A Reverse Mortgage to Buy a Home? Here's How

wsj.com/articles/a-reverse-mortgage-to-buy-a-home-heres-how-1469026043

By Anya Martin

ENLARGE

Illustration: Chris Gash

July 20, 2016 10:47 a.m. ET

Reverse mortgages are typically seen as a way for seniors to remain in their homes while drawing income from their property. But a reverse mortgage can also be used to buy a home.

Here's how it works: Seniors 62 or older buying a primary residence make a down payment and pay closing costs. They then get a lump-sum loan that goes toward the home purchase. No monthly payments are required to pay down the debt. Instead, interest accrues on the loan, and the principal and interest are usually due when the last co-borrower or spouse on the loan moves out or dies.

More Jumbo Jungle

Most reverse mortgages are FHA-insured loans called home-equity conversion mortgages, or HECMs. The loan amount is a percentage of the home's appraised value, up to $625,500. That percentage starts at about 52% of the purchase price and rises with a borrower's age, going up to about 75%.

In general, interest rates on lump-sum HECMs range from 4.25% to over 5%, says Peter H. Bell, president and CEO of the National Reverse Mortgage Lenders Association, a trade group.

If desired, a senior with a reverse mortgage can leave a portion of the proceeds in a line of credit for future use. Interest is charged only on money that is drawn from the line of credit. HECMs that are lines of credit have interest rates starting in the 3% range, but these are adjustable rates that may change throughout the life of the loan, Mr. Bell adds.

Retirees often have trouble meeting underwriting requirements for regular mortgages, which are based on income more than assets, says Richard Mandell, CEO of One Reverse Mortgage, a subsidiary of Quicken Loans. A reverse mortgage "gives retirees the opportunity to move to a different home that better suits their needs, be closer to family or live in a warmer climate," he adds.

> *'If desired, a senior with a reverse mortgage can leave a portion of the proceeds in a line of credit for future use.'*

A top concern has been that seniors will draw down their home equity too rapidly, forcing them to exhaust other savings, says Jamie Hopkins, co-director of the New York Life Center for Retirement Income at the American College of Financial Services in Bryn Mawr, Pa. But used strategically, buying a home with a reverse mortgage allows seniors to invest in higher-yield investments than their home.

Ray and Janet Massey wanted a 3,300-square-foot house with a pool in Katy, Texas, a suburb of Houston, but it was listed at about $533,000. Their previous home, also in the Houston area, was worth only $370,000, with a mortgage that had to be paid off, Mr. Massey says.

The Masseys made a $240,000 down payment, and their reverse mortgage paid for the home. They put down another $250,000 to qualify for a line of credit with a variable rate, currently 5.73%, says Mr. Massey, a 72-year-old retired sales manager at an auto-dealership. He and Janet, who at 71 still works as a packaging-sales executive, have access to money if they need it. But any amount they don't draw grows annually at the current adjustable-rate —even if home values drop, he adds.

"We're happy because we don't have a monthly payment and we can put our money in a safe [federally insured] investment," Mr. Massey says.

If senior borrowers want to tap more equity from their home than an HECM can provide, two lenders offer jumbo reverse mortgages. Finance of America Reverse offers a loan that typically goes up to $2.25 million and is available in 14 states. The American Advisors Group has a loan that is usually capped at $3 million and is currently available in eight states. Qualification rules and terms of the loan vary by the lender. More considerations:

• **Foreclosure possible.** Even though the homeowner is not making mortgage payments, a lender could foreclose if certain required expenses, such as property taxes, homeowners' insurance premiums and homeowners' association fees, aren't paid.

• **Not under construction.** Currently HECM loans cannot be used to pay a builder for a home that is not completed. The FHA is considering a proposed rule that could lift that restriction, Mr. Bell says.

• **Non-recourse loan.** Reverse-mortgage loan amounts are based solely on the home value at the time of underwriting, which in the case of a purchase is the purchase price. So if the home loses value, neither borrower nor heir is responsible for making up the difference upon a sale.

Corrections & Amplifications:
In an earlier version of this article, American Advisors Group was incorrectly referred to as American Advisor Group. (7/20/16)