**Reverse Mortgages Expansion**

**8024.01 Can a surviving spouse remain in a home that is subject to a reverse mortgage even though the surviving spouse is not the borrower under the mortgage?**

Under a recently decided court ruling, a surviving spouse may remain in a home that is subject to a reverse mortgage even though the sole borrower on the mortgage is the deceased spouse.[[1]](#footnote-1) Because eligibility for a reverse mortgage depends upon the borrower’s reaching age 62 (see Q 8013), in some cases married taxpayers have been advised that the younger spouse can sell the home to the older spouse in a quitclaim sale. The older spouse would then qualify for a reverse mortgage, but would be listed as the sole borrower on the mortgage.

U.S. Department of Housing and Urban Development (HUD) regulations governing reverse mortgages, however, allowed the lender to demand that the loan be repaid immediately upon the death of the borrower.[[2]](#footnote-2) A group of surviving spouses who were facing foreclosure on homes that were subject to reverse mortgages challenged this rule, arguing that the HUD regulation violated a federal law because it did not protect the surviving spouse. Federal regulations provide that HUD may not issue a reverse mortgage unless it provides that the homeowner’s obligation to satisfy the loan is deferred until the homeowner’s death, the sale of the home or certain other enumerated events.[[3]](#footnote-3) Under those regulations, the term “homeowner” was defined to include the spouse of the homeowner.

The court agreed with the plaintiffs and ruled that since the regulations specifically referred to a spouse of a homeowner, rather than a co-mortgager or co-borrower, the law meant to protect a surviving spouse of a borrower-homeowner regardless of whether that surviving spouse was also a borrower under the reverse mortgage. As a result of this case, HUD regulations now provide that reverse mortgages issued after August 4, 2014 must allow the surviving spouse to remain in the home that is subject to the reverse mortgage after the borrower dies, so long as the following are true:

1. the non-borrowing spouse must be married to the borrowing spouse when the reverse mortgage is closed and must remain married to the borrowing spouse until the death of the surviving spouse,
2. the marriage must be disclosed at the time of the mortgage origination,
3. the non-borrowing spouse must be specifically named in the loan documents,
4. the non-borrowing spouse must establish legal ownership of the home or legal right to remain in the home within 90 days of the borrowing spouse’s death,
5. the non-borrowing spouse must occupy the home securing the reverse mortgage as his or her principal residence, and
6. the non-borrowing spouse must continue to satisfy all other loan obligations.[[4]](#footnote-4)

If a surviving spouse fails to satisfy the criteria enumerated above, the lender may require immediate repayment of the reverse mortgage.

* 1. **Are there any financial assessments that are required in determining a taxpayer’s eligibility for a reverse mortgage?**

Yes. As a result of several instances in which taxpayers were approved for reverse mortgages where they did not have the financial ability to maintain the home, the Federal Housing Administration (FHA) has issued new financial assessment rules in order to determine whether a taxpayer will be eligible for a reverse mortgage.

For reverse mortgages issued after January 13, 2014, in order to approve a reverse mortgage, the lender must first complete a financial assessment of the taxpayer that includes the following steps:

1. performing a credit history analysis,
2. performing a cash flow/residual income analysis,
3. documenting and verifying credit, income, assets and property charges,
4. evaluating any extenuating circumstances and compensating factors that might otherwise impact a taxpayer’s financial position,
5. evaluating the results of the financial assessment in order to determine eligibility,
6. determining if funding sources for property charges from HECM proceeds will be required, and
7. completing a HECM financial assessment worksheet.[[5]](#footnote-5)

Further, in order to qualify for a HECM reverse mortgage, a taxpayer must now fully satisfy any federal judgments and delinquent debts to the federal government (or enter into an approved repayment plan prior to closing the HECM mortgage). The FHA does not similarly require that any state or local judgments be satisfied prior to closing a reverse mortgage.

* 1. **Are there any limits on the amount of reverse mortgage disbursements that a taxpayer is entitled to receive within the first 12 months of closing?**

Yes. The U.S. Department of Housing and Urban Development (HUD) has conducted studies finding that borrowers under reverse mortgages who received all of the proceeds of the mortgage at the time of closing, or shortly after closing, had a substantially higher risk of default on the mortgage. As a result, new limitations have been introduced to ensure that taxpayer-borrowers are able to meet their financial obligations and remain in homes that are subject to reverse mortgages.

The maximum value that a taxpayer is entitled to receive from a reverse mortgage at the time the loan is closed, or within the first 12 months after closing, is now limited to 60 percent of the “principal limit” or the sum of “mandatory obligations” plus 10 percent of the principal limit.[[6]](#footnote-6) After the first 12 months, the taxpayer is entitled to access the remainder of the loan.

A taxpayer’s principal limit for a HECM reverse mortgage is essentially the maximum amount that the taxpayer is entitled to receive from the HECM before any disbursements are made. It is calculated using a formula that is based upon the age of the borrower, the expected average mortgage interest rate and the maximum claim amount that may be drawn under the loan (which factors in the value of the home and is subject to an overall cap of $625,500). See Q 8014 for a discussion of how the amount that will be available through a reverse mortgage is calculated.

Mandatory obligations include, but are not limited to, expenses such as origination and closing fees, any current mortgage debt, federal tax debt, certain repair expenses required as a condition of closing, the initial mortgage insurance premium (MIP, see Q 8022), and fees required for warranties and inspections.[[7]](#footnote-7)

These new limitations are effective for reverse mortgages issued on or after September 30, 2013.

* 1. **What are the consequences if a taxpayer receives disbursements from a reverse mortgage that exceed the new limitations that apply for 2013 and beyond?**

There are situations where taxpayer could potentially receive reverse mortgage disbursements within the first 12 months that exceed the limitations imposed for loans issued on or after September 30, 2013. While the maximum disbursement that a taxpayer is generally entitled to receive from a reverse mortgage at the time the loan is closed, or within the first 12 months after closing, is now limited to 60 percent of the principal limit, the taxpayer may also elect to receive the sum of his or her mandatory obligations plus 10 percent of the principal limit (see Q 8024.03).[[8]](#footnote-8)

The borrower under a reverse mortgage may receive initial disbursements of more than 60 percent of the principal limit in several situations, including the following:

1. the taxpayer’s mandatory obligations initially exceed 60 percent of the principal limit, or
2. the taxpayer’s mandatory obligations exceed 50 percent of the principal limit and the taxpayer elects to receive the full additional 10 percent of his or her principal limit.

If the borrower’s initial disbursement at the closing (or other disbursements within the first 12 month period) exceeds 60 percent of the principal limit, the cost of the reverse mortgage will increase. Rather than charging an initial mortgage insurance premium (MIP, see Q 8022) of 0.50 percent of the maximum claim amount, the borrower’s initial MIP will increase to 2.50 percent.[[9]](#footnote-9)

* 1. **Are borrowers under a reverse mortgage responsible for any costs relating to the property underlying the mortgage?**

Yes. In connection with the financial assessment that is now mandated by the U.S. Department of Housing and Urban Development (HUD) (see Q 8024.02), a more stringent set of rules has now been implemented to ensure that borrowers under reverse mortgages are able to pay the property charges associated with maintaining the home subject to the mortgage.

If the results of the HUD financial assessment indicate that the borrower may be financially unable to pay the property charges associated with maintaining the home, the lender has two options:

1. It may set aside a certain amount of the reverse mortgage proceeds to pay future property charges. The amount set aside is based on the life expectancy of the youngest borrower, and the current sum of the tax, hazard and flood insurance charges required to maintain the property, adjusted annually by 1.20 percent to reflect anticipated increases over the life of the mortgage;
2. It may authorize the borrower to pay property charges as they become due via withholding from the reverse mortgage monthly disbursements or line of credit.[[10]](#footnote-10)

Property charges are defined to include costs such as property taxes, hazard insurance premiums, applicable flood insurance premiums, ground rents, condominium fees, planned unit development fees, homeowner’s association fees, and any special assessments that may be levied under municipal or state law.[[11]](#footnote-11)

Despite this, if it is determined that a set-aside is required to fund the property charges, only property taxes, hazard insurance and flood insurance can be included, though the borrower remains liable for paying all other property charges that arise. Further, if the lifetime set-aside is insufficient to cover charges, the borrower remains liable for paying any property charges in excess of the set-aside.[[12]](#footnote-12)

The borrower is also entitled to specifically elect to have a set-aside or automatic withholding apply in order to cover applicable property charges even if the results of the financial assessment do not indicate that either option is necessary. If the election is voluntary, the borrower can cancel at his or her request.[[13]](#footnote-13)

1. *Bennett v. Donovan*, 2013 U.S. Dist. LEXIS 140440. [↑](#footnote-ref-1)
2. 24 CFR 206.27. [↑](#footnote-ref-2)
3. 12 U.S.C. 1715z-20(j). [↑](#footnote-ref-3)
4. HUD Mortgagee Letter 2014-07. [↑](#footnote-ref-4)
5. HUD Mortgagee Letter 2013-28. The Department of Housing and Urban Development (HUD) financial assessment guide provides detailed guidelines for the financial review, as well as the factors that must be considered in determining whether to issue the reverse mortgage. It is available at <http://portal.hud.gov/hudportal/documents/huddoc?id=13-28mlatch.pdf> (last accessed September 10, 2014). [↑](#footnote-ref-5)
6. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-6)
7. HUD Mortgagee Letter 2013-27 provides a detailed list of the types of expenses that are treated as mandatory obligations. [↑](#footnote-ref-7)
8. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-8)
9. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-9)
10. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-10)
11. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-11)
12. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-12)
13. HUD Mortgagee Letter 2013-27. [↑](#footnote-ref-13)