVERSE MORTGAGES: PRODUCT COMPLEXITY AND CONSUMER PROTECTION ISSUES UNDERSCORE NEEDS FOR IMPROVED CONTROLS OVER COUNSELING FOR BORROWERS 2 (2009), *available at* http://www.gao.gov/new.items/d09606.pdf.

[16] Fed. Bureau of Investigation, Home Equity Conversion (Reverse) Mortgages Exploited to Defraud Senior Citizens, http://www.fbi.gov/scams-safety/fraud/seniors/intelbulletin_reversemortages.

[17] Pub. L. No. 111-203, 124 Stat. 1376 (2010), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h4173enr.txt.pdf.

[18] *Id.* § 1076 ("Reverse Mortgage Study and Regulations").

Reverse Mortgage Basics

I. Uses and Benefits

A reverse mortgage is a loan against the equity a senior has built up in his or her home. The loan is "reversed" because instead of making monthly payments to the lender, the lender advances sums to the senior against the future sale of the home.

To qualify, the borrower must be 62 years or older and have paid off all or most of the mortgage. The amount of money the senior can borrow depends on age, the current interest rate, the appraised value of the home, the amount the senior owes on the home, the amount of fees charged, and, if the loan is federally insured, the federal loan limit, which is currently $625,500.[19] When a potential borrower needing cash has few or other assets to draw upon, a reverse mortgage can be an attractive option if there are no other less expensive alternatives available.

As a general rule, the older the borrower, the higher the property value, and the less the borrower owes on the mortgage (if there is a mortgage), the more money the borrower can receive. Borrowers may receive reverse mortgage payments in the following three ways, or in a combination of the three: 1) a "lump sum" cash advance at closing; 2) monthly cash advances; or 3) a line of credit. If the borrower chooses the monthly cash advance option, it can be either for a fixed period (term) or for as long as the senior resides in the home (tenure).

The loan becomes due upon the death of the borrower, if the borrower permanently leaves the home (defined as 12 consecutive months), or if the borrower fails to maintain the property, pay property taxes or pay homeowners insurance.

Reverse mortgages that are backed by the Federal Housing Agency (FHA) are called Home Equity Conversion Mortgages, or HECMs. Some seniors erroneously believe that the federal insurance makes reverse mortgages “government loans.” However, the federal insurance backing reverse mortgages does not protect the homeowner from foreclosure if he or she defaults due to an inability to maintain the property, pay property taxes, or pay homeowners insurance. It does protect the borrower in the event the lender is unwilling or unable to make payments. Most notably, the insurance protects the lender in case of default or if the loan balance begins to exceed the property value.[20]

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[19] Press Release, U.S. Dep’t of Housing and Urb. Dev., President’s Economic Recovery Package to Make More Families Eligible for FHA-Insured Mortgages (Feb. 26, 2009), http://www.hud.gov/local/id/news/pr2009-02-26.cfm.

[20] U.S. Dep’t of Housing and Urb. Dev., *supra* note 13.

II. Reverse Mortgage Pitfalls

Reverse mortgages aren't for everyone. A reverse mortgage should be a loan of last resort for a senior who needs cash. The right reverse mortgage may be appropriate for some low-income relatively healthy seniors who lack other retirement assets, do not qualify for lower-cost alternatives and cannot meet their current mortgage obligation. A reverse mortgage might also be a reasonable alternative for seniors who are in foreclosure and have no other way to pay off the delinquent amount, do not want to sell the home and downsize to a smaller property or do not wish to move into assisted living in the future.

Reverse mortgage proceeds can be used for any purpose but a borrower should seriously consider which uses are appropriate and which ones should be avoided. Because the proceeds can be used for any purpose some lenders are pitching reverse mortgages as a veritable ticket to the good life. Despite the ability to use reverse mortgage proceeds without restriction, reverse mortgages are not a good idea for seniors who intend to use the loan proceeds to buy a deferred annuity[21] or to pay nursing home costs since the borrower must remain in the home or the loan will come due. A reverse mortgage is also not a good choice if the borrower will move out of the home in three years or less, because of the high up-front costs of the loan. If the borrower has less than approximately $109,560 in assets while a spouse resides in a nursing home, a reverse mortgage is inappropriate because Medicaid may already cover the costs of the spouse in the nursing home, rendering the reverse mortgage either unnecessary or putting Medicaid eligibility in jeopardy.[22] The maximum asset amount may vary and those considering reverse mortgages should ascertain the amount that applies in their state before proceeding with a reverse mortgage.

Reverse mortgages are expensive. The fees and costs are added to the balance of the loan at the outset. For standard HECM loans, FHA charges a single up-front mortgage premium equal to two percent of the home's appraised value or of $625,000, whichever is less. The borrower is also charged a 1.25 percent premium on the entire loan balance. In addition, the borrower is charged a monthly servicing fee of up to $35. For the new "HECM Saver" option available in October 2010, the up-front insurance premium is lowered to .01 percent of the

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[21] An annuity is a contract a person makes with an insurance company in which the insurance company promises to make payments -- now or in the future -- in exchange for the money invested. Annuities can carry fixed or variable rates and be immediate or deferred. A deferred annuity offers tax benefits but delays payment for a set amount of time. This can be very harmful to the senior who needs liquid assets to pay for day-to-day living or caregiver expenses. According to HUD, deferred annuities are "often inappropriate for older borrowers who may not gain any benefit from the investment if they have to wait 10 or 15 years."

U.S. Dep't of Housing and Urb. Dev., Handbook 7610.1 142 (2010), *available at* http://www.hud.gov/offices/adm/hudclips/handbooks/hsgh/7610.1/76101HSGH.pdf.

[22] *See* Ctrs. for Medicare and Medicaid Servs., U.S. Dep't of Health and Human Servs., Spousal Impoverishment, https://www.cms.gov/MedicaidEligibility/09_SpousalImpoverishment.asp.

home's appraised value.[23] Because of the high costs associated with reverse mortgages it would not make sense to take out a loan if a borrower has sufficient income to live on or alternative assets to draw from. For example:

> A widow's world of assets consists of a home, $1,000 in a checking account, and $100,000 locked up in a 12 month certificate of deposit (CD). If she wanted $100,000 cash (for what ever reason) what choices does she have? If she takes out a reverse mortgage she would incur several thousand of dollars in loan origination fees, closing costs, and compounding interest on the loan principal. If instead, she cashed out the twelve month CD she would only be penalized with the loss of three months worth of interest. In today's market, it is likely that any financial losses for cashing in the CD early would be minimal compared to the cost of obtaining a reverse mortgage. Since cashing out a CD leaves the borrower in a superior position, choosing a reverse mortgage to get cash would be the wrong financial move.

This example illustrates that it is essential to always consider less expensive alternatives first before opting for a reverse mortgage.

Reverse mortgage payouts can impact eligibility for benefits*.* There is also a concern for how reverse mortgage payouts can impact a borrower's eligibility for means-tested benefits programs. A potential reverse mortgage borrower receiving Supplemental Security Income (SSI) and/or Medicaid, or intending to apply for these means-tested benefit programs in the future, should stay away from the "lump sum" type of reverse mortgage, which gives the maximum amount of money available to the senior in one up front payment. A "lump sum" reverse mortgage payout will immediately put the elder above the asset limit for SSI/Medicaid and disqualify the senior for these important benefits, unless careful legal planning is done to avoid this result. Unfortunately, some lenders are currently incentivizing "lump sum" reverse mortgages by slashing closing costs on these specific types of loans.[24] In addition, seniors may find the "lump sum" reverse mortgage more attractive than the other types, including the monthly and credit line options, because it is currently the only reverse mortgage that comes with a fixed interest rate option. Elders receiving a reverse mortgage in the form of a monthly payment or credit line, must also be careful to spend down the money received each month in order to remain eligible for SSI or other needs based benefits.

There is no reverse mortgage crystal ball. If a senior takes out all of her available equity in a "lump sum" reverse mortgage at an age that is on the younger side for getting a reverse

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[23] U.S. Dep't of Housing and Urb. Dev., About Reverse Mortgages for Seniors, http://www.hud.gov/offices/hsg/sfh/hecm/hecmabou.cfm.

[24] Rachel L. Sheedy, *Reverse Mortgage Lenders Cut Fees*, KIPLINGER'S RETIREMENT REPORT, July 13, 2010, *available at* http://www.aarp.org/work/retirement-planning/info-09-2010/kip_reverse_mortgage_lenders_cut_fees.html.

mortgage (for example, in her 60s or 70s), she may find herself needing that money in the future to pay for medical care, assisted living care, home care costs, or home repairs. At that point, the money will not be available to the senior.

In general, reverse mortgage borrowers may remain in their homes until they die or permanently move out unless they default. However, this is of little help to seniors who need money for day-to-day living expenses down the road and find that no more money is available to them. Also, the elder may run out of money necessary to maintain the property or pay property taxes and insurance. These are all loan “triggers” that will cause the lender to call the entire loan due, leading to foreclosure and the eviction of the senior from the home.

The Rise of the Reverse Mortgage as a Social Phenomenon

Today's reverse mortgages are complex products designed to respond to modern problems. Yet modern reverse mortgages share intriguing parallels with the mortgages of the past. To put today's reverse mortgages in perspective we include insights into the product's origins, growth and cultural impact.

I. History and Growth

Originally deriving from the Old French word "mort" meaning dead and "gage" meaning pledge, the term "mortgage" meant that the debtor made a conditional pledge of property to the creditor that would be extinguished if the debtor repaid the debt within a certain period.[25] The modern term "reverse mortgage" comports neatly with the original notion of "mortgage" in that the creditor can look to the home for repayment of the loan upon the death of the debtor.[26] With the modern mortgage, the debt can also become due if the borrower permanently moves out of the home or defaults for not paying taxes, insurance or keeping up with the maintenance of the home.

American reverse mortgages began appearing in the 1960's. These products provided periodic loan advances from private lenders and required that the loan be paid off at some predetermined time. In 1988 the Federal Housing Authority, a branch of the U.S. Department of Housing and Urban Development (HUD), began a federally insured reverse mortgage pilot program called the Home Equity Conversion Mortgage (HECM). This program studied national property values, interest rates and the longevity of a prospective borrower and development a government backed insurance pool to protect the lender's investment. Today, nearly all reverse mortgages are HECMs.

Over the last several years there has been a dramatic growth in HECM loans. According to HUD data, as reported by the National Reverse Mortgage Lenders Association, in HECM's first full year, 1990, there were only 157 loans placed. In calendar year 2001, 8,127 HECMs were sold. By calendar year 2004 the HECM began catching on with 47,266 being sold; then 48,493 in 2005; 85,639 in 2006; and over 100,000 every year since 2007. As of fiscal year 2009 there have been a total of over 640,000 HECM loans created.[27] HUD projects the

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[25] OXFORD ENGLISH DICTIONARY (3d. ed. 2010) (online version), http://www.oed.com/view/Entry/122468?rskey=p7gN0I&result=1&isAdvanced=false#.

[26] Under English common law, upon the debtor's death the mortgage obligation passed to the debtor's heirs. *See* Frank S. Alexander, *Mortgage Prepayment: The Trial of Common Sense,* 72 CORNELL L. REV. 296-97 (1987). In the 18th Century, English Parliament established procedures that enabled creditors to seek not just money from the debtor or debtor's heirs, but the property itself as well. *Id.* at 297.

[27] National Reverse Mortgage Lenders Association, Annual HECM Production Chart, http://www.nrmlaonline.org/rms/statistics/default.aspx?article_id=601.

number of HECMs that will be sold in fiscal year 2017 will be 144,361.[28] The HUD data clearly demonstrates that reverse mortgages are on an upward trend.

II. Cultural Impact

In earlier times the American Dream envisaged a family where parents worked hard and sacrificed in order for their children to attain a better and more secure position in life. That was the reputed passageway out of poverty into the middle class, and owning a home was always the centerpiece of the American Dream. In earlier times, the working class strived to clear the debt off of their homes. When they achieved the goal of paying off their home loans there were often mortgage burning parties. A mortgage burning signified the accomplishment of a lifetime. It represented the autonomy and power of the homeowner over his or her destiny. It was a celebration where family and friends gathered to eat, drink and witness a symbolic event. Retiring debt-free with a chance to leave a legacy was considered a laudable goal.

Times have changed. Enter the reverse mortgage loan, and with it a shift in the social paradigm. With a reverse mortgage, seniors drain off the equity in their homes. Instead of the preservation of a family legacy, seniors are being encouraged to tap into their home equity for whatever reason they so choose. Elder homeowners are encouraged to disregard negative aspects of reverse mortgages with statements like, "It . . . makes sense if you don't care about the costs and want to have fun while you can with the money you have earned because the costs aren't due until you're done with the home."[29] They are being urged to use reverse mortgages to make large gifts, and make donations to favorite charities.[30] They are being tempted to make extravagant purchases like vacation property[31] and are being teased with queries such as, "What better time to just get away than when your working days are behind you and the weather turns a bit gloomy? Proceeds from a reverse mortgage have allowed many homeowners to take that vacation they've always dreamed about, but never had the time or resources to take. Bon voyage!"[32] The marketers are also propagating a darker message that, "The adult children of elderly parents can be cruel and grasping. They view Reverse Mortgages as something being stolen from them. They treat their own parents as thieves."[33]

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[28] IBM GLOBAL BUSINESS SERVICES, *supra* note 5, at 8.

[29] E Home Fellowship, Reverse Home Mortgage Info, http://www.way2hope.org/reverse_home_mortgage_info.htm.

[30] *Id.* ("Some will want to make large gifts or donations with part of the equity from their home and want to see the money used").

[31] Inside Real Estate, Using a Reverse Home Mortgage to Purchase a Home or Vacation Property, http://inside-real-estate.com/stevenduke/2010/05/19/using-a-reverse-mortgage-to-purchase-a-home-or-vacation-property/.

[32] Bills.com, Top 5 Reasons People Get Reverse Mortgages, http://www.bills.com/reverse-mortgage-info-article/.

[33] Mark Flanders, A Reverse Mortgage Stole My Inheritance, Soundbiteblog.com (Mar.8 2007), http://soundbiteblog.com/2007/03/08/a-reverse-mortgage-stole-my-inheritance/.

Senior home equity is a tempting target for self-serving promoters. The AARP 2007 study "Reverse Mortgages: Niche Product or Mainstream Solution?" notes that elders control four trillion dollars in home equity.[34] Proponents of reverse mortgages and those who urge caution agree that reverse mortgages serve a valuable purpose as a source for accessing ready cash for seniors who have no viable alternatives and face immediate financial ruin. However, major disagreements exist over the use of reverse mortgages as a source to fund investments or as a means of getting cash to augment their lifestyles. According to the AARP study, less than one half of all reverse mortgages were sought by those who indicated that the main use was for daily necessities or because the seniors had a desperate need for cash.[35] The study showed that a slight majority of reverse mortgage loans are being used for what was termed as "extras."

Whether the seniors are using equity for extras or necessities, because of the high cost of these loans, the reverse mortgage ultimately means an end to the home passing as part of an elder's estate. Without adequate consumer protections in place, these present-day reverse mortgage realities can exact a significant future negative impact on individuals, families and society.

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[34] DONALD L. REDFOOT, KEN SCHOLEN & S. KATHI BROWN, AARP, MORTGAGES: NICHE PRODUCT OR MAINSTREAM SOLUTION? REPORT ON THE 2006 AARP NATIONAL SURVEY OF REVERSE MORTGAGE SHOPPERS v (2007), *available at* http://assets.aarp.org/rgcenter/consume/2007_22_revmortgage.pdf.

[35] *Id.* at xi, 22, 24, 59.

Today's Reverse Mortgage Marketplace—New Developments Calling for New Protections

While the reverse mortgage market continues to grow, there are deep concerns about aggressive marketing and misleading advertising, the suitability of the products for some borrowers, and the inadequacy of consumer protections to prevent abuses. At the same time, the Federal Bureau of Investigation (FBI) notes that the increase in the HECM loan market is "creating significant opportunities for fraud perpetrators" to take advantage of seniors.[36] The FBI notes that seniors are particularly vulnerable to fraud "because they are most likely to have a 'nest egg,' to own their home, and/or have excellent credit—all of which make them attractive to con artists."[37] The FBI notes that elders are targeted for fraud because they are polite, trusting, less likely to report fraud and when they do, it's usually after considerable delay. Further, elderly victims often cannot aid law enforcement in prosecuting criminals because, according to the FBI, they often make poor witnesses.[38] These characteristics make elders prime targets for financial fraud involving reverse mortgages. Considering these and other realities, we present important findings that should be considered in formulating future consumer protections.

While the reverse mortgage market continues to grow, there are deep concerns about aggressive marketing and misleading advertising, the suitability of the products for some borrowers, and the inadequacy of consumer protections to prevent abuses.

I. Vulnerable Target Market—Documented Decision Making Challenges for Seniors

University of Iowa Study

How responsible should seniors be for making their own financial decisions and how does this play out in the context of aggressive reverse mortgage loan marketing? Described as a first of its kind investigation, in late 2007, the University of Iowa published a study, *The Orbitofrontal Cortex Real-World Decision Making, and Normal Aging*,[39] which recognized that during decision making tasks some older persons' abilities to make sound decisions and avoid fraud may be significantly compromised. When the study was commenced, its authors noted that "despite recent legislative emphasis on this issue, research efforts examining older consumers' vulnerability to fraud are sorely lacking."[40]

The study investigated the hypothesis that some seemingly normal older persons have deficits in reasoning and decision making due to dysfunction in a neural system

[36] Fed. Bureau of Investigation, Fraud Target: Senior Citizens, http://www.fbi.gov/scams-safety/fraud/seniors.

[37] *Id.*

[38] *Id.*

[39] Natalie L. Denburg et al., *The Orbitofrontal Cortex, Real-World Decision Making, and Normal Aging*, 1121 Ann. N.Y. Acad. Sci. 480-498 (2007), *available at* http://www.ncbi.nlm.nih.gov/pmc/articles/PMC2246008/pdf/nihms38390.pdf.

[40] *Id.* (author's manuscript at 2).

which include the prefrontal cortex of the brain.[41] The hypothesis is relevant to the question of why so many older adults fall prey to fraud, and the study's findings suggest a link between prefrontal brain dysfunction, faulty decision making, and vulnerability to misleading advertising.[42]

According to the Iowa Study, the numbers of seniors who may be suffering from this disability is substantial. Their finding indicate that as many as 35 to 40 percent of elders they studied had flawed emotional responses that stem from abnormalities that develop in the brain's prefrontal cortex.[43] The study also determined that these flaws were leading the seniors to make financial decisions based in part on reward and ambiguity, which follow the same approach used by individuals with acquired prefrontal lesions (traumatic brain injury).[44]

Importantly, the University of Iowa Study concluded that "It is hard to overemphasize the ramifications of impaired decision making for older adults."

The significance of this study is that older adulthood is a period of critical and complex decision-making and "there is a lot at stake"[45] with the elderly dealing with such issues as investment of savings and retirement income, purchase of insurance and living trusts, estate planning, and sudden changes in financial roles following the death of a spouse. The study emphasized that most of these decisions are made while the person is on a fixed income and under conditions that would be a challenge even for healthy young adults.[46]

Importantly, the University of Iowa Study concluded that "It is hard to overemphasize the ramifications of impaired decision making for older adults. From a public policy perspective, our research has immediate implications for the voluntary and regulatory control of advertising."[47] If the study's conclusion is correct, then considering possible executive dysfunction in conjunction with fraudulent marketing, older adults considering reverse mortgages are more susceptible to financial abuse than was otherwise imagined. The Iowa Study showed that many older adults, who are perceived as normal and free of obvious neurologic or psychiatric disease, actually have reasoning and decision-making deficits.[48]

Counseling may not be effective in helping a substantial number of seniors overcome false impressions they may hold about the reverse mortgage they intend to purchase. The Iowa Study indicates that older adults are less likely to decipher implied claims

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[41] *Id.* (author's manuscript at 1).
[42] *Id.* (author's manuscript at 10).
[43] *Id.* (author's manuscript at 1).
[44] *Id.*
[45] *Id.* (author's manuscript at 2).
[46] *Id.*
[47] *Id.* (author's manuscript at 10).
[48] *Id.* (author's manuscript at 1).

and are vulnerable to what they called the "truth effect" which is the tendency to believe repeated information more than new information.[49] This means that older adults have relatively poor context or source memory but relatively intact familiarity of repeated claims.[50] This would mean that the repetitive messages in the advertising of reverse mortgages and the intensity of marketing will override any new information that might contradict the claims for the advertized products. For many of the seniors, by the time they are receiving counseling they have already made up their mind to purchase the reverse mortgage and the counseling session is basically an administrative procedure they are forced to go through before they are given the money. If the Iowa Study is correct, any new information, such as information a counselor might tell a senior, will be overridden by the "truth effect" (the repetitive messages) that led them to the reverse mortgage in the first place.

Given the Iowa Study findings, policy makers and concerned citizens should reevaluate the overall effectiveness of reverse mortgage counseling and implement ways to make it more effective. Counseling can only be effective if there are strong protections against misleading marketing.

II. GAO Finds Misleading Marketing Common, Counseling Lacking and Cross-Selling Confusing for Consumers

The GAO found that 26 different entities made potentially misleading claims in HECM marketing materials the GAO had gathered and analyzed for its investigation.

In June 2009, the Government Accountability Office (GAO) published an in-depth report examining Home Equity Conversion Mortgages (HECMs).[51] The report raised many issues of concern for both consumers and regulators. The most significant findings, discussed in more detail below, include misleading marketing of HECMs, serious counseling shortcomings, and confusing cross-selling of products to consumers creating opportunities for abuse.

Regarding misleading marketing, the GAO found that 26 different entities made potentially misleading claims in HECM marketing materials the GAO had gathered and analyzed for its investigation.[52] While the GAO found "few such claims among the materials from the top 12 HECM lenders,"[53] the 26 entities whose materials contained potentially misleading claims includes entities regulated by federal banking regulators, the Federal Trade Commission (FTC), state regulators, and both members and nonmembers of the National Reverse Mortgage Lenders Association (NRMLA).[54]The GAO characterized these claims as

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[49] *Id.* (author's manuscript at 7).
[50] *Id.*
[51] GOV'T ACCOUNTABILITY OFFICE, *supra* note 15.
[52] *Id.* at 19-20.
[53] *Id.* at 19.
[54] *Id.* at 19-20.

The GAO found that the cross-selling of products in conjunction with reverse mortgages confuses consumers and creates opportunities for abuse.

"inaccurate, incomplete" or employing "questionable sales tactics."[55] The six most common misleading implications include:

1. The borrower cannot owe more than the value of the home.
2. The lender cannot foreclose on a HECM and the borrower cannot lose the home.
3. The borrower can access lifetime income or cannot outlive a reverse mortgage.
4. A reverse mortgage is a government "benefit" or "entitlement" or any implication that the HECM is not a loan.
5. Geographic or time limits for obtaining a reverse mortgage.
6. Government affiliation through the use of government language and symbols. [56]

Additionally, the GAO found that the cross-selling of products in conjunction with reverse mortgages confuses consumers and creates opportunities for abuse. Cross-selling can be described as encouraging borrowers to use reverse mortgage funds to purchase insurance or other products that may not be in the borrower's best interest, and are potentially unsuitable given the borrower's personal financial circumstance. The GAO noted, for example, that cross-selling "an annuity that defers payments for a number of years may be unsuitable for an elderly person."[57]

The GAO also noted the need to improve HUD oversight of HECM counselors.

The GAO also noted the need to improve the U.S. Department of Housing and Urban Development (HUD) oversight of HECM counselors. It found that the quality and content of in-person counseling sessions was lacking. The GAO found that there were no guidelines in place for telephone counseling, an alarming observation given that the GAO identified that 90 percent of HUD reverse mortgage counseling takes place by telephone.[58] To improve counseling oversight, the GAO recommended that HUD should take the following steps:

- implement methods to verify the content and length of HECM counseling sessions;
- issue detailed guidance for HECM counseling providers about how to record the amount of counseling time on the counseling certificate;
- issue detailed procedures for HECM counseling providers on how to assess prospective counselees' ability to pay for HECM counseling; and
- implement internal controls to ensure that HECM providers comply with counselor referral requirements.[59]

In response to the GAO investigation showing that HUD counseling was severely lacking in many areas, HUD recently implemented new counseling education guidelines.[60]

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[55] *Id.* at 19.
[56] *Id.* at 21-22.
[57] *Id.* (Summary Page - "What GAO Found").
[58] *Id.* at 56.
[59] *Id.* at 48.

Early indications are that concerns persist regarding the adequacy and sufficiency of counseling provided to potential reverse mortgage borrowers.

Notwithstanding this change, early indications are that concerns persist regarding the adequacy and sufficiency of counseling provided to potential reverse mortgage borrowers. Among them, 90 percent of borrowers continue to receive reverse mortgage counseling over the phone which continues to present problems regarding authenticity. The person providing the phone counseling cannot verify with 100 percent certainty that the person on the phone is really the potential reverse mortgage borrower. Phone counseling also presents challenges when multiple individuals need to or would benefit from being involved in the counseling session, including co-borrowers or non-borrowers who may share the dwelling and would be impacted by the reverse mortgage.

III. Aggressive Marketing Surge

Breaking Down Barriers

Whether by accident or design, marketers of reverse mortgages are invariably sweeping in the kinds of individuals described in the University of Iowa study, those with damaged cortexes impeding their ability to resist fraudulent marketing. Even healthy individuals are at risk of falling prey to persistent and misleading advertising and other marketing methods involving reverse mortgages.

Brokers are being enticed to sell reverse mortgages with promises of high commissions and easy sales.

The brokers and lenders of reverse mortgages are saturating the airwaves, print media, and internet and using sophisticated marketing methods that target and track prospective senior purchasers. The marketers are pushing their products with a sustained intensity that is designed to create a need for a reverse mortgage and to break down whatever resistances the seniors may have.

The reverse mortgage marketers are very mindful of what they need to do in order to be successful in selling to seniors. For example, one group called Response Maker is telling reverse mortgage sellers, "These Consumers Understand--Simply having a reverse mortgage offer mentioned on the AARP webpage and through most senior web links is an excellent way to gain trust from your candidates as most of the seniors that would respond to this ad have had some contact or consideration with the AARP"[61]

There are some data mining companies that are aggressively offering to sell lists of "totally exclusive, hot prospects to work with" [62] to insurance agents and financial advisors who sell reverse mortgages, life insurance and annuity products and others

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[60] U.S. Dep't of Housing and Urb. Dev., *supra* note 21.

[61] Response Makers, Reverse Mortgage Leads – How to Generate Quality Responders, http://www.responsemaker.com/reversemortgageleadsc.html.

[62] Advisors Prospecting and Leads Program Details. http://www.advisorsproshop.com/prospect_pro_details.asp.

offering rapid on line sales leads, which they will post directly to an agent's URL "Within 10 seconds of us gathering all their information and determining interest services."[63] They say they'll pre-screen and relay information to the agent about a senior's home value, mortgage balance (if any), age, age of spouse, names and ages off everyone on title, and the reason the senior needs extra money. Brokers are told that the advantages of having information immediately relayed to them is that "it eliminates any call back problems related to paper lead sheets where sometimes the prospect isn't home at the set call back time or the wrong spouse picks up the phone and says 'Not interested' or sometime their memory fails by the time the agent gets them on the phone."[64]

Elders are "softened" for the reverse mortgage pitch by receiving a constant stream of positive messages about the product.

At the same time, brokers are being enticed to sell reverse mortgages with promises of high commissions and easy sales. A recent letter sent to life insurance agents by Senior American Funding, Inc. "Reverse Mortgage Specialists" touts that with "commissions as high as they are, making one sale today is like making three sales last year." In pitching its Reverse Mortgage Seminar marketing package to agents, Senior American Funding, Inc. promises "These Reverse Mortgage seminars are a golden goose right now. If you can close two Reverse Mortgage sales at a net commission of $10,000 from a seminar that cost you $2,500, you receive a 400% return on your money."[65]

Building Trust--the Use of Celebrity Spokespersons

Elders are "softened" for the reverse mortgage pitch by receiving a constant stream of positive messages about the product. Paid celebrity spokespersons recognized and trusted by seniors have appeared in television commercials touting the benefits of reverse mortgages. These have included actors James Garner,[66] Robert Wagner[67] and Henry Winkler.[68] Actor and former Senator Fred Thompson is also a paid celebrity spokesperson. He is featured in advertisements by American Advisors Group (AAG) and appears on the company website with a caption offering "The Best Advice for a Better Life."[69]

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[63] Fidelity Data, Inc., Reverse Mortgage Lead Generation Program, http://fidelitydata.com/ReverseMortgageLeads.htm.

[64] *Id.*

[65] Letter from Senior American Funding, Inc., to Agents (on file with authors).

[66] Financial Freedom, TV Commercial, http://www.financialfreedom.com/Commercial/.

[67] *Senior Lending Network, Robert Wagner Reach Out to Area Seniors*, PR NEWSWIRE, Apr. 21, 2009, *available at* http://news.prnewswire.com/DisplayReleaseContent.aspx?ACCT=104&STORY=/www/story/04-21-2009/0005010001&EDATE.

[68] One Reverse Mortgage, LLC, Retirement Your Way!, https://www.onereversemortgage.com/about/retirement-your-way.

[69] American Advisors Group, http://www.aagreverse.com/index.php.

Reverse Mortgage "Mills"-- Feeding Demand

Reverse mortgage mills are seminars offered by companies with an interest in generating sales commissions by targeting seniors in order to convince them to take out a reverse mortgage. These seminars often take place at senior centers, restaurants, and hotels, and often feature free lunch or dinner. The sales person may recommend that a reverse mortgage should be used to fund living trust, deferred annuities, or long term care insurance.

. . . "free lunch" seminars involving reverse mortgages and other types of investments raise a concern about the possibility of "unscrupulous and abusive sales practices and investment frauds targeted towards senior investors."

In a joint report issued in September 2007 by the Securities and Exchange Commission (SEC), the North American Securities Administrators Association (NASAA) and the Financial Industry Regulatory Authority, securities regulators noted that so-called "free lunch" seminars involving reverse mortgages and other types of investments raise a concern about the possibility of "unscrupulous and abusive sales practices and investment frauds targeted towards senior investors."[70] The seminars they investigated sell many products, including reverse mortgages.[71] According to the NASAA, ". . . research has found that 78 percent of seniors received a free lunch seminar invitation and 60 percent received six or more invitations in the past three years."[72] The investigation found that "half of the examinations found that firms used advertising and sales materials that may have been misleading or exaggerated or included apparently unwarranted claims,"[73] and that "individuals attending the sales seminars may not understand that the seminar is sponsored by an undisclosed company with a financial interest in product sales."[74] The concerns raised extend beyond susceptibility to misleading advertising and confusion about the sponsor's financial stake in selling the products. Worse yet, the products sold to the unsuspecting seniors may not be suitable for those who fall for the sales pitch. The investigation found that "some firms may not be adequately considering the individual needs and circumstances of each customer when determining whether a product was suitable for that customer."[75] For examples of advertisements used to attract seniors to "free lunch" seminars, the joint report includes 14 pages of "illustrative examples of the types of advertisements commonly used."[76]

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[70] U.S. SEC. AND EXCHANGE COMM'N, NORTH AMERICAN SEC. ADMINISTRATORS ASS'N, & FIN. INDUS. REG. AUTHORITY, PROTECTING SENIOR INVESTORS: REPORT OF EXAMINATIONS OF SECURITIES FIRMS PROVIDING "FREE LUNCH" SALES SEMINARS 2 (2007), *available at* http://www.sec.gov/spotlight/seniors/freelunchreport.pdf

[71] *Id.* at 4.

[72] Press Release, NASAA, "Free Lunch" Investment Seminar Examinations Uncover Widespread Problems, Perils for Older Investors (Sep. 10, 2007), http://www.nasaa.org/nasaa_newsroom/current_nasaa_headlines/7176.cfm

[73] U.S. SEC. AND EXCHANGE COMM'N ET AL., *supra* note 70, at 13.

[74] *Id.* at 16.

[75] *Id.* at 21.

[76] *Id.* at 29-42. The following disclosure appears with the sample advertisements: "This appendix contains a sample of advertisements (many of which appeared in local newspapers and mass-mailed invitations) soliciting attendance at sales seminars. They are included as illustrative examples of the

New Products--New Opportunities for Marketing Confusion

There are many reverse mortgage products to choose from. Borrowers can choose the regular HECM option, with its different interest rate options (fixed or adjustable), length of loan options (tenure or term), and payout options ("lump sum", monthly, credit line or combination). Beginning in October 2010, FHA began offering a new reverse mortgage that has much lower up-front fees than the standard HECM. It is called the "HECM Saver" and with it, seniors can borrow 10 percent to 20 percent less than they can with a standard HECM reverse mortgage.[77] Additionally, borrowers owning pricier homes beyond the HECM loan limits have the option of taking out a proprietary loan, which is not covered by federal insurance. Borrowers may also purchase a new home with reverse mortgage proceeds via the HECM for Purchase program. Under this program, the senior must occupy the new property within 60 days from the date of closing. This is a very expensive way to finance a new home and should be weighed carefully against the option of selling the principal residence and downsizing to a smaller property.[78]

It is not uncommon for reverse mortgage purveyors to exploit the ever changing market, including changes in reverse mortgage principal limits, in order to pressure seniors to take out reverse mortgages.

In some cases, new products can help borrowers achieve their goals in a suitable fashion. However, it is not uncommon for reverse mortgage purveyors to exploit the ever changing market, including changes in reverse mortgage principal limits, in order to pressure seniors to take out reverse mortgages. Whenever the federal loan limit changes or there is an anticipated adjustment in the mortgage insurance premium, some reverse mortgage sellers will tell prospective reverse mortgage borrowers that they had better "act now or suffer the consequences," meaning that they will receive less money if they wait. In this way the frequent changes and confusion over the multitude of reverse mortgage products feed the high pressure advertising machine.

IV. Selling Unsuitable Products

Activity of Insurance Companies in Marketing Reverse Mortgages: Long-Term Care Insurance and Annuities

The AARP study, *Reverse Mortgages: Niche Product or Mainstream Solution*, cautions against using reverse mortgages as a funding source for long-term care insurance or annuities.[79] Recommendation 16: "Sales practices that attempt to convince consumers to use home equity to pay for such insurance should be defined

types of advertisements commonly used. Including them in this report does not indicate that they contain either accurate or inaccurate statements. The names of the sponsors, addresses, telephone numbers and other identifying information have been redacted."

[77] Fed. Housing Admin., U.S. Dep't of Housing and Urb. Dev., Consumer Fact Sheet for HECM Saver, http://www.hud.gov/offices/hsg/sfh/hecm/factsheetconsumerhecmsaver.pdf.

[78] *See* U.S. Dep't of Housing and Urb. Dev., HECM for Purchase: Frequently Asked Questions, http://www.hud.gov/offices/hsg/sfh/hecm/faqs_hecm.cfm.

[79] REDFOOT, ET AL., supra note 34, at 119.

as violations of suitability standards. Alternatively, states should require a statement of the combined average monthly cost of the insurance plus the reverse mortgage projected on an annual basis to beyond the consumer's life expectancy."[80]

Not everyone needs long-term care insurance. In some instances, individuals will automatically qualify for Medicaid the government's long-term care benefits program and therefore never need a long-term care insurance policy. Due to the high costs of a reverse mortgage's compounding interest, origination fees, service fees, insurance, and other costs, the longer an individual pays for long-term care insurance premiums through a reverse mortgage, the more unsuitable the transaction. Potential borrowers need to see illustrations of the compounding costs of the reverse mortgage alongside of the long-term care insurance policy's projected policy payouts (minus the annual long-term care insurance premium costs) in order to understand whether or not long-term care insurance would make sense for them.

Deferred Annuities and Reverse Mortgages

Insurance brokers are now actively seeking agents to promote reverse mortgages. According to Neil Granger, a career life agent and expert witness on annuities and long-term care insurance, agents are being told by brokers that they can "ethically" get seniors to pull out equity in order to buy insurance. Granger says, "I can't think of any instances where it is appropriate to use home equity to fund deferred annuities or any financial justification for doing so."[81] Using a reverse mortgage to fund a deferred annuity has caused problems for seniors.[82]

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[80] *Id.*

[81] Interview of Neil Granger by Prescott Cole (Nov. 28, 2010).

[82] *See, e.g.*, Maryl Harris, *Reverse Mortgage Brokers Are No Angels*, CBS MONEYWATCH, Oct. 29, 2009, *available at* http://moneywatch.bnet.com/saving-money/blog/consumer-reporter/reverse-mortgage-brokers-are-no-angels/392/; *Reversals of Fortune*, CONSUMER REPORTS, Sep.2009 ("Selling More Than Loans"), *available at* http://www.consumerreports.org/cro/magazine-archive/september-2009/personal-finance/reverse-mortgages/selling-more-than-loans/reverse-mortgages-selling-more-than-loans.htm.

Here is a brief example that highlights the shortcomings of using home equity through a reverse mortgage 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 question is, what will the cost be for financing the deferred annuity through a reverse mortgage?

Assume reverse mortgages interest rates are now around six percent. Because of compounding, in ten years at six percent interest, 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 averaging three percent interest. It is absolutely 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 asset out of the senior's control for years and there are substantial penalties and fees for early withdrawals.

H.R. 3221—More Protections Needed

In December of 2007, Senator Claire McCaskill chaired a hearing of the Special Subcommittee on Aging to examine some of the abuse in the reverse mortgage market. [83] The Coalition to End Financial Abuse (CEASE), a broad-based coalition of non-profit organizations, raised the issue of insurance agents who were promoting reverse mortgages as a source for generating cash to purchase annuities. CEASE informed the Committee that many of these insurance agents were the same ones who had been working the trust mills and other senior financial scams[84] and very adept at using false and misleading information in order to sell their products. CEASE noted that misrepresenting the facts is a way to panic seniors into purchasing unsuitable financial products such as annuities with funds from reverse mortgages[85] and that fear is the financial predator's greatest tool.[86]

As a result of the December 2007 hearing, Congress developed H.R. 3221, which was later signed into law.[87] H.R. 3221 prohibits brokers and lenders who sell HECM

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[83] For news coverage of the hearing, *see, e.g.*, *The Next Subprime: Reverse Mortgages*, SALON.COM, Dec. 13, 2007, http://www.salon.com/technology/how_the_world_works/2007/12/13/reverse_mortgages/index.html; *Claire McCaskill Hearing Shows Reverse Mortgages Out of Control*, DAILY KOS, July 1, 2009, http://www.dailykos.com/story/2009/7/1/749007/-Claire-McCaskill-hearing-shows-reverse-mortgages-out-of-control.

[84] Letter from Prescott Cole to Senator Claire McCaskill 2 (Dec. 12, 2007) (on file with author).

[85] *Id.* at 3.

[86] *Id.*

[87] The Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, 122 Stat. 2654 (2008), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ289.110.pdf.

loans from promoting annuities or employing any party that participates in or is associated with financial insurance activity. H.R. 3221 is limited to HECM loans, which means this law didn't affect sellers of non-HECM products.

Regardless of whether or not H.R. 3221's restriction applied to brokers and lenders of non-HECM reverse mortgages, the new law does did not prevent insurance agents from working up their senior clients and directing them to get reverse mortgages to fund insurance products. These agents will continue to be attracted to the reverse mortgage market because equity rich seniors offer them lucrative sales opportunities in a largely unregulated environment. The new law eliminates leads some insurance agents may have been getting from HECM brokers but it hasn't slowed down the agents who do their own senior outreach and marketing.

The new law has a carve-out for banks that sell HECMs. If those banks have financial service desks where insurance agents are selling annuities then the broker isn't allowed to send the senior over to the insurance agent. What is allowed is for the insurance agents, sitting at the financial services desks, to send senior customers over to the reverse mortgage desks to arrange for loans to fund the annuities.

The new law called for a study to determine consumer protection and underwriting standards and to examine and determine appropriate consumer protections and underwriting standards that would ensure the purchases of insurance products are appropriate for consumers. The study H.R. 3221 envisioned is to be a consultative effort with recognized experts in consumer protection, industry representatives, representatives of counseling organizations, and other interested parties. Many consumer advocates believe even if a study has findings and makes recommendations, the most senior borrowers needing protection can hope for would be a proposal for future legislation. The real world, net effect of H.R. 3221 is that it will be years before the public can expect any legislative protection from insurance agents who target a senior's home equity.

V. The Ghost of Subprime Past--Subprime Revisited

Following in the wake of the subprime mortgage meltdown are concerns that today's reverse mortgage market has a lot in common with the failed subprime market and that the warning signs are too significant to ignore. According to John Dugan, who served as the 29th Comptroller of the Currency for the U.S. Department of the Treasury from August 2005 to August 2010, subprime loans and today's reverse mortgages share these troubling common characteristics: "a vulnerable customer class; complex product features that can be difficult to explain and can be susceptible to deceptive marketing; nontraditional, asset-based underwriting; and the potential for skewed incentives for key distributors of the product."[88]

The possibility of reverse mortgages becoming the "new subprime" is a huge cause for concern as misaligned incentives drove subprime lenders to engage in high-volume improvident lending and consumer abuses.

The possibility of reverse mortgages becoming the "new subprime" is a huge cause for concern as misaligned incentives drove subprime lenders to engage in high-volume improvident lending and consumer abuses. Further, securitization, a significant factor in the subprime explosion in the late 1990s and at the beginning of this decade is becoming commonplace in the reverse mortgage industry, according to the National Consumer Law Center (NCLC). In its 2009 report entitled "Subprime Revisited," NCLC found that "reverse mortgage lenders are also looking to securitization to supply a steady stream of capital to meet the growing demand for reverse mortgage products."[89] NCLC aptly notes that securitization can be both a blessing and a curse for seniors who are considering reverse mortgages. Securitization provides more capital for making reverse mortgage loans, but it also creates incentives for reverse mortgage lenders and brokers to push borrowers into reverse mortgages that may not be suitable for the borrower.

Ultimately, the record number of failed subprime loans is recognized by many as being a major catalyst for the United States economic crisis with reverberations in international economies as well.[90] Beyond impacting whole economies, the subprime mortgage meltdown has lead to untold losses for consumers and investors, many of whom are seniors who are now considering reverse mortgages as an option for making ends meet due to reduced retirement assets. Alarms should sound as former subprime lenders seek new opportunities in the reverse mortgage market now that subprime lending has all but come to a halt. The public, policymakers and legislators should be aware that this time, yesterday's subprime lenders are now preying on a growing elderly population who are trying to remain financially independent in their own homes during a depressed economy.

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[88] John. C. Dugan, Office of Comptroller of Currency, Speech Before the American Bankers Regulatory Compliance Conference, Orlando, Florida (June 8, 2009), http://www.occ.gov/news-issuances/speeches/2009/pub-speech-2009-61.pdf, at 6.

[89] NAT'L CONSUMER LAW CTR., *supra* note 4, at 10.

[90] CONG. RESEARCH SERV., THE U.S. FINANCIAL CRISIS: THE GLOBAL DIMENSION WITH IMPLICATIONS FOR U.S. POLICY 12 (2009), *available at* http://fpc.state.gov/documents/organization/115947.pdf; The London Summit 2009, Statement of the G-20, Global Plan for Recovery and Reform (2009), http://www.londonsummit.gov.uk/resources/en/news/15766232/communique-020409; *Credit Crisis—The Essentials*, N.Y. TIMES, July 12, 2010, *available at* http://topics.nytimes.com/top/reference/timestopics/subjects/c/credit_crisis/index.html.

VI. Broadening the Bull's-Eye—Seniors at Risk

Increased Loan Limits Leading to Rising Crime Against Seniors

In 2009, Congress increased the FHA loan limit applicable to HECMs to $625,500 opening the door to many more homeowners who might not otherwise qualify for a reverse mortgage under the previously lower limit of $362,790. However, the rising HECM loan limit is creating heightened law enforcement concern about foreclosure rescue scams and other frauds against seniors involving reverse mortgages.

. . . "unscrupulous loan officers, mortgage companies, investors, loan counselors, appraisers, builders, developers, and real estate agents are exploiting Home Equity Conversion Mortgages (HECMs)—also known as reverse mortgages—to defraud senior citizens."

In March 2009 the Federal Bureau of Investigation (FBI) issued a Bulletin warning about this new potential for abuse. In a joint investigation involving the FBI and HUD's Office of Inspector General, the agency reported that "unscrupulous loan officers, mortgage companies, investors, loan counselors, appraisers, builders, developers, and real estate agents are exploiting Home Equity Conversion Mortgages (HECMs)—also known as reverse mortgages—to defraud senior citizens." [91]

The most common types of schemes involving reverse mortgages highlighted in the FBI bulletin involve equity theft, foreclosure rescue, and investments. While the mechanics of each of these schemes vary, the common factor is that increased HECM loan limits create incentives for perpetrators to involve unwitting seniors in their schemes. In the end, the perpetrators either abscond with the HECM funds, pocket equity that a senior was expecting from a mortgage, or succeed in fraudulently obtaining HECM proceeds by cross-selling useless investment products to the senior. The increased risk to seniors from those who use the lure of a reverse mortgage to defraud a senior underscores the need for stronger protections in the reverse mortgage marketplace.

Regulatory/Law Enforcement Investigations

Media accounts involving reverse mortgage scams detail how seniors are being taken advantage of. The *Atlanta Constitution Journal* reported in April 2010 that the U.S. Attorney's Office had obtained a conviction against two men who scammed senior citizens trying to get reverse mortgage loans.[92] Another recent example involves charges in Florida against a woman who is accused of attempting to defraud a 71 year old in a scam involving a reverse

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[91] Fed. Bureau of Investigation, *supra* note 16.

[92] Kristi E. Swartz, *Lithonia Men Plead Guilty to Mortgage Fraud on Senior Citizens*, ATLANTA JOURNAL-CONSTITUTION, Apr. 8, 2010, *available at* http://www.ajc.com/news/dekalb/lithonia-men-plead-guilty-447412.html.

mortgage.[93] According to another news account, it appears that reverse mortgages are also being used in money laundering scams perpetrated against seniors by organized gangs.[94]

Also, a well known reverse mortgage seller, American Advisors Group (AAG), is the subject of actions by several state attorneys general alleging misleading advertising involving the company's direct mailing materials. Illinois Attorney General Lisa Madigan accused AAG and another company, Hartland Mortgage Centers Inc. of "unfair and deceptive marketing practices to solicit seniors for reverse mortgages."[95] In a press release announcing the lawsuit, Attorney General Madigan stated, "These companies used extremely misleading language in their advertising, sometimes even disguising their loans as government benefits that borrower don't have to repay."[96] In February 2010, Massachusetts banned AAG from conducting business in the state for two years.[97] The company has also had run-ins with regulators in several other states. [98]

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[93] Eliot Kleinberg, *Suburban West Palm Beach Woman Charged with Defrauding 71-Year-Old*, THE PALM BEACH POST NEWS, http://www.palmbeachpost.com/news/crime/suburban-west-palm-beach-woman-charged-with-defrauding-429990.html.

[94] *HECM Fraud Investigations Underway, Says HUD OIG*, REVERSE MORTGAGE DAILY, Nov. 29, 2009, http://reversemortgagedaily.com/2009/11/29/hecm-fraud-investigations-under-way-says-hud-oig/.

[95] Press Release, Ill. Atty. Gen., Madigan Sues Two Reverse Mortgage Brokers for Using Deceptive Marketing to Target Seniors (Feb. 8, 2010), http://www.illinoisattorneygeneral.gov/pressroom/2010_02/20100208.html.

[96] *Id.*

[97] *See* Andy Kroll, *Law & Order: Mortgage Victims Unit*, MOTHER JONES, July 6, 2010, *available at* http://motherjones.com/politics/2010/07/fred-thompson-mortgage-spokesman-american-advisors-group; Mass. Office of Consumer Affairs and Bus. Reg., In the Matter of American Advisors Group (Order to Show Cause and Notice of a Right to Hearing), http://www.mass.gov/?pageID=ocaterminal&L=6&L0=Home&L1=Business&L2=Banking+Industry+Services&L3=Banking+Legal+Resources&L4=Enforcement+Actions&L5=2009+Enforcement+Actions&sid=Eoca&b=terminalcontent&f=dob_aag06292009&csid=Eoca. For a copy of the AAG solicitation giving rise to the Commonwealth of Massachusetts Complaint, *see* http://www.mass.gov/Eoca/docs/dob/aag06292009.pdf.

[98] *See* Andy Kroll, *supra* note 97.

The High Cost of Unsuitable Reverse Mortgages

I. HECM Foreclosure Claims Jump

In August 2010, The Department of Housing and Urban Development's Office of Inspector General (OIG) published a report following an audit motivated by the increasing number of defaults involving HECM loans. The OIG found that an increasing number of borrowers had not paid taxes or homeowners insurance premiums as required, thus placing the loan in default.[99] As of March 2010 there were as many as 20,631 loans that were in default.[100] The maximum claim amount for the 20,631 loans that defaulted for nonpayment of taxes and insurance was more than $3.68 billion.[101] During fiscal year 2009, approximately 83 percent of HECM borrowers withdrew their credit line as a "lump sum" at loan closing; thus, the borrowers had no additional funds available to draw on in future years and payment of taxes and insurance by the servicer would cause the loans to immediately exceed the principal limit and be in default.[102]

The alarming rise in HECM defaults suggests that there are serious systemic problems in the reverse mortgage marketplace that impact the seniors who borrow and taxpayers as well. For these seniors who may have been sold an unsuitable product and have stripped out their equity, curing may be impossible and eviction through foreclosure inevitable. For taxpayers, ultimately, HECM reverse mortgage loan bailouts are funded by their dollars when FHA-insured HECM loans fail. These are the cases in which reverse mortgage lenders obtain a home through foreclosure or a deed in lieu of foreclosure and do not sell such homes for enough to satisfy the balance of the outstanding debt. The HECM lenders then make claims to the Federal Housing Agency (FHA) for the difference and taxpayer dollars are used for payment of those claims.[103]

Since lenders are not required to ensure that the seniors they sell loans to are receiving suitable products, there is almost no incentive to ensure that the products are appropriate for a particular borrower's needs. With the ability to make claims against FHA insurance for HECM loans, lenders are operating in a virtually risk-free environment while borrowers and taxpayers are left to bear the burden of failed HECM reverse mortgages. The current state of imbalance of risk and reward, putting sellers in the most favorable position, must be addressed to curb abuses in the reverse mortgage market.

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[99] U.S. DEP'T OF HOUSING AND URB. DEV., *supra* note 14, at 1.
[100] *Id.* at 11.
[101] *Id.* at 10.
[102] *Id.* at 4.
[103] *Reversals of Fortune*, CONSUMER REPORTS, Sep. 2009 ("The Next Financial Fiasco? It Could Be Reverse Mortgages"), *available at* http://www.consumerreports.org/cro/magazine-archive/september-2009/personal-finance/reverse-mortgages/overview/reverse-mortgages-ov.htm.

II. Seniors' Options Dwindle—Residential Care Facility Move Impossible

A senior with home equity has the potential of selling his or her home and moving into a residential care facility for the elderly (RCFE), should they need assisted living arrangements. Some RCFE offer continuing care, meaning the elder resident can stay in the facility even when they need a higher level of care, such as nursing home care. RCFEs with few exceptions require private pay. By contrast, besides risking default, a cash strapped senior who develops dementia or other debilitating infirmities will not be able to sell their home and move into a RCFE after a reverse mortgage strips all of the available equity from the home, particularly if home equity is their only asset.

III. Some Seniors Risk Forcible Removal

Other serious consequences may follow when a senior is put into a reverse mortgage that is unsuitable. These include forcible removal from the home if the elder becomes incapable of sustaining him or herself and requires custodial care. Adult Protective Services or family members cannot allow an at-risk elder to remain unattended or neglected in their homes. At-risk elders face removal "for their own good" and, without the means to privately pay for a nursing home they are apt to end up on government benefits at a Medicaid long-term care nursing home.

IV. Collateral Damage: Displacement of Non-Borrowing Spouses and Others Living in the Home

Not all borrowers live by themselves. Prospective purchasers of reverse mortgage loans need to consider what will become of the non-borrowers living with the borrower once the borrower has either, died, defaulted or permanently moved from the home. Residing along with the borrowers are often close personal relations, non-borrowing spouses, children and grandchildren. Regardless of relationship to the borrower, all non-borrowers have the same limited legal status; they are "tenants." If the high cost loan cannot be repaid when it is due there will be a foreclosure sale. Unless the new owner makes some arrangement or accommodation with the tenants, they will be forced to move out.

Plight of the Non-Borrowing Spouse

The case of Betty Banks illustrates the pitfalls of a non-borrowing spouse risking eviction from the home after the borrowing spouse dies. According to a Complaint for Damages filed in the Superior Court of the State California, for the County of Los Angeles on August 24, 2010, Betty Banks and her now deceased husband, Auther Banks purchased a Financial Freedom reverse mortgage after they were approached by a representative of American Mortgage Professionals, Inc., a reverse mortgage broker. Mrs. Banks alleges that the loan broker explained that Mrs. Banks was "not old enough to go on the loan because she was not yet 62 years old" and that "the representative stated that they would just eliminate . . . [Mrs. Banks] name from the loan so that Auther Banks could qualify for the loan alone."[104] Mrs. Banks alleges she was told that was the only way Auther Banks could get the loan. Mr. Banks died in April of 2008 and a loan of $272,000 is now due. Mrs. Banks, who is not able to pay off the loan, now risks eviction from her home since she was not a borrower on the reverse mortgage contract.

Plight of the Heirs

Reverse mortgage are non-recourse home loans, meaning that the debt is secured only by the home and the lender cannot come after the borrower/s when there is a default, even if the amount of the debt exceeds the market value of the elder's house. Upon the death of the borrower/s the would-be heirs to the estate are not responsible for repaying the loan. However, if the heirs are interested in inheriting the home, then the reverse mortgage loan (the entire principal, plus accrued interest and service fees) must be paid in full to the lender before the heirs can rightfully take possession of the home. This debt may exceed the actual market value of the home. If the heirs are not able to clear the debt, the lender has the right to foreclose and sell the property. It is doubtful that many of heirs, especially low-wealth heirs, will have the means to pay off the debt and most homes will fall into foreclosure.

Selling a home through a foreclosure does not yield top market dollar. The purpose of a forced sale is not to maximize the amount of the sale; rather it is to make the creditors (lenders) whole. When a home is sold through foreclosure the heirs will be able to keep any residue (the Net Sale Proceeds above the Sales Costs after the Loan Payoff). Since the residue of a foreclosure will be small by comparison to what the reverse mortgage lenders will get many heirs will view the outcome as unfair.

Looking Forward

The year 2007 was an important year for the reverse mortgage industry. That was the first year that the sales of reverse mortgage exceeded 100,000. In every year since 2007 there has been over 100,000 reverse mortgages sold per year.[105] Knowing that loans will be due upon the death of the borrower and that number of reverse mortgage loans is predicted to grow, we can assume that more non-borrowing spouses and other dependents of the reverse mortgage borrower will be impacted by a borrower's death or departure from the home.

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[104] Complaint at 5, Banks v. Financial Freedom (Cal. Dist. Ct. Aug. 24, 2010) (on file with authors).

[105] U.S. DEP'T OF HOUSING AND URB. DEV., A TURNING PONT IN THE HISTORY OF HUD'S HOME EQUITY CONVERSION MORTGAGE PROGRAM 1 (2008), *available at* http://www.huduser.org/periodicals/ushmc/spring08/ch1.pdf.

Complaints to HUD are on the rise from non-borrowing spouses and others living in the home forced to move after the borrowing spouse moves out or dies.[106]

This information, taken together portends a significant future negative impact of reverse mortgages on American society. There is a need for a study to determine whom besides the borrower is living in the homes where reverse mortgages have been sold. It is imperative for policy makers and concerned citizens to have greater insight into this important emerging issue in order to understand the impact that reverse mortgages will have on homelessness and the increased demand for long-term care Medicaid.

[106] *As Complaints Increase, HUD to Address HECM Non-Borrowing Spouse Issue*, REVERSE MORTGAGE DAILY, Apr. 29, 2010, http://reversemortgagedaily.com/2010/04/29/as-complaints-increase-hud-to-address-hecm-non-borrowing-spouse-issue/.

Recommendations

We urge the newly developing Consumer Financial Protection Bureau and other federal and state regulators to consider our findings and to include our recommendations in developing strong and comprehensive policies to protect the public against abuses in the reverse mortgage marketplace.

Establish a suitability standard that promotes long-range solutions and includes strong consumer remedies for violating that standard

As a matter of public policy, reverse mortgages should be considered suitable only when a senior has no other viable option. Reverse mortgages should be considered the loan of last resort due to their high cost, potential for exposing senior borrowers to fraud, misrepresentation and financial abuse, and the risk of displacement of non-borrowers who may share the dwelling.

To ensure that reverse mortgages are sold only to borrowers for whom the product is suitable, at a minimum, the suitability standard should require brokers and lenders to take into account the following:

- Negative consequence and potential harm these products may cause the borrower or others living in the home.

- Whether the borrower truly understands the complexities and potential harm of the reverse mortgage loan being considered.

- Whether the borrower's need for money can be met by other viable alternatives to taking out the reverse mortgage. Alternatives can be other sources of assets that the senior may have access to, less costly loans (such a forward mortgage equity line), inter-family loans, local government loan or grant programs (otherwise known as "single purpose" loans), and public benefits programs.

California's AB 329 requires a lender to give a potential borrower a checklist detailing the issues he or she should discuss with their reverse mortgage counselor.[107] This checklist can be the starting place for developing a list of essential items that lenders and brokers should be required to consider in their suitability determinations. Regulators should exercise their authority to collect and analyze data from brokers and lenders to monitor broker and lender compliance with the suitability standard and institute enforcement actions against lenders and brokers who make unsuitable reverse mortgage loans. Lenders and brokers who violate the

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[107] AB 329 (Cal. 2009) (to be codified at Cal. Civ. Code §§ 1923.2, 1923.5), *available at* http://info.sen.ca.gov/pub/09-10/bill/asm/ab_0301-0350/ab_329_bill_20091011_chaptered.pdf.

suitability standard should be subject enforcement action to revoke their licenses, civil monetary fines for issuing unsuitable loans and a recognized private cause of action as remedies for violations.

Establish a recognized fiduciary relationship

Most seniors assume that lenders and brokers are required to act in their best interest. However, this is not true. While in some cases, courts have implicitly recognized a fiduciary relationship between the lender or broker and borrower, mortgage industry groups continue to argue that it is not necessary.

This report outlines in great detail why a fiduciary duty is necessary both to promote suitability and to protect the senior borrower. We recommend that persons who offer, sell, or make or arrange reverse mortgages have a fiduciary obligation to the borrower, and that any person who breaches this fiduciary duty be liable to the borrower for any damages caused by that breach, including attorney's fees and court costs.

Outlaw deceptive marketing by loan originators and brokers

Seniors may have capacity issues that make them easy prey for financial predators. Research shows that once these seniors have made a decision it is very difficult for them to correct their course of action, even when they are given truthful information and told that the information they had been relying on is false. Therefore, it is imperative to outlaw all deceptive and misleading marketing by loan originators, brokers and others who profit from making reverse mortgages. All advertisements for reverse mortgages should be required to include information about the importance of suitability and the potential negative consequences from obtaining a reverse mortgage.

At a minimum this truthful information about reverse mortgages should include:

- A reverse mortgage is not a suitable choice if you have less expensive alternatives for meeting your financial goals. Consider all alternatives before choosing to proceed with a reverse mortgage.

- You will be required to continue paying your property taxes, insurance and property maintenance costs. If you fail to pay these costs, you will face default and foreclosure and may lose your home.

- Although reverse mortgages do not affect your qualification for Medicare, they could affect your qualification for means-tested programs such as SSI and Medicaid.

- Your spouse or other family member living in the home may lose their right to stay in the home if you die or move out.

Adopt stronger policies against brokers and lenders who cross sell reverse mortgages with annuities and other unsuitable financial products

The new law enacted by H.R. 3221 needs to be strengthened so that brokers and lenders who sell HECM loans are not promoting annuities. That bill created exceptions for banks, so long as they didn't make purchasing an annuity a condition of getting a reverse mortgage and they didn't direct a prospective borrower to an insurance salesperson. What the bill left unaddressed is the conduct of the insurance agent or financial planner who sells products or services and convinces the senior to purchase a reverse mortgage in order to finance the transaction. The prohibition needs to be extended to all reverse mortgage loans and not just HECMs. There needs to be a declaration that the use of reverse mortgage equity to purchase annuities is per se unsuitable and insurance agents or brokers who sell an annuity when they know or should know that reverse mortgage equity will be used to purchase that annuity, shall be held civilly liable in a private cause of action.

The issue of long-term care companies getting into the reverse mortgage business should also be addressed.[108] This phenomenon should be studied to determine if it is leading to abusive practices, with regulations promulgated if problems are found.

Extend a reverse mortgage borrower's right to cancel from 3 days to 30 days

Seniors who purchase annuities and change their mind generally have 10 days to cancel the transaction without penalty via a "free look" period.[109] In California that "free look" period is 30 days for seniors.[110] Seniors who take out reverse mortgages, however, only have three days to cancel the loan transaction, even though they are likely making the last, biggest financial investment of their lives. Three days is simply too short for a senior borrower who may be the victim of a hard sell to determine how to cancel the loan and get their money back. The FBI noted that senior "victims' realization that they have been swindled may take weeks—or more likely, months—after contact with the fraudster." [111]
We believe that reverse mortgage borrowers are due at least the same amount of time to cancel loan transactions as are annuity purchasers in California.

[108] *See Insurance Agency Jumps into HECM Lending*, MORTGAGEORB, Jan. 15, 2010, http://www.mortgageorb.com/e107_plugins/content/content.php?content.5082.

[109] U.S. Sec. and Exchange Comm'n, Variable Annuities – Free Look Period, http://www.sec.gov/answers/freelook.htm.

[110] Cal. Ins. Code § 10127.10(a) (Deering 2010).

[111] Fed. Bureau of Investigation, *supra* note 36.

Strengthen Quality and Content of Counseling

Counseling may not be effective in helping a substantial number of seniors overcome false impressions they may hold about the reverse mortgage they intend to purchase, however there is room for improvement. Below are some practical measures that can be taken to improve the content and quality of counseling that is delivered to potential reverse mortgage borrowers and those who may be significantly impacted by their decision.

Incorporate suitability into the counseling session

Currently, HUD-approved reverse mortgage counselors can only withhold a counseling certificate if the borrower cannot answer five or more of the ten basic questions about reverse mortgage loans that are presented at the end of the counseling session.[112] This is insufficient to make a determination of whether a reverse mortgage is appropriate for a particular borrower. Counselors should be able to withhold a counseling certificate if the counselor determines that a reverse mortgage is not suitable for a particular borrower. In order to make this determination, there should be a stand-alone suitability counseling session at which the sole focus is whether a reverse mortgage is suitable for a particular borrower. This portion of the counseling session would examine the senior's need for money, what the senior intends to do with the money, and whether there are alternative means for getting the needed funds. The quality and intensity of questions would be no more intrusive that what borrowers of conventional bank loans are currently being asked. The suitability criteria would contain a set of inquiries whose responses would lead the counselor to disapprove a loan where appropriate. If the counselor determines or suspects that the reverse mortgage is not in the best interest of the senior, or knows or suspects that the equity will be used to finance an annuity or other unsuitable financial product, then the counseling certificate should be denied.

Break the counseling session into two parts

Some have complained that the new HECM counseling guidelines effective September 11, 2010 are causing the counseling sessions to run up to two hours in length, leading to "senior fatigue."[113] To maximize the borrower's opportunity to learn as much as possible about the reverse mortgage process without undue fatigue, it is reasonable to break the counseling session up into two one-hour parts on different days. The first hour would complete the borrower's budget analysis using the National Council on Aging's Financial Interview Tool (FIT), which is now required under the new counseling protocols,[114] and reverse mortgage alternatives. The second hour would cover the anatomy and features of the reverse mortgage loan and whether the loan is suitable for the particular borrower.

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[112] U.S. Dep't of Housing and Urb. Dev., *supra* note 21, at 43.

[113] *Longer Counseling Sessions for Reverse Mortgages*, REVERSE MORTGAGE DAILY, Nov. 28, 2010, http://reversemortgagedaily.com/2010/11/28/longer-counseling-sessions-for-reverse-mortgages/.

[114] U.S. Dep't of Housing and Urb. Dev., *supra* note 21, at 150.

Require all counseling to be conducted in-person

90% of HUD-approved reverse mortgage counseling is conducted over the phone.[115] Taking into account the complexities of reverse mortgage loans, how much is riding on the transaction for the borrower, the possible hearing or cognitive impairments of the borrower, and the difficulties of determining who exactly is on the phone, in-person counseling should be required for all borrowers, except under hardship circumstances. This is currently the law in North Carolina.[116]

Require counseling for all reverse loan products

In North Carolina, all potential reverse mortgage borrowers, not just HECM borrowers, are required to receive counseling from a HUD-approved counselor. This way, potential proprietary reverse mortgage loan borrowers receive the same education and counseling as potential HECM loan borrowers. This is also the law in California. This counseling requirement should be expanded to protect borrowers in all states where it is not presently required.

Counseling sessions should be digitally recorded

All counseling sessions should be digitally recorded and the record preserved for the life of the loan. The digital record will be preserved as evidence should any questions arise later regarding the borrower's capacity at the time the loan was originated, who participated in the session, or if there were any persons who unduly influenced the borrower to obtain the loan.

Remove counseling exemption for current HECM borrowers seeking a refinance

Current HUD reverse mortgage counseling protocols exempt some borrowers looking to refinance their existing HECM reverse mortgages from counseling if they meet certain requirements.[117] This exemption should be removed. Borrowers looking to refinance existing reverse mortgages are also at risk of taking out loans that are not in their best interest. They require counseling just as much as potential borrowers who have never had a reverse mortgage.

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[115] GOV'T ACCOUNTABILITY OFFICE, *supra* note 15, at 61.

[116] N.C. Housing Fin. Agency, Reverse Mortgage Counseling in North Carolina, http://www.nccob.org/NR/rdonlyres/FA81D3F6-32EF-4BDD-902E-906BE1743634/0/RVMLendercounselingletter.pdf.

[117] U.S. Dep't of Housing and Urb. Dev., *supra* note 21, at 40.

Remove counseling exemption for non-borrowing spouses and adult children

Current HUD reverse mortgage counseling protocols do not require non-borrowing spouses or adult children living in the home to participate in the HUD counseling session. This is a mistake. Although the counseling guidelines state that HUD "recommends" that the non-borrowing parties participate in the counseling session,[118] this is not enough, since those residents will be displaced when the loan is called due. All members of the household need to know what the reverse mortgage could mean for them in the future.

Add Protections for Non-Borrowing Spouses and Others Living in the Dwelling

Create an originator's duty to non-borrowing tenants

Reverse mortgage originators should be required to investigate who besides the borrower resides in the home. The originators should be required to give written notifications to all non-borrowing tenants that the title holders are contemplating a reverse mortgage. The notification should include information about the about their potential legal status and the limits of their rights to remain in the dwelling after the borrower dies or permanently moves out of the home. The written notifications should advise the non-borrowing tenants that they need to develop a relocation plan for themselves. The originators should be required to retain copies of the results of their investigations along with proof that the non-borrowers received the required written notifications.

Conduct a study on displacement risks for survivors

This study should look at the impact on surviving residents living in homes that are subject to reverse mortgages. The study should also investigate and evaluate the long-term societal impact of this displacement on individuals, communities and social services/programs.

Thinking ahead: Spotlight on International Action

We encourage the G-20 to include reverse mortgage protections in its investigation regarding ensuring consumer protections in the financial services marketplace, pursuant to the latest pronouncement from the G-20 Summit Meeting in Seoul, So. Korea in November 2010.119

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[118] *Id.* at 40-41.

[119] The Seoul Summit Document reads, "*Enhancing consumer protection:* We asked the FSB to work in collaboration with the OECD and other international organizations to explore, and report back by the next summit, on options to advance consumer finance protection through informed choice that includes disclosure, transparency and education; protection from fraud, abuse and errors; and recourse and advocacy." G-20 SEOUL SUMMIT 2010, THE SEOUL

Reverse mortgages are raising concerns in some G-20 countries and others around the globe. India,[120] Taiwan,[121] Australia,[122] Canada[123] and the UK[124] are just some of the countries in which reverse mortgages are being promoted as a way for seniors to provide for themselves financially as they age. If the trends in other countries follow the experience in the United States, there will be important opportunities for incorporating more global consumer protections for all reverse mortgage borrowers.

SUMMIT DOCUMENT 10 (2010), *available at* http://media.seoulsummit.kr/contents/dlobo/E2._Seoul_Summit_Document.pdf.

[120] *New Reverse Mortgage Plan May Have More Takers*, BUSINESS LINE, Mar. 16, 2010, http://www.thehindubusinessline.com/2010/03/17/stories/2010031752250600.htm.

[121] *Equity Release Plan to be Worked Out in Second Half of 2010*, FOCUS TAIWAN, Mar. 6, 2010, http://focustaiwan.tw/ShowNews/WebNews_Detail.aspx?Type=aECO&ID=201003060013.

[122] Wouter Klijn, *Reverse Mortgage Growth Continues Slowdown*, INVESTOR DAILY, May 31, 2010, http://www.investordaily.com.au/cps/rde/xchg/id/style/9316.htm?rdeCOQ=SID-0A3D9633-1732674E.

[123] *Investigate All Your Options*, THE CALGARY HERALD, Apr. 17, 2008, http://www.canada.com/calgaryherald/news/neighbours/story.html?id=65a919c2-be13-4b93-986c-2ca7bad36a7e. *See also* L'UNION DES CONSOMMATEURS, THE REVERSE MORTGAGE: FOR AN OPTIMUM CONTROL (2007) (on file with authors).

[124] *See* L'UNION DES CONSOMMATEURS, *supra* note 123, at 12-17 (discussing reverse mortgages in the UK).

Reverse Mortgage Tips for Consumers

If you need cash, consider alternatives to a Reverse Mortgage first.

Seniors are being told that having a reverse mortgage ends their financial worries. This is not altogether true. Despite the claim that the borrowers don't have to pay back the loan until they either die or permanently move out of the house, there are ongoing financial obligations that seniors need to keep in mind. Before depleting this last major asset through a reverse mortgage, make sure that this finite amount will be enough to meet your financial needs for the future. Would-be borrowers must think about how much money they will still be paying in continuing expenses once they have a reverse mortgage.

Borrower Beware-Continuing Expenses with Reverse Mortgages

- The borrower needs to stay current on all payments owed for property taxes, homeowners' insurance and, if applicable, all homeowners' association fees.
- The borrower is also obligated to adequately maintain the home or the loan may be called, for example, if the borrower cannot repair a leaky roof, wood rot or termite infestation.
- If the senior defaults on the loan, there may be a foreclosure (Borrowers with reverse mortgages can and do experience foreclosures).

Alternatives to Reverse Mortgages

Explore eligibility for less expensive programs or benefits

- Reverse mortgages are very expensive loans, and as such, they should be considered only as a last resort. Before considering a reverse mortgage, a senior should first determine if he or she qualifies for less expensive programs that offer monetary assistance or cost-cutting benefits. These programs include Supplemental Security Income (SSI), Medicaid, prescription drug discount programs, energy and telephone discount programs, City and County grants and low-cost home improvement loans (sometimes called "single purpose" loans), state property tax postponement programs, In-Home Supportive Services, and Veterans pensions to pay for in-home care.
- For a complete list of reverse mortgage alternatives by state, go to http://www.hecmresources.org/hecmresources/states/state_index.cfm

Family Financing: A win-win

- Seniors should also consider whether an inter-family loan might be better for their situation. In an inter-family loan, a family member or family members advance money to the senior instead of having a bank do the lending. If a senior has family members who are able and willing to consider such an arrangement, the senior's home equity can be used as collateral for this "private reverse mortgage" arrangement. The forwarded money, with interest, is tracked and recorded. When it comes time to sell the home, the investors are able to regain their contributions along with the interest it earned.

- There are several advantages to inter-family loans over the conventional reverse mortgage. First, the costs associated with family investors are typically a fraction of what they would be from an institutional lender. A successful inter-family loan would mean: 1) the senior can stay in the home; 2) the family investors have a secure loan that produces interest, and 3) when it comes time to sell the home, the senior would have preserved more of the home equity to share with the heirs then they otherwise would have if the senior had gone to a bank for the loan. As a practical matter, it is in the ultimate financial interest of the senior and the would-be heirs to preserve the inheritance rather than having the senior's home being sold in order to pay back an expensive reverse mortgage loan.

- The first step in getting started would be for the senior to talk to his or her adult children and discuss how much money the senior requires. If it is a manageable sum for the would-be investors, then a contract can be drawn up to clarify the terms and to protect those investors. Each investor's contribution would be tracked on a spreadsheet along with the calculated interest. A senior should contact an estate planning attorney or a Certified Public Accountant (CPA) to set up the necessary paperwork. The setup costs associated with this would be a small fraction compared to the thousands of dollars required to start a reverse mortgage.

Counseling — Advice for Potential Reverse Mortgage Borrowers

- Attend a face-to-face counseling session with a local HUD counselor rather than the phone counseling that is permitted. At this time, the only state that requires face-to-face counseling is North Carolina. http://www.nccob.org/NR/rdonlyres/FA81D3F6-32EF-4BDD-902E-906BE1743634/0/RVMLendercounselingletter.pdf

- Do not rely on HUD counseling alone to determine whether a reverse mortgage is appropriate for your needs. Either before or after meeting with a HUD-approved counselor, meet with either a Certified Financial Planner (CFP) or Certified Public Accountant (CPA), and/or with an elder law attorney before deciding on any reverse mortgage. Use this opportunity to discuss personal financial goals in more depth while obtaining specific advice regarding potential options to--or information about--appropriate reverse mortgage products.

- To find local counselors in their area, seniors should

  consult: https://entp.hud.gov/idapp/html/hecm_agency_look.cfm

  or contact the AARP Foundation at 1-800-209-8085