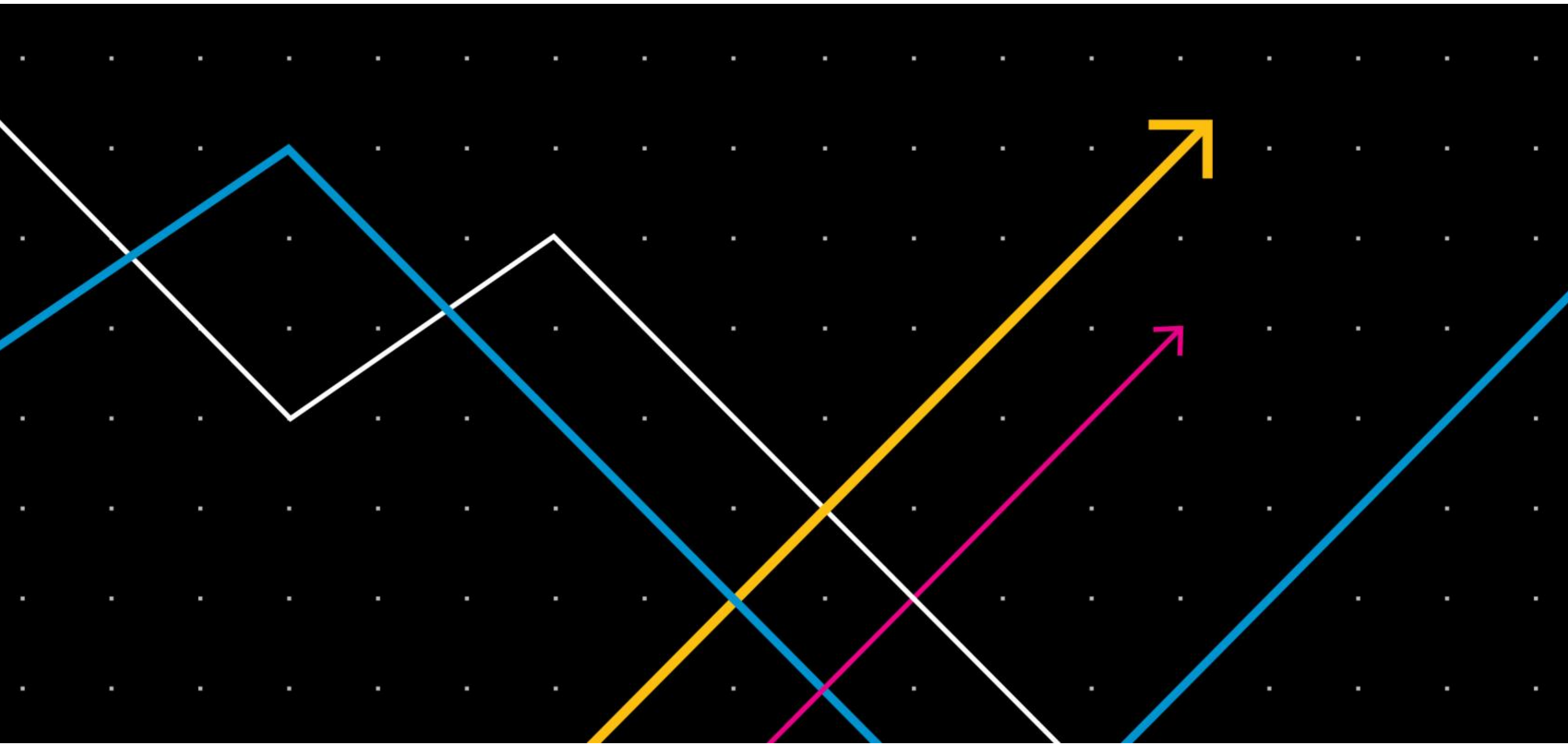

RESEARCH REPORT

Seniors’ Access to Home Equity

Identifying Existing Mechanisms and Impediments to Broader Adoption

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February 2017

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Acknowledgments

This report was funded by Fannie Mae. We are grateful to them and to all our funders, who make it possible for Urban to advance its mission.

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The authors would like to thank Pat Simmons, Stephanie Moulton, Ellen Seidman, and participants in the October roundtable, "Impediments to and Opportunities for Meeting Retirement Needs by Tapping into Home Equity," for helpful comments and suggestions.

Seniors’ Access to Home Equity

Introduction

Many Americans express concern about financial security in retirement. The recent rebound in the housing and equity markets notwithstanding, only half of American workers say they are confident about having enough money saved for retirement (Helman, Copeland, and VanDerhei 2015). Similarly, in Fannie Mae’s National Housing Survey® (NHS) of homeowners ages 55 and older conducted in the second quarter of 2016,[1] 37 percent of respondents were either somewhat concerned (26 percent) or very concerned (11 percent) about their financial situation in retirement.[2] Worries about retirement security stem from several factors, including social security changes that shrink the share of preretirement earnings replaced by the program (Munnell and Sundén 2005), rising medical and long-term-care costs (Johnson and Mommaerts 2009, 2010), student loan burdens, and the shift from employer-sponsored defined-benefit pension plans that guarantee lifetime income to 401(k)-type defined-contribution plans whose account balances depend on employee contributions and uncertain investment returns (Munnell 2014; Munnell and Sundén 2005). In addition, increased life expectancies require retirement savings to last longer. Many studies predict that under current policies and practices, the next generation of retirees may see their living standards fall during old age (Butrica, Smith, and Iams 2012; Favreault et al. 2012; Munnell, Hou, and Webb 2014; VanDerhei 2011).

But there may be a way to prevent that prediction from becoming reality. Current and future retirees could improve their living standards and financial security by liquefying a portion of their home equity to supplement their retirement income. Seniors have a higher homeownership rate and are more likely to be mortgage free than the general population. According to the US Census Bureau, the homeownership rate for seniors ages 65 and older was 79 percent in the third quarter of 2016. In contrast, the overall US homeownership rate was 63.5 percent. Further, roughly two-thirds of homeowners ages 65 and older own their home without a mortgage. Extracting home equity would allow these households to access liquidity and smooth consumption without the substantial costs and disruption of selling and downsizing (Hurst and Stafford 2004). For lower-income retirees or those who are financially burdened, tapping home equity could obviate the need to cut spending on essentials, such as food, health, and medicine. Higher-income households could leverage equity to improve in-home safety and mobility by installing senior-friendly equipment (e.g., stair lifts, ramps, and grab bars) or pay for other home improvements.

Home equity has the potential to enhance retirement security because the homeownership rate generally exceeds ownership rates for most financial assets. According to the Federal Reserve's 2013 Survey of Consumer Finances, 65.2 percent of American households owned their primary residences, but only 49.2 percent had retirement accounts, 19.2 percent had cash-value life insurance policies, 13.8 percent had stocks, and 10 percent had savings bonds (Bricker et al. 2014).

More importantly, homes are the most valuable financial asset owned by Americans. National housing wealth owned by Americans dwarfs the value of other assets. The national average net worth per owner-occupied housing unit in 2015 was over $150,000 across all age groups, $175,000 for 60- to 64-year-olds, $190,000 for 65- to 69-year-olds, and $205,000 for those over age 70 (Li and Goodman 2016).[3] Similarly, according to the 2013 Survey of Consumer Finances, the median value of the primary residence for homeowners was $170,000. In contrast, the median value for US retirement accounts was $59,000, $8,000 for cash-value life insurance, $27,000 for stocks, and $1,000 for savings bonds. Not surprisingly, Fannie Mae's NHS showed that the average maximum loan amount homeowners ages 55 and older thought they could get approved to borrow against their homes was $145,000 (the median amount was $94,000), a reflection of how much housing wealth Americans own. Owner-occupied households ages 65 and older could have increased their 2012 median income 40 percent by selling their home and annuitizing the proceeds (Butrica and Mudrazija 2016).

The nationwide aggregate value of Americans' primary residence home equity is also staggering. Table 1 shows the dollar volume of accumulated home equity (net of debt secured by the house) for American homeowners by age group in 2015. The first take-away is that households possess an aggregate home equity of over $11 trillion. Forty percent of this equity, or $4.4 trillion, is held by homeowners ages 65 and older. Not all of this equity is extractable. Even homeowners without a mortgage cannot cash out 100 percent of their home value without a sale. The third and fourth columns in table 1 adjust for lender limits on the maximum amount of a mortgage, compared with the home's value. The third column assumes a post–equity extraction combined loan-to-value ratio (CLTV) of 85 percent, which yields extractable equity of $3.6 trillion for homeowners ages 65 and older and $8.5 trillion for all age groups. The last column assumes a more conservative CLTV of 75 percent, but still yields an extractable equity of $3.1 trillion for those over age 65 and $7 trillion for all age groups. These findings strongly suggest that home equity not only has the potential to be a major source of financial security for households, but also represents a huge untapped market for home equity lending.

TABLE 1

Net Housing Wealth for All Owner-Occupied Housing Units, by Age Group, 2015

Billions of dollars

Age group	Net housing wealth ($)	Wealth accessible up to 85% CLTV ($)	Wealth accessible up to 75% CLTV ($)
18–29	159	107	83
30–39	748	479	345
40–49	1,660	1,172	894
50–59	2,678	2,051	1,666
60–64	1,428	1,135	950
65–69	1,348	1,089	923
≥70	3,008	2,494	2,158
Total	**11,030**	**8,527**	**7,018**
65 and older	**4,356**	**3,582**	**3,080**

Source: Li and Goodman (2016).
Note: CLTV = combined loan-to-value ratio.

Table 2 shows the results of an analysis similar to that shown in table 1, except the dollar amounts are replaced by the number of homeowner households (i.e., owner-occupied housing units). Currently, the United States has over 73 million homeowner households. Roughly 30 percent, or 22 million of these homeowners, are ages 65 and older. When these numbers are adjusted to exclude households with a current CLTV over 85 percent and 75 percent, the number of households still exceeds 50 million, while those 65 and older add up to about 20 million. Once again, this points to a significant market opportunity for increasing home equity lending.

TABLE 2

Owner-Occupied Housing Units with Extractable Equity, by Age Group, 2015

Age group	Housing units	Units with equity accessible up to 85% CLTV	Units with equity accessible up to 75% CLTV
18–29	2,593,788	1,566,268	1,145,027
30–39	9,477,887	5,909,133	4,253,343
40–49	13,863,045	10,031,195	8,308,589
50–59	17,403,755	14,145,581	12,775,687
60–64	8,169,867	7,005,120	6,559,898
65–69	7,105,658	6,274,613	5,965,109
≥70	14,672,714	13,776,590	13,441,880
Total	**73,286,714**	**58,708,498**	**52,449,533**
65 and older	**21,778,372**	**20,051,203**	**19,406,989**

Source: Li and Goodman (2016).
Note: CLTV = combined loan-to-value ratio.

In spite of this wealth and the availability of multiple equity extraction mechanisms—primarily Home Equity Conversion Mortgages (HECMs), closed-end home equity loans, Home Equity Lines of Credit (HELOCs), and cash-out refinance—few retirees tap into home equity, and most who do typically wait until they experience a serious financial shock, such as substantial medical expenses or the death of a spouse (Poterba, Venti, and Wise 2011; Smith, Soto, and Penner 2009; Venti and Wise 2004). Indeed, a whopping eighty percent of homeowners ages 55 and older surveyed in Fannie Mae's NHS said they were "not at all interested" in tapping home equity in retirement.

The analysis presented in this report suggests there are multiple reasons home equity extraction remains low. The single most important one, by far, is limited demand. There are two reasons for this:

- First, seniors tend to have a general desire to stay financially conservative and avoid debt in old age. This behavior could be driven by their desire to leave a bequest or save for emergency expenses or for long-term-care costs. Others may be worried about losing their home.
- Second, continued improvements in health and medicine allow more seniors to work and earn well into old age, reducing the need to depend on debt, including equity extraction.

Beyond these behavioral factors are structural impediments to equity extraction related to poor financial literacy, product complexity, high costs, and fear of misinformation and fraud, particularly with reverse mortgages. The recent postcrisis tightening of credit has also affected home equity lending. As varied as these impediments to equity extraction are, they all ultimately lead to one outcome: high levels of net home equity and extractable housing wealth (table 1).

This report offers several recommendations to ease barriers to equity extraction. Most of them are geared toward addressing structural impediments, as opposed to changing seniors' conservative attitudes toward debt or their long-held preferences and beliefs. These recommendations include the following:

- Improving reverse mortgage financial literacy by introducing the product to individuals at a younger age. This could be achieved by incorporating housing wealth and reverse mortgages into retirement planning. Reverse mortgage literacy can also be improved through enhancements to HECM counseling.
- Reducing the cost of reverse mortgages by simplifying product design, phasing out rarely used product options, fostering competition between reverse mortgage lenders, and reducing borrowing costs by improving the liquidity of HECM mortgage-backed securities (HMBS).

- Improving access to credit by reducing HECM premiums in a risk-neutral manner, such as by commensurately reducing the maximum amount that can be borrowed. This could be achieved by reintroducing a modified version of HECM Saver. In the longer run, stakeholders could also explore new alternatives. Shared appreciation mortgages (SAMs) and converting a portion of the home into a rental are two opportunities.

This report is the second in a series that studies the potential for using home equity to improve retirement financial security. The first report showed who taps home equity, how, and how equity extraction patterns vary by race, ethnicity, education, and income (Butrica and Mudrazija 2016). This report digs deeper into existing equity extraction mechanisms, identifies barriers to equity extraction, and offers recommendations to improve seniors' access to equity.

The next section evaluates each equity extraction mechanism in detail by analyzing recent trends in usage and effectiveness along such dimensions as costs, eligibility guidelines, repayment terms, and ease of use. Relying on a literature review and the expertise of Urban Institute researchers, the subsequent section analyzes these product characteristics to identify key barriers and impediments to equity extraction. Lastly, the report offers recommendations that could reduce these barriers.

Current Mechanisms for Accessing Equity

Housing is different from most other assets because of its dual function as a financial asset and consumption good. Because most households buy a home to live in and raise a family, they may not view it as a financial asset. Elderly people conventionally are classified as income poor but asset rich (Rowlingson 2006). Therefore, it becomes interesting to explore whether people, especially the elderly, consider the wealth stored in their homes as a financial resource to be tapped in old age (Naumanen and Ruonanvaara 2010).

The financial services industry has developed various products to enable households to extract equity from their home without selling it. These products can be broadly classified into two types:

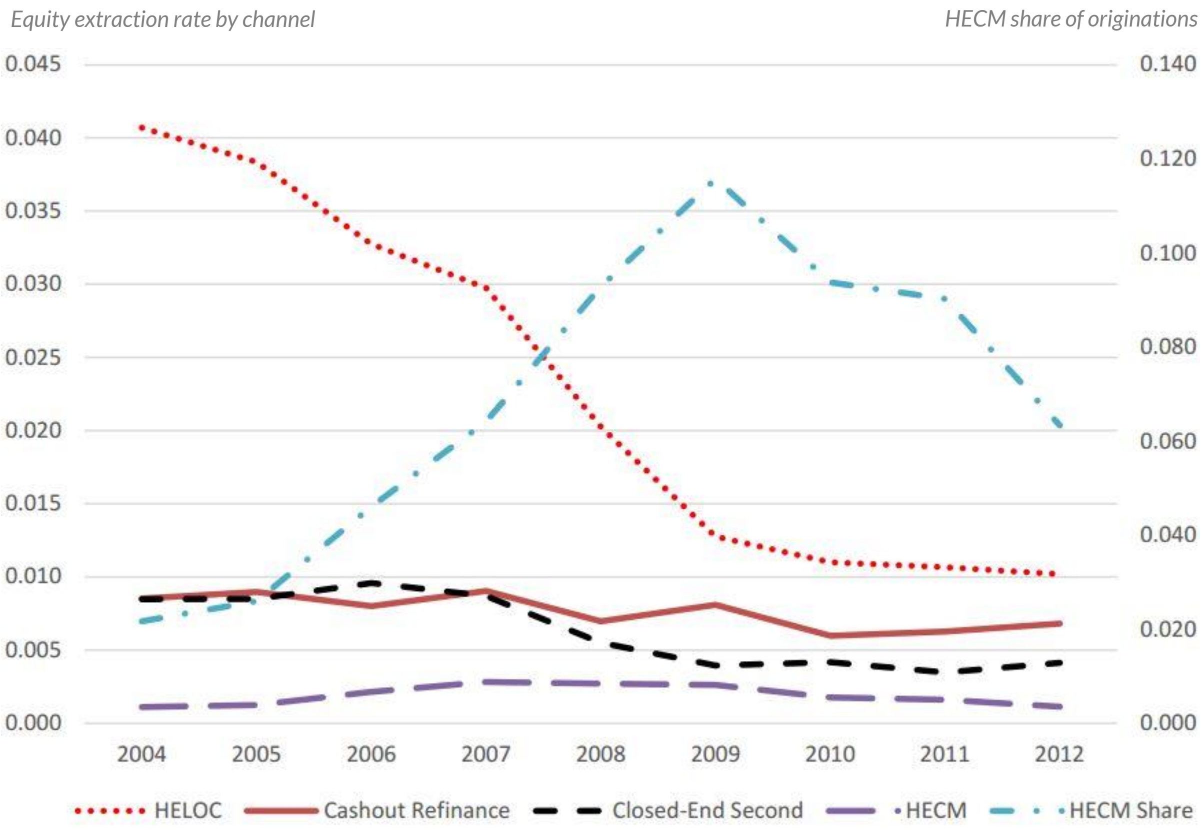
- **Reverse mortgage** products allow households to borrow against their homes without making monthly payments. The principal and interest are due when the house is sold, the last surviving spouse dies, or the borrower fails to keep up with the mortgage terms. There are two types of reverse mortgages. The more popular, by far, is the government-backed reverse mortgage called the Home Equity Conversion Mortgage, which is originated by private lenders and insured by the Federal Housing Administration (FHA). This insurance protects lenders against the risk that proceeds from the sale of the house at loan maturity will fall short of the amount owed. The second type is a fully private product not insured by the government, in which private lenders fully retain the risk.

- **Forward home equity lending** products also allow households to borrow against the equity in the home, but require a monthly payment over the term of the mortgage. These are commonly of three types: Home Equity Lines of Credit, closed-end home equity loans (also called closed-end seconds), and cash-out refinances.

These two mechanisms for accessing equity differ from each other in basic product characteristics and in how borrowers use them. Forward equity lending tends to be more popular among higher-creditworthy borrowers, while HECMs are more common among the less creditworthy because these borrowers typically have limited means for making monthly payments and are less likely to be approved for forward mortgages. Moulton and coauthors (2015) showed the differences in consumer usage across various equity extraction channels. Using Federal Reserve Bank of New York/Equifax Consumer Credit Panel sample data and the US Department of Housing and Urban Development's (HUD) HECM origination data, the authors calculated the equity extraction origination rate for each channel as a proportion of the total population ages 62 and older from 2004 to 2012 (figure 1, left y-axis).[4] Each of the four equity extraction channels had an origination rate of 4 percent a year or less over this period, with only HELOCs having a rate exceeding 1 percent. Such low utilization rates across channels demonstrate how uncommon equity extraction is among seniors. This conclusion is supported by Butrica and Mudrazija's (2016) related finding that the share of owner-occupied households ages 65 and older who potentially extracted home equity in 2012 was low.

FIGURE 1

Mean Equity Extraction Origination Rate as a Proportion of Population Ages 62 and Older



Source: Moulton and coauthors (2015).
Notes: HECM = Home Equity Conversion Mortgage. HELOC = Home Equity Line of Credit.

Other Mechanisms for Equity Extraction

A third option for liquefying home equity that does not require borrowing is selling the home; buying a smaller, cheaper home or renting; and pocketing the difference. This "selling and downsizing" strategy, however, has downsides that reduce its appeal. The round-trip process of selling one home and buying another can be time consuming, involve high transaction costs, and cause temporary disruption to daily life, especially for seniors with health issues. Most seniors also want to age in place (Munnell, Soto, and Aubry 2007; Venti and Wise 2004). Furthermore, recent survey data from Freddie Mac indicate that, "relatively few older [ages 55 and older] homeowners think it is very important to downsize in their next move" (Becketti and Yannopoulous 2016, 6).

Lack of appetite for selling and downsizing is also supported by Fannie Mae's NHS, albeit with an apparent contradiction. Asked when they expect to move next, 65 percent of homeowners ages 55 and older said "never." Yet when the same respondents were asked about their preferred method for taking out equity, a plurality (47 percent) favored selling and downsizing. Only 16 percent favored home equity loans and lines of credit, 6 percent favored reverse mortgages, and 4 percent were in favor of cash-out refinancing. Thirty-two percent were unsure. One possible explanation for the contradiction is that seniors' desire to avoid debt might be stronger than their desire to age in place. In other words, seniors may prefer to age in place only if it does not involve borrowing.

The desire to age in place is also backed by evidence showing that the large baby boomer generation is not reducing housing consumption even though many are retiring or experiencing life changes that might precipitate downsizing. The percentage of baby boomers living in detached single-family homes increased slightly from 2006 to 2012, even though the percentage of baby boomer households with at least one child declined significantly over the same period (Simmons 2014). This trend holds true for all boomers in aggregate and for older boomers born between 1946 and 1955, who are unlikely to have young children in the home and who have begun to retire in substantial numbers.

Possible reasons retirees might want to stay in their homes include a deep-rooted connection to the home or the community, proximity to friends or family, and protection from the rent increases seniors could incur if they sold their home and entered the rental market. Even though selling and downsizing allows seniors to extract equity, seniors are more interested in aging in place. The relative attractiveness of selling and downsizing is also diminished by the presence of substitutes (e.g., reverse mortgages and forward home equity lending products) that allow seniors to achieve a similar financial outcome with less disruption.

A final avenue through which homeowners could consume equity, albeit indirectly, involves underspending on home maintenance. The ensuing degradation in the home's market value, realized at the time of sale, should have the same economic effect as equity extraction. Although literature about this is scarce and dated, one study confirms that older homeowners tend to spend less on maintenance and repairs than younger homeowners. Using American Housing Survey panel data for homes that were owner occupied in 1985 and observed until 2001, Davidoff (2004) concluded that household heads ages 75 and older spent an average of $1,100 a year less on routine home maintenance and repairs than younger household heads. More importantly, the study showed that older homeowners experience weaker house price appreciation than younger households of similar homes in the same geographies by roughly 3 percent a year.

But it is worth pointing out that equity extraction via reverse mortgages was extremely rare during the 1985 to 2001 period (figure 2) covered by Davidoff (2004). Seniors who wanted to age in place had fewer options for equity extraction and were more likely to cut back on maintenance spending to boost their nonhousing consumption. But with reverse mortgages gaining popularity, today's seniors have better access to equity extraction products and thus less of a need to cut back on home maintenance.

Reverse Mortgages

Reverse mortgages allow seniors to borrow against the value of their home. Unlike a traditional forward mortgage, no loan payments are made until the house is sold or the last surviving spouse dies. Reverse mortgages were introduced in the early 1960s to help older homeowners age in place. An essential characteristic of reverse mortgages is that the amount owed increases with time, in contrast to the decreasing loan balance typical of forward mortgages. The absence of monthly payments for reverse mortgages results in compounding interest, which is added to the principal amount each year.

THE FHA'S HOME EQUITY CONVERSION MORTGAGE

The Home Equity Conversion Mortgage is a reverse mortgage product originated by private lenders, but insured by the FHA. It allows borrowers who are at least 62 years old to convert equity in their home into a one-time lump-sum payment, a line of credit, a stream of annuity payments, or a combination of these options. Eligibility guidelines require borrowers to occupy the property as their primary residence; have the financial resources to pay for property taxes, insurance, and home maintenance; and undergo HECM counseling. In recent years, HUD has also introduced rules that limit the amount that can be borrowed at the time of closing. In general, HECM underwriting rules were strengthened after the financial crisis in response to the heavy losses FHA's Mutual Mortgage Insurance Fund sustained because of the legacy HECM portfolio. These changes and their impact on HECM volumes are discussed later.

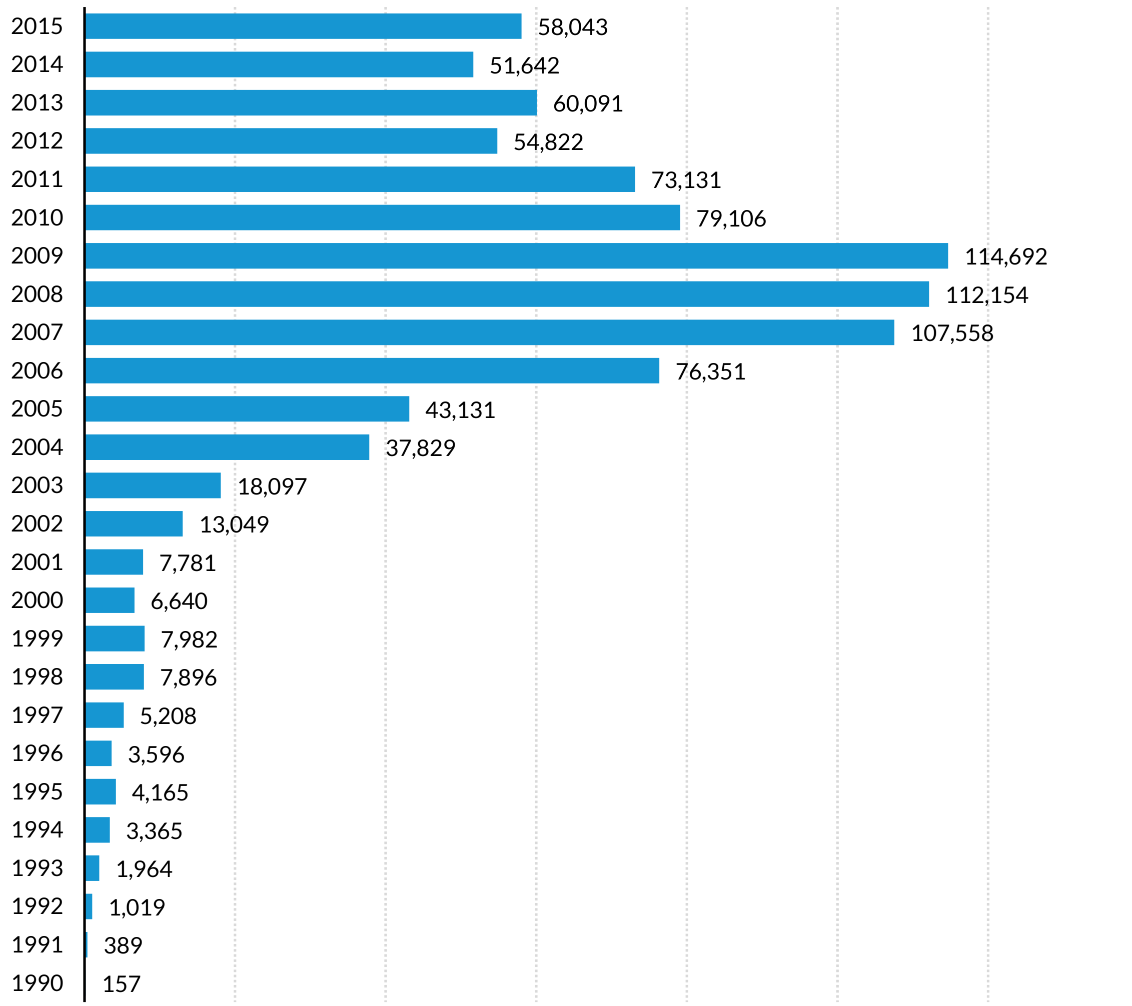
Although HECMs do not require monthly payments, borrowers are responsible for the timely payment of real estate taxes and mandatory flood and homeowner insurance premiums. Failure to do so constitutes "technical default," causing the mortgage to become due and payable. Inability to pay off the mortgage could lead to foreclosure. When the homeowner no longer occupies the home (upon death or home sale), the principal, interest, HECM premiums, and other charges and fees must be fully repaid. Any remaining equity can be transferred to heirs. If the house value at maturity falls short of the amount owed to the lender, the FHA's insurance covers the deficit, protecting lenders against losses. The FHA's insurance also protects borrowers from lender inability to disburse required loan proceeds (e.g., under the line of credit or annuity options).

Home Equity Conversion Mortgages are offered as fixed-rate or adjustable-rate mortgages, but the differences between the two extend beyond just the rate type. The fixed-rate product is available only as a closed-end loan under which funds are disbursed as a lump-sum payment. The adjustable-rate option allows borrowers to choose a lump-sum payment, line of credit, annuity, or a combination of the three. For adjustable-rate HECMs, interest accrues only for the portion of the initial principal limit the borrower draws.[5] This greater flexibility, however, comes at the risk that interest rates could rise over the term of the loan, increasing the cost to the borrower.

In spite of being introduced several decades ago, reverse mortgage volumes remained tiny until the early 2000s. Home Equity Conversion Mortgage endorsements began growing substantially in the early- to mid-2000s (figure 2) as house prices rose rapidly, peaking at 114,700 loans in 2009. As house prices fell during the housing bust, the endorsement count dropped sharply to about 55,000 in 2012. Home Equity Conversion Mortgage dollar origination volumes tell a similar story (figure 3). After peaking at roughly $22 billion in 2009, the initial principal limit was cut by more than half by 2012 and has remained between $9 to $10 billion a year since then.

FIGURE 2

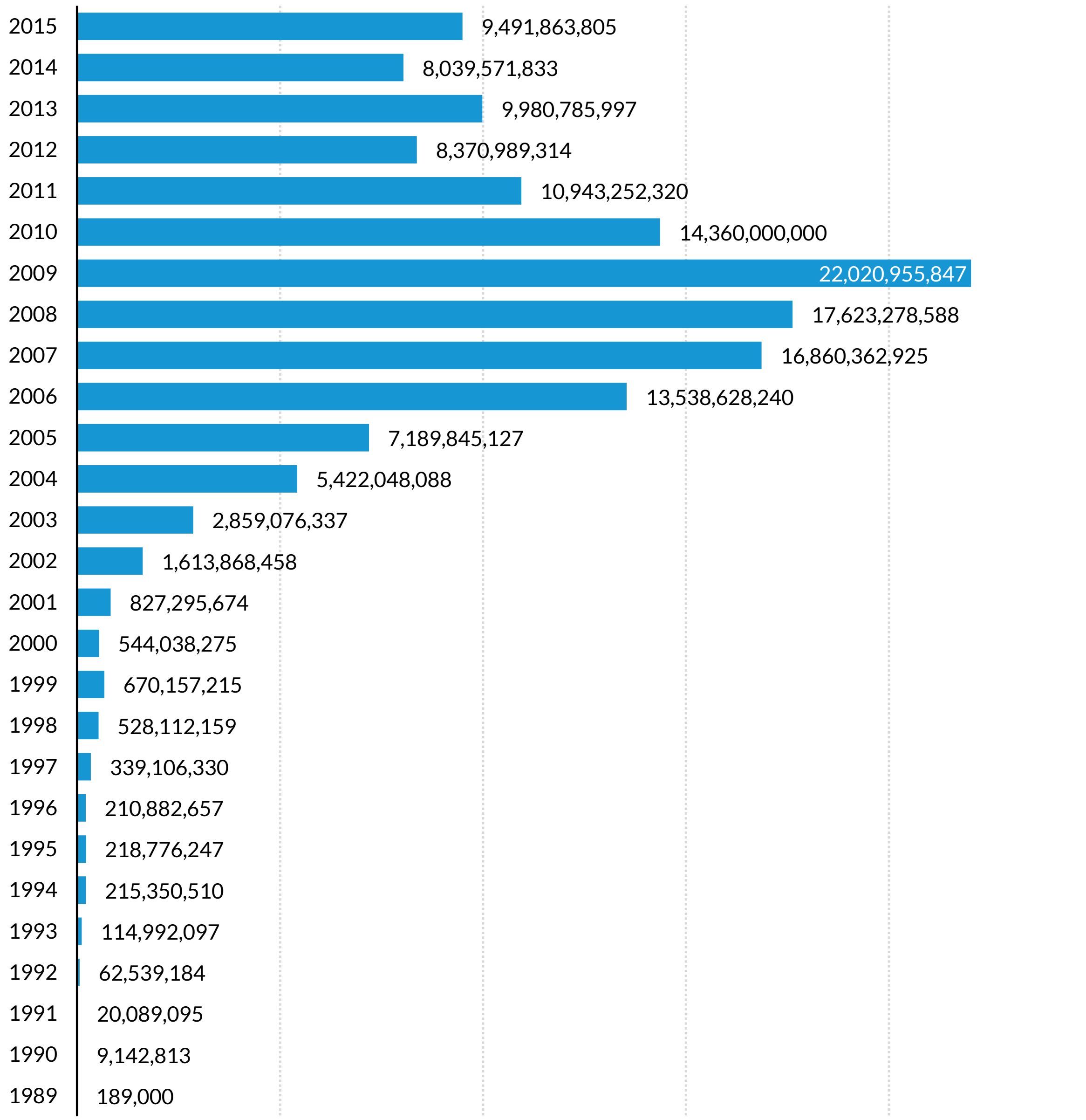
HECM Endorsement Count by Fiscal Year (Number of Loans)



Source: Urban Institute calculations based on US Housing and Urban Development HECM endorsement data.
Note: HECM = Home Equity Conversion Mortgage.

FIGURE 3

HECM Initial Principal Limit Endorsed by Year (Dollars)



Source: Urban Institute calculations based on US Housing and Urban Development HECM endorsement data.
Note: HECM = Home Equity Conversion Mortgage.

Four types of costs are associated with HECMs. The borrower can finance these costs into an HECM loan (which reduces loan proceeds) or pay them at the time of closing.

1. **HECM mortgage insurance premiums** (up-front and annual): The up-front mortgage insurance premium generally equals 0.5 or 2.5 percent of the appraised home value, depending on the disbursement option selected. Borrowers who withdraw more than 60 percent of their initial principal limit in the first 12 months are charged 2.5 percent, while those who draw 60 percent or less are charged 0.5 percent. The FHA also charges an annual insurance premium for the life of the loan, which equals 1.25 percent of the outstanding loan balance.
2. **Third-party charges**: Closing costs from third parties can include an appraisal, title search, homeowners insurance, surveys, inspections, recording fees, and taxes.
3. **Origination fees**: The origination fee compensates the lender for processing the HECM loan.
4. **Servicing fee**: Lenders charge a monthly servicing fee to cover the cost of mailing account statements, ensuring borrower compliance with loan terms (e.g., home maintenance), and payment of real estate taxes and homeowner insurance premiums. The servicing fee is $30 or $35 depending on the loan option and is typically added to the amount owed.

PROPRIETARY REVERSE MORTGAGES

Older wealthier homeowners with substantial equity in their homes have historically had the option to obtain a proprietary reverse mortgage that is not government insured and does not protect lenders from the risk of loss. Although proprietary reverse mortgages have been available for decades, the market for these mortgages was always tiny and has all but disappeared after the housing bust.

Proprietary and HECM reverse mortgages, though similar along such dimensions as age requirements and no monthly payment, have critical differences. Proprietary reverse mortgages generally carry higher interest rates, allow lower loan proceeds as a percentage of home value, and offer limited consumer protection. Moreover, under HECM rules, HUD protects borrowers from lender inability to disburse payments over the loan term. Finally, HECM loans require mandatory borrower counseling, but the proprietary version does not.

Despite these barriers, proprietary reverse mortgages appeal to borrowers for a couple of reasons. The loan amount under HECM is limited by the home's appraised value and by the FHA loan limit ($625,000). Wealthier homeowners whose home values significantly exceed the loan limit but want to borrow more cannot do so through HECM. Proprietary reverse mortgages can be useful here. Lending to borrowers with higher home values—who typically have better credit profiles—has appealed to lenders in the past despite the absence of government insurance because of the potential for greater profits. Proprietary reverse mortgages can also appeal to borrowers in need of smaller amounts of cash or to those who need short-term financing. Because the up-front HECM premium is calculated as a percentage of the appraised home value, regardless of loan amount or the term, HECMs can be expensive for these borrowers, creating another opportunity for proprietary reverse mortgage lending.

Even though proprietary reverse mortgages were previously available, this market has almost disappeared in recent years. Before the housing crisis, proprietary reverse mortgages were funded through private mortgage securitization facilitated by Wall Street or through balance sheet lending by large national lenders. But both executions stopped as capital markets investors shunned these securities postcrisis and large lenders exited the reverse mortgage business. These developments and their impact on reverse mortgage lending are discussed later.

Forward Equity Lending: Home Equity Lines of Credit, Home Equity Loans, and Cash-Out Refinances

A Home Equity Line of Credit (HELOC) is an agreement between a lender and a borrower under which the lender agrees to lend up to a certain amount based on the value of the homeowner's equity over a fixed duration. HELOCs generally have a draw period followed by a repayment period. During the draw period, a borrower has revolving access to approved funds and is often required to make interest payments only. During the repayment period, a borrower can no longer make additional draws on the line, and the outstanding principal is either due immediately in a balloon payment or is repaid over the remaining loan term. HELOCs are similar to credit cards in that borrowers have a preapproved spending limit that they can tap when needed. But unlike credit card debt, which is unsecured, HELOCs are secured by homeowner equity and present less risk to lenders. Consequently, HELOC interest rates tend to be lower than rates on credit card debt. HELOC fees can include an origination fee, an annual fee, and an appraisal fee to verify the house's market value. HELOCs typically have adjustable interest rates that depend on when the borrower draws the funds, rather than when the HELOC was approved.

Home equity loans, unlike HELOCs, are closed-end loans. The full loan amount is disbursed at the time of closing, and the loan is repaid via monthly payments over a fixed term. Many of the costs of obtaining a home equity loan are similar to those incurred when obtaining a HELOC. These include an appraisal fee to assess home value, origination fees, and closing costs.

One important benefit of a closed-end home equity loan over a HELOC is that a home equity loan usually carries a fixed interest rate, which makes monthly payments predictable so consumers know their repayment costs. That said, HELOCs are generally offered to borrowers with high credit scores and higher income and assets, and these borrowers tend to be better prepared financially to weather the risk of rising rates. Interest payments for home equity loans and HELOCs are income tax deductible, which reduces the cost of borrowing. Home equity loans and HELOCs also have lower “all-in costs” than reverse mortgages when measured over the life of the loan (discussed in the next section).

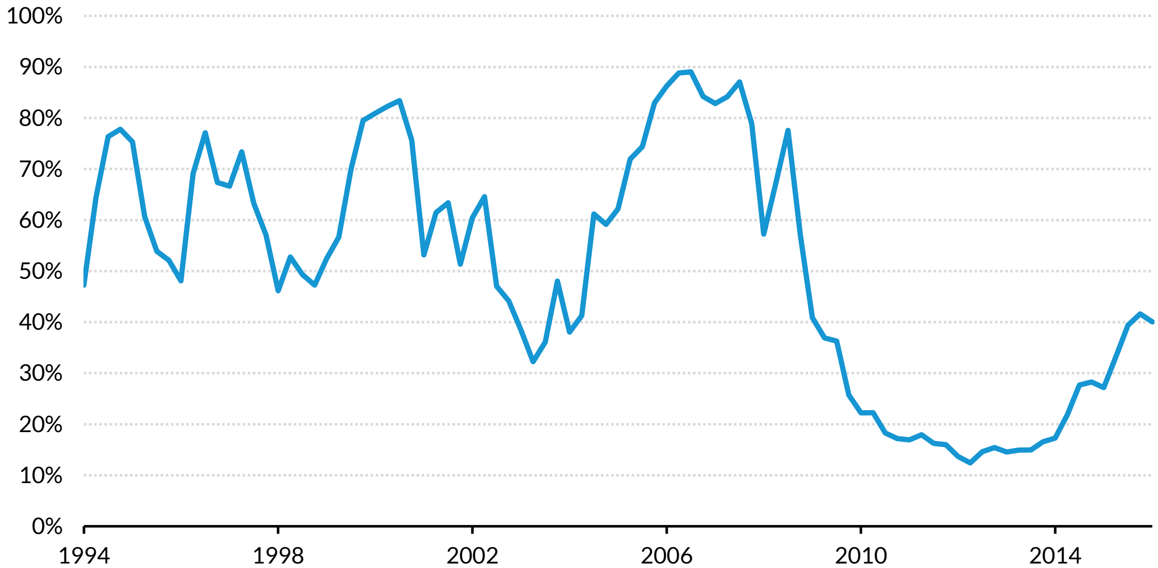
A third form of forward equity extraction is cash-out refinance. A cash-out is a special type of refinance of the first mortgage in which the new (post-refinance) loan amount is greater than the loan amount outstanding before refinance. The difference is paid to the borrower in cash and can be used for consumption, investment, or any other purpose. This mechanism allows homeowners to cash out a portion of their home’s equity at the time of refinance, resulting in a single mortgage with a single monthly payment, rather than multiple loans and payments that result from HELOCs or home equity loans.

Households extracted an estimated $1.9 trillion in home equity through cash-out refinance between 1991 and 2005 (Greenspan and Kennedy 2008). Closing costs and preexisting home equity debt repaid at the time of the cash-out totaled $260 billion and $565 billion, respectively. The net “take home” cash was about $1.03 trillion. Cash-out refinances became more popular during the housing bubble, as a higher percentage of refinance borrowers chose to borrow more than the loan amount outstanding at the time of the refinance.

According to Freddie Mac’s cash-out refinance report for the second quarter of 2016, the share of prime conventional refinances that resulted in a loan amount at least 5 percent greater than the original loan’s unpaid principal balance increased from 35 percent in 2003 to nearly 90 percent in 2006 as house prices rose (figure 4).[6] But the subsequent bust caused a sharp contraction in cash-out refinance activity. By 2012, the share had fallen to 10 percent, although by 2016, it had recovered to 41 percent, roughly in line with the 2003–04 level. Despite these increases, the volume of cash-out refinances remains small, averaging just $31 billion annually between 2010 and 2015,[7] indicating how rarely this vehicle is used.[8]

FIGURE 4

Cash-Out Refinance Share of Prime Conventional Refinances



Source: Freddie Mac quarterly refinance report for the first quarter of 2016.

Impediments to Equity Extraction

Despite the various mechanisms for accessing home equity, most equity held by seniors remains untapped. This section discusses the main reasons. Some of these impediments are behavioral and have to do with seniors' long-held values, beliefs, and attitudes, such as general risk aversion to debt in old age or the desire to save for emergencies or maximize wealth transfer to descendants by leaving a bequest. Other barriers include poor financial literacy and the fear of getting scammed, especially for reverse mortgages. Many structural impediments to equity extraction are caused by the postcrisis exit of large reverse mortgage lenders, inefficient product design, and the high cost of reverse mortgages. Finally, the aftermath of the financial crisis has witnessed an extraordinarily tight credit environment, which has affected the supply of credit across all equity extraction channels. These barriers to equity extraction can be broadly classified as follows:

- Limited demand
- Inadequate financial literacy
- High costs
- Insufficient credit availability

Limited Demand

An aversion to debt (driven by bequest motives and the desire to save for emergencies) and the presence of substitutes to borrowing (e.g., delaying retirement or working in retirement to supplement income from savings) affect seniors' demand for home equity extraction.

LEAVING A BEQUEST, AVERSION TO DEBT, SAVING FOR EMERGENCIES

The National Council on Aging indicates older homeowners are disinclined to liquidate housing wealth because they want to save it for making a bequest, paying for emergencies, or for nursing home expenses (Stucki 2005). Other seniors want to avoid debt for fear of losing their home. The Fannie Mae NHS supports these hypotheses. When asked about their main concerns regarding equity extraction in retirement, 36 percent of homeowners ages 55 and older stated they did not want to have debt, 19 percent wanted to save equity for heirs, and 10 percent wanted to save it for emergencies. Thirty percent said they did not need the money. Seniors' willingness to extract equity could also be affected by greater indebtedness. Recent cohorts of older Americans are more likely to carry housing debt into retirement and have higher levels of debt compared with previous retiree cohorts of the same age (Butrica and Mudrazija 2016). All things equal, indebted households are less likely to apply for or get approved for another mortgage.

The common thread connecting these behaviors is that they all ultimately lead to less demand for debt. This finding sheds light on why an overwhelming majority—80 percent—f homeowners ages 55 and older in Fannie Mae's NHS are "not at all interested" in tapping equity. An additional 10 percent were "not very interested." These findings somewhat echo Delgadillo, Stokes, and Lown's (2014) assertion that elderly homeowners with strong bequest motives decide against a reverse mortgage to preserve the wealth they prefer to leave to their estates. Other studies highlight homeowners' desire to save home equity for emergencies (Shan 2011).

Conventional wisdom suggests many older homeowners would be open to extracting equity to make major home improvements to facilitate aging in place. But according to a 2016 survey commissioned by Freddie Mac, 77 percent of homeowners ages 55 and older said they could "stay in their current residence for the rest of their lives without making major renovations" (Becketti and Yannopoulous 2016). Of the remaining 23 percent who said they would need to make renovations, 33 percent said they would tap savings and 19 percent said they could not make renovations. In other words, 52 percent of homeowners who thought they would need to renovate would not incur any home renovation debt. Forty-one percent indicated they would use some kind of debt (14 percent said they would use HELOCs, 12 percent would use bank loans, 8 percent would use cash-out refinance, 5 percent would use reverse mortgages, and 2 percent would borrow from family). Fannie Mae's NHS also revealed a lack of desire to tap any equity. Only 6 percent of homeowners ages 55 and older were either "somewhat" or "very interested" in tapping equity in retirement. But home improvement topped the list of purposes for tapping equity within this subgroup.

The most discouraging sign for the demand for equity extraction concerns reverse mortgages. Fannie Mae's NHS survey revealed a wide disconnect between seniors' awareness of reverse mortgages and their preference for using it. Although 49 percent of homeowners ages 55 and older said they were "familiar" with reverse mortgages, only 6 percent said they would "prefer" reverse mortgages to extract equity. Forty-seven percent were in favor of selling and downsizing, once again suggesting an aversion to debt. Sixteen percent said they would prefer home equity loans or lines of credit.

SENIORS ARE WORKING INTO OLD AGE

Even when seniors may desire additional cash, borrowing is hardly the only option. The labor force participation rate has been in a long-term decline for all age groups, except for those over age 55

(Toossi 2015). Although the participation rate for the 55-and-older age group is, not surprisingly, the lowest among all age groups, it is the only one to experience an increase in the last two decades. It increased from 30.1 percent in 1994 to 40 percent in 2014. Particularly interesting is the fact that this increase is broad based and holds true for younger (ages 55 to 64), middle-aged (ages 64 to 74), and older (ages 75 and older) seniors.

Reasons seniors may be working into retirement include increases in the full retirement age for social security benefit eligibility (Hewitt 2015), the increasing dominance of defined-contribution retirement plans as fewer employers offer defined benefit plans, and continued improvements in health, medicine, and longevity that allow older Americans to work longer than they could previously. Seniors who are working longer and earning well into retirement have less need to extract equity to meet their living expenses. This could partly explain Fannie Mae's NHS finding that 59 percent of homeowners ages 55 and older are "not at all concerned" or "not very concerned" about their personal financial situation in retirement. Those who work past traditional retirement age are also likely to have greater savings when they eventually stop working and, perhaps more importantly, fewer years to consume those savings, reducing the need to extract equity.

Overall, seniors seem to have a strong desire to stay financially conservative and avoid debt in retirement. This is partly because many seniors feel comfortable with their financial situation in retirement, are confident in their ability to use substitutes for equity extraction, or have other preferences and beliefs that lead them to avoid debt.

Inadequate Financial Literacy

Lack of financial literacy and inadequate financial planning for retirement are common issues faced by current and future retirees. Using 2004 Health and Retirement Study data, Lusardi and Mitchell (2007) found that 30 percent of early baby boomer households (in which at least one member was born between 1948 and 1953) reported they had not thought about retirement. Lack of planning was concentrated among less-educated respondents and minorities. Additionally, Adams and Lichtenberg (2014) showed that seniors tend to be more trusting and vulnerable and often have health problems (e.g., reduced vision, impaired hearing, or memory and cognitive disorders) that impair their ability to enhance their financial knowledge or comprehend complex financial products. Seniors are thus at a disadvantage when making important financial decisions. Inadequate financial knowledge, a common challenge for seniors, affects decisions about reverse mortgages more than it affects forward channels for three reasons.

REVERSE MORTGAGES ARE COMPLEX

Even though the first reverse mortgage in the United States was made 55 years ago, they are still poorly understood, in part because of their complexity. The aspect of reverse mortgages that consumers find the most difficult to grasp is the increasing loan balance (CFPB 2012). Many borrowers obtain reverse mortgages without fully understanding the ultimate cost of the loan, particularly because it requires no monthly payments. Reverse mortgage consumers are also confused by the myriad of options available. Borrowers can choose from a lump-sum amount, a line of credit, an annuity, or a combination of an annuity and a line of credit. Further, there are different types of annuities (term and tenure). Reverse mortgage borrowers also have to choose a fixed- or adjustable-rate mortgage.[9] Finally, they may need to decide whether to obtain an HECM or a proprietary reverse mortgage, although the proprietary market is almost nonexistent. Complex and unfamiliar concepts, including equity conversion, discourage borrowers from finding a suitable product (Chen 1973).

Forty-nine percent of homeowners ages 55 and older in Fannie Mae's NHS said they were "familiar" with reverse mortgages. But when this subset was asked to pick the most concerning aspect of reverse mortgages, only 9 percent cited "difficult to understand." Although this result suggests that reverse mortgage product complexity is not a major issue, 43 percent of the responses to this question were uncommitted (27 percent answered none of the above, 8 percent said don't know, and 8 percent selected "other"), 20 percent were afraid of getting scammed, 16 percent were worried about keeping their home, and 12 percent indicated reverse mortgages were costly. An unusually large proportion of uncommitted responses is perhaps a reflection of how poorly understood reverse mortgages are. Along these lines, Davidoff, Gerhard, and Post's (2015) survey of US homeowners ages 58 and older revealed a wide lack of understanding of reverse mortgages among the general population.

REVERSE MORTGAGES ARE MORE VULNERABLE TO MISINFORMATION AND SCAMS

Misleading and aggressive advertising often make it difficult for seniors to understand reverse mortgages holistically. Making matters worse, increased misinformation and confusion attract fraudsters who prey on unsuspecting seniors. This is probably why 20 percent of the 49 percent of homeowners ages 55 and older who expressed familiarity with reverse mortgages in the Fannie Mae NHS said that the risk of getting scammed concerned them the most. The HECM program has attempted to address this problem by requiring mandatory borrower counseling to ensure consumers understand reverse mortgages before they obtain one. Proprietary reverse mortgage lenders, however, are under no obligation to offer counseling. While misinformation makes reverse mortgage counseling harder, the fear of scams erodes the overall reputation of reverse mortgages, reducing homeowners' desire to even consider one.

TODAY'S REVERSE MORTGAGE LENDERS HAVE LIMITED BRAND RECOGNITION

Although many large and well-known financial institutions offered reverse mortgages before the housing bubble, most have left this business because of reputational risk and the losses they sustained after house prices fell. Stringent regulation and higher bank capital requirements postcrisis might also be discouraging banks from growing their presence in this sector. The exit of large lenders has created opportunities for smaller lenders with limited name recognition to offer reverse mortgages. Before the crisis, the largest reverse mortgage lenders included Wells Fargo, Financial Freedom, Bank of America, and MetLife (RMI 2010, 2). At least three of the four were popular household names. Today, the top four reverse mortgage lenders are American Advisors Group, Liberty Home Equity Solutions, One Reserve Mortgage, and Security 1 Lending—all with lesser brand recognition. All else being equal, consumers worried about getting scammed are more likely to choose brand-name lenders over others that are not well known, making reverse mortgages an even tougher sell in the current environment.

Another downside of large lenders exiting the reverse mortgage business is that when they leave, they also stop performing ancillary activities, such as product marketing, education, and advertising. This removes a reliable source of trusted information from the marketplace, leaving potential borrowers more vulnerable to misinformation.

High Cost of Reverse Mortgages

Of all the features of a reverse mortgage, the one most often advertised and the most appealing to borrowers is that no monthly payments are required. But despite the marketing emphasis on this aspect, the "all-in cost" of a reverse mortgage—measured over the life of the loan from closing to maturity—tends to be much higher and much more uncertain than the cost of alternatives. Factors that affect the eventual cost of reverse mortgages include timing and amount of draw(s), life expectancy, compounding interest, and direction of interest rates for adjustable-rate reverse mortgages.

As discussed previously, HECM up-front costs include lender origination fees, an up-front mortgage insurance premium (0.5 or 2.5 percent of the house's appraised value), and an ongoing annual mortgage insurance premium (1.25 percent of the loan amount). According to HECM endorsement data for September 2016, the interest rate for fixed-rate HECMs, excluding HECM premiums and other costs, averaged around 5 percent.[10] The rate for adjustable-rate HECMs averaged around 4.4 percent. After adding just the 1.25 percent annual HECM premium, the annual financing cost for reverse mortgages increases to 6.25 percent and 5.65 percent for fixed- and adjustable-rate HECMs, respectively. In contrast, the current interest rate for closed-end home equity loans and HELOCs is under 5 percent.[11]

The eventual cost of reverse mortgages is even higher relative to forward lending once the up-front HECM premium charges are added. Finally, the compounding of interest and HECM premiums pushes the total cost of reverse mortgages to levels that exceed the cost of getting a forward loan (AARP 2012).

The literature also shows that reverse mortgage costs are a major barrier for seniors. A 2006 survey of seniors who completed HECM reverse mortgage counseling found that the primary reason many counselees decided not to obtain a reverse mortgage was high costs (Redfoot, Scholen, and Brown 2007). Sixty-nine percent of HECM counselees in this survey said that costs were high (38 percent said they were somewhat high and 31 percent said they were very high). But according to a more recent survey of seniors who completed reverse mortgage counseling between 2006 and 2011, a smaller 31 percent of those who decided against obtaining one indicated costs were "too high" (Moulton et al. 2016). Interestingly, in Fannie Mae's NHS survey, only 12 percent of the 49 percent of homeowners ages 55 and older who were familiar with reverse mortgages singled out high cost as the main concern. A possible explanation for this disconnect is that the Fannie Mae result pertained to seniors self-reporting their familiarity with reverse mortgages, while the former study surveyed seniors who had undergone HECM counseling and were better informed about the true cost of reverse mortgages.

Despite high costs, lower-income seniors facing a financial hardship or lacking the means to make monthly payments for forward mortgages might find reverse mortgages the only viable option for extracting home equity without moving. Moulton and coauthors (2015) showed that reverse mortgages are more popular among lower-credit-score, lower-income, and minority borrowers, while forward equity extraction products are more popular among more-creditworthy borrowers.

Inadequate Credit Availability

After the housing bubble, lenders have become highly cautious with their underwriting guidelines. This has significantly reduced the likelihood of lenders approving a loan that has even a small probability of default.[12] As a result, credit scores, incomes, and debt-to-income ratios, among other credit parameters, have become much more conservative. The result is a significantly constrained credit environment that affects seniors' ability to extract equity from their homes through forward home equity lending. The tight credit environment has been especially severe on homeowners with lower incomes, lower credit scores, and higher debt burdens (Goodman, Zhu, and George 2015). For this reason, and because retirees tend to have lower incomes, they are more likely to experience tighter credit conditions than the general population.

Reverse mortgages are somewhat less affected by tight underwriting because the lack of monthly payments makes the risk of borrower default largely inapplicable. Although homeowners can still default on their insurance and property tax payments, recent changes to HECM guidelines have mitigated this risk. These guidelines (discussed next) require lenders to verify borrowers' ability to pay property tax, insurance, and other homeownership expenses and could negatively affect HECM origination volumes. Reverse mortgage credit availability has also been affected by large lenders exiting the market in recent years.

CHANGES TO HECM RULES

In recent years, HUD has tightened HECM underwriting in response to the heavy losses the FHA's insurance fund sustained on its HECM portfolio postcrisis. In 2013, HUD changed HECM loan disbursement rules to limit the amount borrowers could withdraw during the first year to 60 percent of the initial principal limit. This rule change had a provision for higher disbursement amounts, if needed, to pay off "mandatory obligations," such as existing mortgages or HECM origination and counseling fees for a higher up-front premium. This change was to encourage borrowers to access their equity slowly over time, rather than at once, to reduce the risk to HUD.[13] In 2016, HUD codified additional changes that require lenders to assess borrower ability to make property tax and homeowners' insurance payments by taking into account credit history, cash flow, and income. This change introduced an element of credit underwriting into HECM lending that was not required previously.

Although designed to reduce HECMs' default rate, these underwriting changes could also reduce reverse mortgage credit availability for seniors who do not demonstrate sufficient means to cover homeownership expenses. Moulton, Haurin, and Shi (2015) studied the ex-post effect of the new HECM disbursement rules on a dataset of 30,000 seniors who were counseled for reverse mortgages between 2006 and 2011. The authors found that although such restrictions would have reduced the default rate 20 percent, they would have led to a 7.5 percent contraction in HECM loan volume. Although this decline in credit availability is concerning, the huge corresponding reduction in the default rate—nearly three times the percentage reduction in loan volume—suggests that this rule change's benefits outweigh the cost.

EXIT OF LARGE REVERSE MORTGAGE LENDERS

Two of the nation's largest reverse mortgage lenders—Wells Fargo and Bank of America—announced their exit in 2011 in the wake of nationwide house price declines and an economy still battered by the Great Recession.[14] Their exits may also have been driven by the reputational risk of foreclosing on seniors who fall behind on their property tax and home insurance payments. The third-largest reverse mortgage lender at the time, MetLife, initially expanded its reach in 2011 in an attempt to fill the void created by the exit of Bank of America and Wells Fargo, but eventually also exited in early 2012.[15]

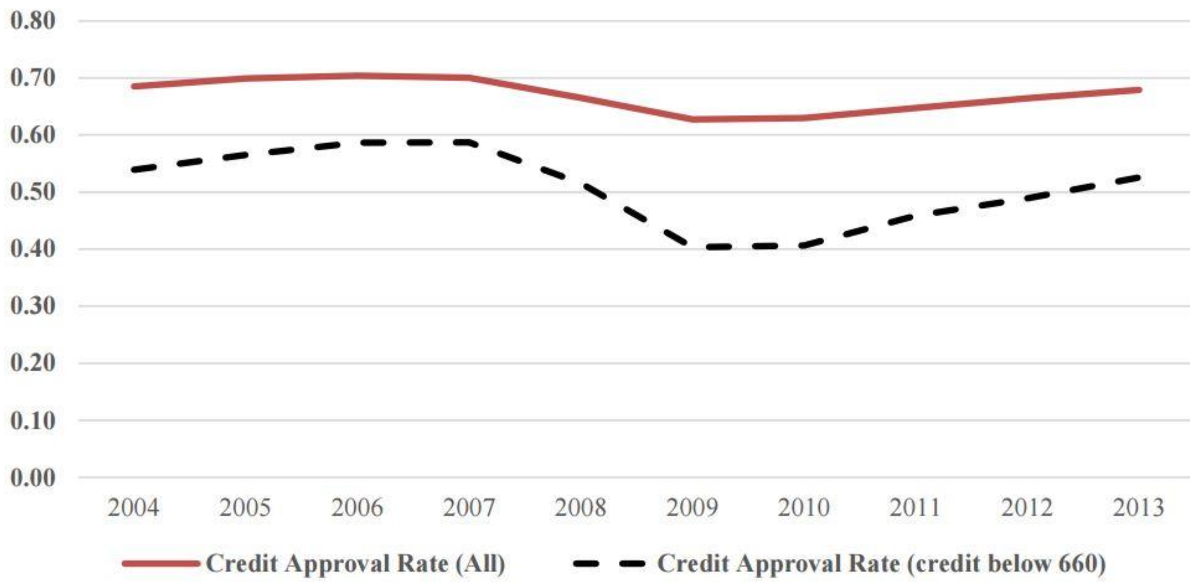
Although several smaller nonbank originators offer reverse mortgages today, their small scale and limited access to capital can inhibit their ability to reach more potential borrowers nationwide. This has likely contributed to the recent sharp decline in HECM initial principal limit endorsements (figure 3). This decline in HECM volume is expected, considering the steep nationwide decline in house prices (and housing equity) during the Great Recession. But that HECM lending volumes have failed to recover despite significant house price appreciation during the last three years indicates the presence of other barriers.

FORWARD EQUITY LENDING MORE AFFECTED BY TIGHT CREDIT

Research shows that in the forward equity lending channel, tight credit has affected less-creditworthy borrowers the most. Combining a sample of Federal Reserve Bank of New York/Equifax Consumer Credit Panel data (for HECMs, HELOCs, cash-out refinances, and closed-end second liens) for senior homeowners ages 62 and older with HUD loan-level HECM origination data, CoreLogic's zip code data on housing prices, and American Community Survey data from 2004 to 2012, Moulton and coauthors (2015) showed that HECMs tend to be more popular among less-creditworthy seniors, while HELOCs tend to be prevalent among the most-creditworthy borrowers. The study showed that senior homeowners with credit scores below 660 experienced a more significant tightening of home equity credit, as measured by loan approval rate, than did the entire sample. The credit approval rate for the entire sample peaked at 70 percent in 2006 before dropping 7 percentage points to 63 percent in 2009. But for seniors with credit scores below 660, the approval rate dropped 20 percentage points, from 60 percent to 40 percent over the same period (figure 5).

FIGURE 5

Credit Approval Rate Trends for Seniors



Source: Moulton and coauthors (2015).

Although the credit approval rate has improved since 2009, including for those with scores below 660, that does not necessarily translate into an equal increase in equity extraction across lending channels. Different channels exhibit varying sensitivities to eased credit conditions. Moulton and coauthors (2015) showed that a 1 percentage point increase in the credit approval rate would increase HELOC origination volume 0.73 percent, cash-out refinance originations 1.1 percent, closed-end home equity loan originations 0.6 percent, and HECM originations 0.14 percent. Because low-income and less-creditworthy seniors are more likely to depend on HECMs than others, the credit approval rate improvement since 2009 has likely translated into a much smaller increase in equity extraction at the lower end of the credit spectrum.

Reducing Barriers to Equity Extraction

Two kinds of barriers limit home equity extraction: first, policy barriers such as lack of financial literacy, high cost of reverse mortgages, and inadequate credit availability more generally; and second, behavioral impediments (aversion to debt or desire to save for emergencies or leave a bequest) that may be rooted in seniors' beliefs and values. While none of these impediments are easy to overcome, changing peoples' long-held preferences and attitudes can often take a generation or longer. Further, aversion to debt in old age seems responsible and prudent given reduced earning capacity; the heightened risk of delinquency, including from health emergencies; the risk of losing a home to foreclosure; or problems caused by leaving unpaid debt and other financial issues for heirs to clean up.

Consequently, any recommendations aimed at reducing barriers for equity extraction must strike a balance to ensure equity remains reasonably accessible, if and when needed, while discouraging unnecessary debt that puts HUD, lenders, seniors, or their children at risk. Accordingly, this section focuses on ways to reduce policy barriers to equity extraction as opposed to changing seniors' inherent aversion to risk and debt. In addition, the recommendations offered in this section apply mostly to reverse mortgages. This is neither intentional nor surprising. It simply reflects the fact that impediments to equity extraction through reverse mortgages far outnumber those for forward extraction channels. Nevertheless, a few improvements can be made to forward equity lending products that might make it easier for seniors to extract home equity.

Improving Reverse Mortgage Financial Literacy

Reverse mortgages are undeniably complex. But other complex financial products—such as stocks, bonds, mutual funds, and insurance—do not suffer from the same financial literacy issues as reverse mortgages do. Seniors are comfortable investing their life savings in stocks, bonds, and certificates of deposit, or obtaining various insurance, loan, and credit card products. Therefore, product complexity alone does not explain why reverse mortgages are poorly understood. If seniors have succeeded in overcoming the "complexity factor" for other financial products, why have they not been able to do the same for reverse mortgages?

Two reasons seem likely. First, the complexity problem for reverse mortgages has been exacerbated by fraud and misinformation. A Consumer Financial Protection Bureau review of reverse mortgage advertisements and a focus group's impressions of those advertisements revealed that consumers did not even know that reverse mortgages were loans because ads either did not include interest rates and repayment terms or included them in the fine print (CFPB 2015). Other consumers pointed out that phrases such as "government insured," "government-backed program," and "tax-free money" led them to believe reverse mortgages are a federal government program or a benefit (similar to Medicare), further cementing their belief that reverse mortgages are not loans. The result is increased misunderstanding about how reverse mortgages work. Therefore, it is possible that already skeptical seniors might simply assume the worst and close their eyes to reverse mortgages for good.

Second, consumers typically do not think about reverse mortgages, which are a niche product, until retirement or later. As a result, the level of knowledge about reverse mortgages among the public is low or nonexistent before retirement. In contrast, the public is more familiar with and trusts other mainstream banking, investment, and insurance products from a younger age. Unfamiliarity with an esoteric financial product means seniors would have to leave their comfort zone to use reverse mortgages. There are a few ways to address these issues.

INTRODUCE REVERSE MORTGAGES EARLIER IN LIFE

One way to improve reverse mortgage financial literacy is to introduce reverse mortgages earlier in life. Financial education is more effective when delivered frequently, regularly, and through various stages of life (Beck 2015). Most workers get introduced to investment and financial products during retirement planning through employer 401(k) plans, individual retirement accounts, or self-education. For many workers, the decision to contribute (or decline contributions) to an individual retirement account or an employer 401(k) plan forces them to focus, if only briefly, on retirement planning options. One way to educate future retirees about reverse mortgages could be through retirement planning. Knowing that this product exists and understanding its basics earlier in life could reduce skepticism about reverse mortgages. Some financial planners have already begun recommending reverse mortgages as a component of retirement planning.[16] An ancillary but crucial benefit is that the more informed future retirees are about reverse mortgages, the less inviting this space would be for scammers and fraudsters.

Bringing reverse mortgages into retirement planning may have another upside. Incorporating home equity wealth into financial planning could enable people to think more holistically about retirement, allowing them to optimize or diversify their investment strategies. Liquefying home equity could allow retirees to postpone drawing from retirement savings until later, giving assets more time to grow. For others, obtaining a reverse mortgage or a home equity loan could be a temporary alternative to selling stocks in a bear market. This would allow retirees to cover their living expenses without incurring losses on their retirement savings. The loan could be paid off once markets bounce back. Having said that, it is not clear if financial planners and investment advisers would be willing to discuss reverse mortgages because of potential liability and licensing issues.

IMPROVE EDUCATION, OUTREACH, AND COUNSELING

A shorter-term recommendation is for federal entities, such as HUD and the Social Security Administration, to increase education and outreach to seniors. The Social Security Administration, which touches most seniors and retirees, could disseminate information on how reverse mortgages might work with social security benefits to improve financial security. Educating seniors about using reverse mortgages to delay social security could also be financially appealing for the Social Security Administration.

HUD could establish rules requiring an independent review and certification (by a HUD-approved professional) to ensure reverse mortgage contracts are reasonable and well understood by the applicant. Older seniors are likely to suffer from cognitive, visual, or hearing disorders that might limit their ability to understand simple concepts (Beck 2015). A mandatory review of reverse mortgage contracts by an independent third party would not only prevent seniors from making the wrong financial decision, but would also discourage fraud and abuse.

Another recommendation for enhancing reverse mortgage literacy is through improvements to HECM counseling. In particular, it may be beneficial to have different types of counseling for different classes of borrowers. Consumers seeking to extract home equity can differ depending on creditworthiness, borrowing needs, household income and assets, and so on. Counseling that does not adequately take these distinctions into account may not give counselees the precise information they need to make the right decision. For instance, wealthy borrowers considering HECMs may be better suited for forward home equity products, such as HELOCs. These borrowers might benefit from counseling that compares the pros and cons of HECMs to those of forward equity extraction products. On the other hand, low-income borrowers with limited means may benefit from counseling that focuses more on such areas as appropriate uses of HECMs, effective coping strategies, and minimizing borrowing. Customized counseling would result in well-informed consumers who make better financial decisions, saving them (and lenders) valuable time and money.

HUD could also improve its newly announced HECM counseling guidelines.[17] Under current rules, counseling must be completed before the reverse mortgage loan application is processed by the lender.[18] But this might cause HECM counseling to occur too late in the process, perhaps after seniors have already made up their mind to obtain a reverse mortgage. This standard could be enhanced by requiring lenders to refer borrowers to HECM counseling as the first step after initial contact.

Lowering the Cost of Reverse Mortgages

The up-front mortgage insurance premium for HECMs is 0.5 or 2.5 percent of the appraised home value. Borrowers who withdraw more than 60 percent of their initial principal limit in the first 12 months are charged 2.5 percent, while those who draw 60 percent or less are charged 0.5 percent. This premium structure encourages slow withdrawal of equity. The FHA also charges an annual mortgage insurance premium of 1.25 percent of the loan balance. For reference, the corresponding up-front and annual premiums for the FHA's forward single-family mortgage program are 1.75 and 0.85 percent of the loan amount, respectively.

Thus, combined HECM premiums for homeowners who withdraw more than 60 percent of their initial principal limit in the first year are more than premiums for the FHA's forward mortgages. HECMs can be expensive even for those who pay the reduced 0.5 percent up-front premium because of higher interest rates and compounding of interest and premiums. Reverse mortgage premiums are more expensive than premiums for the FHA's forward mortgages because reverse mortgage borrowers do not have to make payments until maturity, which increases the loan balance and HUD's risk exposure. Similarly, because lenders do not receive periodic principal or interest payments, they see their risk exposure increase over time and have to compensate by charging a higher rate.

Although high mortgage insurance premiums are not in borrowers' best financial interests, HECMs present greater credit risk to the FHA. As much as HECM premiums may seem like a tempting area for exploring cost reduction, caution is warranted. Efforts to reduce premiums must be studied carefully and, when needed, accompanied by a commensurate reduction in risk. Further, there are other avenues for reducing reverse mortgage costs.

SIMPLIFY REVERSE MORTGAGE PRODUCT DESIGN

Simplifying reverse mortgages could reduce borrower expenses. Unlike forward mortgage borrowers, who typically only have to make a few decisions (essentially, choose a fixed- or adjustable-rate mortgage and a mortgage term), reverse mortgage borrowers have to decide on many more options: fixed rate versus adjustable rate; lump-sum disbursement, line of credit, term annuity, tenure annuity, or a combination of the different payment options; and the timing and pace at which to withdraw funds for the line of credit. This optionality makes it difficult for borrowers to comprehend reverse mortgages and for lenders to value them, forcing lenders to compensate by charging higher interest rates and fees than they otherwise would.

To reduce product complexity while limiting adverse borrower impact, HUD could consider eliminating rarely used features. The HECM tenure annuity option tends to be uncommon. According to the fiscal year 2015 HECM actuarial report, less than 2 percent of HECM borrowers received loan proceeds via tenure annuities during each fiscal year from 2009 to 2015 (IFE Group 2015). For fiscal year 2015, only 1.58 percent of HECM borrowers received tenure annuities, 1.09 percent received term annuities, 93.63 percent received a line of credit, and 3.71 percent received a combination of annuity and line of credit. An earlier analysis of loan-level data for HECM loans endorsed between 1989 and 2007 showed that only 10 percent of borrowers chose tenure annuities (Shan 2011). These low take-up rates suggest that tenure annuities could be phased out. One reason the annuity disbursement option may be less popular is that reverse mortgages tend to be a product of last resort for homeowners in need of emergency or immediate funds.

The borrower impact of phasing out tenure annuities should be minimal because the few who still preferred an annuity could always buy one from financial services firms using HECM funds. Further, the line-of-credit disbursement could be structured like an annuity, where borrowers would draw a certain amount periodically. Although obtaining tenure annuities from the private sector could cost more, such expenses could be offset by any resulting reductions in the interest rate or HECM insurance premiums.

The lump-sum payment and the line-of-credit disbursement options offer lenders and HUD greater financial certainty than tenure annuities because of the smaller impact of life expectancy assumptions. This is because the maximum amount a borrower can borrow under the lump sum and the line-of-credit option is largely set at the time of closing. Having a good sense of their maximum possible exposure allows lenders and HUD to manage this risk better. Tenure annuities, on the other hand, require monthly payments to be made to borrowers as long as they occupy the home and therefore suffer from greater longevity risk. This uncertainty might be priced into HECM costs and passed on to borrowers. But adequate protections for consumers shopping for annuities in the private market are also needed because of a history of inappropriate and abusive cross-selling practices targeting reverse mortgage borrowers (CFPB 2012).

In addition to phasing out annuities, the line-of-credit disbursement option could be simplified. An advantage to borrowers of a line of credit is that the untapped portion of the line does not accrue interest. This reduces interest costs and gives borrowers greater flexibility because they can decide how much to draw and when. The line of credit is especially powerful because it grows and stays open as long as the borrower remains in the home. But the downside of this borrower-friendly disbursement option is that it exposes lenders to the risk that borrowers will draw unpredictable amounts of cash at unpredictable times, requiring lenders to maintain certain levels of liquidity or access to liquidity at all times.

This issue is more relevant today than it was precrisis because nonbanks—which currently dominate the reverse mortgage lending space—do not have the same low-cost access to liquidity and financing that depository institutions do. These higher costs are passed on to borrowers. To realize cost efficiencies here, HUD could consider reducing lender uncertainty by putting a term limit on the line-of-credit disbursement option. Borrowers would have a certain number of years (a draw period) during which they could draw on the line. The amount drawn during the draw period would be repaid to the lender the same way as today (i.e., upon death or sale of the house).

Putting a term limit on the line-of-credit disbursement option would also help protect HUD from the "ruthless strategy" under which a borrower obtains a HECM line of credit but then opportunistically draws funds only if the value of the house falls below the approved line.[19] In other words, the borrower uses HECM as an insurance policy against falling house prices, creating losses for HUD. Setting a term limit would reduce but not eliminate this risk.

Despite the risk to HUD, the literature shows that HECM borrowers rarely exercise the ruthless strategy. Davidoff and Wetzel (2014) showed that the percentage of HECM borrowers choosing the ruthless strategy is almost zero. Any resulting cost savings for the HECM program will thus likely be limited. At the same time, current HECM premiums might already be pricing in the risk of the ruthless strategy. And to the extent they do, evidence showing that borrowers almost never use the ruthless strategy could be grounds for a risk-neutral reduction in HECM premiums.

REDUCE REVERSE MORTGAGE MARKETING COSTS

Another reason for the high cost of reverse mortgages is marketing related. Reverse mortgage marketing tends to be high-touch and time consuming for three reasons. First, lenders need to allocate significant resources to overcome limited product awareness and consumer skepticism through advertisements and consumer awareness campaigns. Second, product complexity means lenders have to allocate time and resources to educate seniors on the pros, cons, costs, and risks associated with reverse mortgages. This can require high-touch, one-on-one dialogue, education, and training, all of which increase lender costs. Finally, because reverse mortgage lending volumes are currently small, the fixed costs of origination are spread over few loans. This increases the per loan origination costs. In 2015, only 56,000 HECM reverse mortgages were originated by as many as 2,200 lenders (RMI 2016). That translates into an average of just 25 loans per lender.

Although marketing costs can be lowered by reducing product complexity and improving financial literacy, more can be achieved by increasing competition among lenders. Because seniors tend to be less financially savvy or suffer from health conditions, they may not shop around or possess the expertise to compare multiple offers. While lenders may have an incentive to compete with each other to get borrowers in the door, they may have less of an incentive to compete with each other on price (e.g., on origination fees and interest rates).

Increased price competition might be introduced in a couple of ways. First, HUD or the Consumer Financial Protection Bureau could create a reverse mortgage tool similar to the latter's forward mortgage rate tool that allows borrowers to easily check average rates offered in their state to ensure they are not overpaying.[20] HUD could also enhance HECM borrower counseling to put additional emphasis on obtaining multiple price quotes, as well as educating seniors on how to compare multiple offers. The impact of these changes could be amplified by requiring HECM counseling to be completed before signing the loan contract.

IMPROVE LIQUIDITY OF HECM MORTGAGE-BACKED SECURITIES

Reverse mortgage costs are also affected by structural issues within the HECM mortgage-backed securities market. The HMBS market is small. Currently, the total HMBS outstanding is about $55 billion, a fraction of the $5.8 trillion outstanding for forward mortgage agency MBS.[21] The HMBS market is small in part because it was created in 2007 and is still in its infancy. Before 2007, Fannie Mae was the predominant secondary market outlet for HECMs, although Wall Street interest increased during the housing bubble. But Fannie Mae mostly held HECM loans on its balance sheet as opposed to securitizing and selling. That meant there were no capital markets for trading reverse mortgage securities before the creation of the HMBS market.

Growth in HMBS outstanding has been stymied by small reverse mortgage origination volumes in recent years. The HECM initial principal limit endorsed has averaged only about $9.5 billion a year during the last five years after peaking at just over $22 billion in 2009.[22] HMBS is also a somewhat unique asset class because it does not pay investors a regular coupon, unlike most other fixed-income securities. As a result, HMBS appeal to a smaller buy-and-hold investor base (Strumberger 2012). This reduces HMBS liquidity and increases transaction costs, which are passed on to borrowers.

Thus, growing and diversifying the investor base for HMBS could reduce HECM borrowing costs. A more liquid market would reduce transaction costs (the bid-ask spread), lowering rates. Improved liquidity would also make it cheaper for lenders to manage their interest rate risk (e.g., prepayment risk). This could reduce their inclination to price for such risks through higher rates. Finally, a more liquid HMBS market could attract investors and capital from across the globe, especially because HMBS carry an explicit government guarantee. A recommendation for broadening the investor base would be to educate foreign investors, sovereign funds, and other fixed-income investors and market HMBS to them as a viable alternative to US Treasury securities. HECM mortgage-backed securities also have yield, prepayment, and maturity profiles different from those of forward mortgage-backed securities. In that sense, HMBS could also offer a valuable diversification opportunity to investors.

Improving Credit Availability

The decline in credit availability postcrisis has had a disproportionate impact on less-creditworthy borrowers. These borrowers tend to have lower incomes and are less likely to be approved for a traditional home equity loan, a home equity line of credit, or a cash-out refinance, products that require monthly payments. Although many of these borrowers relied on cash-out refinances during the housing bubble, the volume of cash-out refinancing has taken a hit recently, as underwriting has become more stringent. Consequently, such borrowers are more likely to choose reverse mortgages. But here, too, HUD's changes to the HECM program that require lenders to verify a borrower's ability to pay taxes and insurance—as well as the exit of large lenders from the HECM market—have worsened credit availability. Risk aversion after the crisis and a significantly tightened regulatory and risk management environment have also reduced lenders' willingness to extend credit.

REINTRODUCE A MODIFIED VERSION OF HECM SAVER

Tight credit's structural nature and its wide variety of underlying causes make it a vexing barrier to ease. But one change to the HECM program could expand credit availability for low- and moderate-income borrowers without necessarily exposing HUD or lenders to greater risk. In September 2010, HUD introduced the HECM Saver program as a lower-cost vehicle for seniors who desired a smaller disbursement but found HECM Standard premiums too expensive.[23] HECM Saver allowed borrowers to withdraw 51 to 61 percent of the appraised value of the house depending on age and interest rates, while the HECM Standard product allowed proceeds as high as 77 percent of the home value. Because a smaller loan amount reduced HUD's risk exposure, the HECM Saver charged reduced premiums. Specifically, HUD nearly eliminated up-front premiums for the Saver program, charging borrowers only 0.01 percent, negligible compared with the 2 percent charged for HECM Standard at the time. The annual premium was 1.25 percent for both products.

Despite its lower cost, HECM Saver was discontinued in 2013 because of limited demand, as most borrowers continued to opt for higher loan amounts available under HECM Standard. Aversion to HECM Saver may have been a result of the fact that both the Saver and Standard versions charged the same 1.25 percent annual premiums, even though Saver posed less risk to the FHA. The negligible up-front premiums under Saver were only a small portion of HECM borrowing costs. Therefore, borrowers might not have had much financial incentive to choose Saver's lower disbursement. A secondary reason why Saver was unsuccessful is that interest rates for Saver turned out to be higher than those for HECM Standard because capital markets investors assigned it a higher probability of prepayment, presumably because a smaller loan would be easier to pay off. The Saver product thus turned out to be more expensive than Standard, further dampening borrower interest.[24] These two reasons raise the question of whether HECM Saver should have reduced the annual premium as well to ensure sufficient price advantage over HECM Standard.

Home Equity Conversion Mortgage take-up rate could also be improved by offering more granular pricing. A drawback of the current annual premium structure is that it may be encouraging some seniors to borrow more than they need, while discouraging those who want to borrow less because they find the premiums too expensive. One way to address both issues would be to experiment with a more granular premium structure. That is, the current 60 percent disbursement threshold could be replaced by multiple tiers—say, 40, 50, 60, and 70 percent—with progressively higher annual premiums for larger disbursements. Saving money by borrowing less could appeal to seniors who currently avoid HECMs as too expensive. Similarly, requiring higher premiums for larger loans could discourage big equity extractions for discretionary purposes.

ALTERNATIVES TO REVERSE MORTGAGES: SHARED APPRECIATION MORTGAGES AND PARTIAL RENTALS

A final recommendation to improve equity extraction is to encourage the development of new substitutes for reverse mortgages. Shared appreciation mortgages and converting a portion of the home to a rental are two such opportunities.

A SAM allows a homeowner to sell a portion of future equity in the house in exchange for a lump-sum payment. As with reverse mortgages, SAMs require no monthly payments until the house is sold or the SAM contract expires. When either of these events occur, the lender receives a pro-rata share of the house price appreciation (or losses if house price declines), typically based on a preset formula and a predetermined house price index. SAM age requirements are more lenient than a HECM's, making it accessible to a wider population. SAMs also offer greater repayment certainty than reverse mortgages because, depending on structure, they can come with a fixed term, at the end of which the lender receives a fixed portion of future equity.

But SAMs have challenges. Despite a long history, it remains a nascent product that is used rarely, lacks standardization, is difficult to understand, offers limited or no consumer protection, and can be costly if borrowers do not understand all details before signing the contract. For example, although SAM lenders advertise that they would share future gains and losses in home equity, the fine print can contain "stop loss" clauses that limit lender losses to a certain level. Nevertheless, such issues could be mitigated, as SAMs receive more scrutiny from policymakers and regulators.

SAMs also do not allow seniors to age in place once the loan term expires and the payment becomes due. At maturity, seniors would be forced to sell their home or obtain reverse mortgages to pay back the SAM lender. Still, if SAM borrowing costs turn out to be lower than those of reverse mortgages, even delaying the use of reverse mortgages until later in life might be more economical. Additionally, because SAMs are a better substitute for reverse mortgages than forward loans that require a monthly payment, they can compete better with reverse mortgages. That could put competitive pressure on HUD and the industry to make reverse mortgages simpler, cheaper, more appealing, and more consumer friendly. Overall, there seems to be a case for more experimentation with SAMs so the industry and policymakers can better grasp the suitability of this product for equity extraction.

Another option for using the home to improve retirement financial security is to convert a portion of the home into a rental unit. As landlords, seniors could use rental income to pay for living expenses or qualify for a home equity loan. This approach could help seniors meet financial needs with minimal costs, risk, and disruption. First, seniors could age in place with no risk of losing their home. Second, rental income would help seniors avoid debt and its associated risks without compromising on a comfortable retirement. Third, by keeping ownership of the property, seniors could pass it down to their children.

Despite its benefits, the rental strategy poses some challenges. Renting out a portion of the home to a stranger may not appeal to many seniors for safety, privacy, or other reasons. In addition, some homes may need retrofitting or modification before they are ready for renting and would require up-front investment, which may not be easy to finance. Furthermore, local zoning ordinances, housing codes, or homeowner association bylaws may prohibit renting out a portion of a single-family dwelling. Lastly, in some parts of the country, rents might not be high enough or demand for renting may not be strong enough to make this option viable. But for senior homeowners living in geographies with vibrant rental markets, partial renting could be a useful vehicle for achieving greater financial security.

Conclusion

Home equity extraction can be a useful financial tool for seniors who lack sufficient funds to live comfortably during their "golden years." The financial services industry offers products that retirees can use to convert home equity into cash to meet living expenses. At one end of the spectrum are forward loan products (e.g., cash-out refinances, home equity loans, and HELOCs) that are generally used by borrowers with incomes high enough to repay the loan. At the other end of the spectrum are reverse mortgages, which tend to be used more by borrowers whose monthly income may not be high enough to support loan repayment or borrowers who may have the means, but not the desire, to make monthly payments.

Despite these products' availability, several barriers hinder seniors' ability to extract equity in a way that is easy, efficient, and economical. Some of these barriers are a by-product of imperfect product design or insufficient product awareness and can be addressed through product changes, regulation, or policy interventions. Other barriers, such as debt aversion or the desire to leave a bequest, are deeply rooted in traditional beliefs that are difficult, and potentially unwise, to alter.

The recommendations in this report address the former set of barriers through a combination of more-efficient product design, lowering or eliminating unnecessary costs, enhancing financial literacy, and exploring new mechanisms for equity extraction. As with all financial products, it is important to remain cautious and stay true to the original mission of equity extraction (i.e., to allow seniors to age comfortably in place) rather than encouraging unnecessary spending through debt and leverage that might be detrimental to seniors and pose undue risk to lenders, insurers, and investors.

Appendix

About the Fannie Mae National Housing Survey®

The Fannie Mae National Housing Survey results in this report are based on approximately 1,000 telephone interviews of American homeowners ages 55 and older conducted via landline and cell phone in the second quarter of 2016. The survey was conducted by Penn Schoen Berland, in coordination with Fannie Mae. For the sample to accurately represent the US population, 60 percent of calls were made to cell phones, and the set of homeowners ages 55 and older was weighted to make it reflective of American Community Survey data in terms of gender, age, race or ethnicity, income, and education.

Selected Survey Results

APPENDIX TABLE A.1

How Concerned Are You about Your Personal Financial Situation in Retirement?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Very concerned (%)	11	14	7	10	10	15	5	10	12	14	9	9
Somewhat concerned (%)	26	33	22	18	20	23	20	17	31	38	24	19
Not very concerned (%)	19	21	22	13	17	17	24	11	22	24	19	19
Not at all concerned (%)	40	29	43	56	49	43	46	58	31	22	40	50
Don't know (%)	4	2	6	4	4	2	4	4	4	2	7	3
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.2

When Do You Expect to Move Next?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Never (%)	65	56	67	80	75	68	72	83	56	49	62	73
Less than 1 year (%)	4	6	3	4	3	4	3	3	5	6	3	4
1–3 years (%)	6	6	6	4	4	5	4	3	7	7	8	6
3–5 years (%)	5	8	4	2	2	3	3	1	8	11	4	5
More than 5 years (%)	8	12	7	2	5	7	5	1	12	15	10	2
Don't know (%)	12	12	13	8	11	13	13	8	12	11	14	10
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.3

How Interested Are You in Tapping into Your Home Equity in Retirement?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Very interested (%)	2	3	1	2	1	3	0	1	2	3	2	2
Somewhat interested (%)	4	6	3	4	4	4	2	4	5	6	4	3
Not very interested (%)	10	11	9	8	8	7	8	9	12	14	10	5
Not at all interested (%)	80	78	81	84	84	84	85	81	77	75	76	90
Don't know (%)	3	2	6	3	3	2	4	3	4	2	8	0
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.4

For Which of the Following Purposes Would You Be Most Interested in Tapping into Your Home Equity in Retirement? Please Tell Me All That Apply.

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Meet everyday living expenses (%)	34	38	31	23	31	50	27	12	36	33	33	63
Pay for medical care not covered by insurance or Medicare (%)	40	54	19	23	34	47	13	27	44	56	21	7
Help meet expenses for your children (%)	18	22	9	16	27	32	27	21	12	18	0	0
Pay for home improvement expenses (%)	54	52	51	64	57	42	57	74	52	57	48	29
Other (%)	8	6	6	16	15	13	16	16	4	3	2	16
Don't know (%)	5	3	17	0	0	0	0	0	9	5	25	0
Unweighted base	**65**	**32**	**18**	**15**	**26**	**11**	**7**	**8**	**39**	**21**	**11**	**7**
Base	**68**	**39**	**14**	**14**	**28**	**12**	**5**	**11**	**40**	**27**	**10**	**3**

Note: This question was only asked of respondents who said they were very or somewhat interested in tapping equity in retirement.

APPENDIX TABLE A.5

Which of the Following Ways of Taking Equity out of Your Home Are You Familiar With?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Reverse mortgages (%)	49	49	53	46	48	45	55	43	51	51	51	53
Home equity loans or home equity lines of credit (%)	62	71	66	41	52	57	65	36	73	79	67	57
Cash-out refinancing (%)	36	38	41	28	31	30	40	24	42	42	43	40
None of the above (%)	23	19	21	33	29	25	24	37	17	15	18	21
Don't know (%)	4	3	4	5	4	3	3	6	4	3	6	2
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.6

What, If Any, Are Your Main Concerns about Tapping into Your Home Equity in Retirement?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
I want to save it to give to my children or heirs (%)	19	19	19	19	19	18	20	19	19	19	18	20
I want to save it for an emergency (%)	10	10	11	7	9	12	8	8	10	9	13	4
I don't need the money (%)	30	25	29	41	35	33	29	43	25	20	29	36
I don't want to have debt (%)	36	40	39	27	35	36	41	27	38	42	37	28
I don't have enough income to qualify for additional debt (%)	7	8	7	6	5	4	4	6	9	10	10	5
I don't have enough equity to qualify for additional debt (%)	5	6	4	3	3	3	4	2	6	7	5	6
Other (%)	3	2	3	4	3	3	4	3	2	1	1	9
Don't know (%)	5	4	6	5	5	5	4	5	5	3	8	4
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.7

If You Were Going to Take Equity out of Your Home in Retirement, Which Method or Methods Would You Prefer?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
Reverse mortgages (%)	6	5	6	8	6	4	4	8	7	6	7	7
Home equity loans or home equity lines of credit (%)	16	19	17	11	15	18	17	10	18	20	16	13
Cash-out refinancing (%)	4	5	6	2	2	1	4	2	6	7	7	1
Selling your home and purchasing a less-expensive one (%)	35	42	32	28	33	36	37	27	38	45	26	31
Selling your home and renting (%)	12	11	10	15	11	9	8	15	12	12	11	17
None of the above (%)	26	23	27	32	31	31	29	33	21	18	25	28
Don't know (%)	6	3	8	9	6	4	5	9	6	3	12	7
Unweighted base	**1,071**	**427**	**356**	**288**	**569**	**185**	**214**	**170**	**502**	**242**	**142**	**118**
Base	**1,071**	**471**	**343**	**257**	**546**	**171**	**182**	**193**	**525**	**300**	**161**	**64**

APPENDIX TABLE A.8

What, If Anything, Concerns You Most about Reverse Mortgages?

	All Homeowners				Outright Homeowners				Homeowners with Mortgage			
	55+	55–64	65–74	75+	55+	55–64	65–74	75+	55+	55–64	65–74	75+
I'm not sure if I will still keep the title to my home (%)	5	5	5	3	5	6	5	4	4	5	4	1
I'm worried that my family won't be able to stay in our home if I pass away (%)	11	9	14	11	9	6	12	10	13	11	17	15
They are too costly (%)	12	13	10	12	11	12	12	9	13	13	8	20
They are difficult to understand (%)	9	10	8	11	12	16	8	13	7	7	8	6
I'm afraid of getting scammed (%)	20	24	18	16	18	21	17	17	22	26	18	15
Other (%)	8	7	8	7	7	6	8	7	8	8	9	7
None of the above (%)	27	24	26	34	30	27	28	36	24	23	24	29
Don't know (%)	8	7	10	5	7	7	10	4	8	7	11	6
Unweighted base	**548**	**210**	**193**	**145**	**277**	**83**	**117**	**77**	**271**	**127**	**76**	**68**
Base	**528**	**230**	**181**	**117**	**260**	**78**	**99**	**83**	**268**	**152**	**82**	**34**

Note: This question was only asked of respondents who said they were familiar with reverse mortgages.

Notes

1. Selected results from this survey are shown in the appendix.
2. Forty percent of homeowners ages 55 and older were not at all concerned, 19 percent were not very concerned, and 4 percent were unsure.
3. The average net worth was calculated by subtracting all outstanding debt secured by the housing unit from the house value.
4. The right y-axis shows HECM share of equity extraction originations.
5. The initial principal limit is the loan amount a borrower is approved to receive and is based on several factors, including the appraised value of the house, the FHA loan limit, and borrower age.
6. "Refinance Statistics," Freddie Mac, accessed February 7, 2017, http://www.freddiemac.com/finance/refinance_report.html.
7. Excluding the volume of preexisting home equity loans and HELOCs consolidated into the first-lien. On a consolidated basis, the average equity cashed out each year from 2010 to 2015 was $58 billion.
8. The share of cash-out refinances varies partly because borrowers' motivations change with interest rates. When rates are low, the primary goal of refinancing is to save money by reducing the monthly payment. The share of cash-out refinances tends to be small during such periods. When rates are high, borrowers have no incentive to refinance for rate reasons. And those who refinance tend to be driven more by their desire to cash out, causing the cash-out share to be higher.
9. Recent changes to HECM disbursement rules have shifted borrower demand heavily toward the adjustable-rate product. See "Revised Changes to the Home Equity Conversion Mortgage (HECM) Program Requirements," letter to approved mortgagees, November 10, 2014, https://portal.hud.gov/hudportal/documents/huddoc?id=14-21ml.pdf.
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22. Urban Institute calculations based on HUD data.

23. US Department of Housing and Urban Development, "HUD Announces New Reverse Mortgage Option," press release, September 22, 2010, http://portal.hud.gov/hudportal/HUD?src=/press/press_releases_media_advisories/2010/HUDNo.10-205.

24. After discontinuing HECM Saver, HUD announced a dual premium structure—which remains in place today—that allows for the reduced 0.5 percent up-front premium as long as first-year withdrawals are limited to 60 percent of the initial principal limit or less. Otherwise, the up-font premium is 2.5 percent. The annual premium is the same (1.25 percent of the loan amount) under both options.

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