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Is your home a good safety net for you when you are older?

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Denice Gierach,
Owner and Founder,
Gierach Law Firm

Since we are all living longer than medical science may have predicted when we were young, many times the principal assets an older person may have will be his or her home. Since most elderly people want to stay in their homes for the rest of their lives, if their physical health allows, many are faced with a tough choice: either sell the home and move to an apartment or assisted-care facility, or make use of a reverse mortgage.

Reverse mortgages are a somewhat popular way for the elderly to make use of the equity in their homes. Many times bankers who they have always dealt with are eager to assist their elderly clients in obtaining the use of the equity in their home. If they do take this route, they argue, that senior should be able to earn more money on the cash, if it is properly invested, than the home as it may appreciate.

Just what is a reverse mortgage?

In a reverse mortgage, the lender pays the borrower/homeowner money, which could be paid out to the homeowner as a lump sum, payment in monthly payments, a line of credit or a combination of methods. The home remains titled in the name of the owner subject to the lien that the lender places on the property for the amount paid out to the homeowner. The owner is still responsible for maintaining the property, as well as the payment of insurance and real estate taxes on the home. The homeowner does not make any payments generally on the mortgage; instead, in many cases even the interest will be accrued.

This debt may actually increase over time, taking into account the amounts that the homeowner draws from time to time. After a period of time, there may be no more equity left in the home, as the amount of the draws may equal the value of the loan. There also may be times in which the amount of the loan may exceed the value of the property, which might occur when the real estate values are down. In that case, when the loan comes due, the homeowner will generally not owe more than what the home is worth.

One of the considerations about whether to use a reverse mortgage is a review of the fees. The fees for such a loan could be substantial - typically about 7 percent of the home's value. The fees are added to the loan balance generally and accrue interest over the period of the loan. All of these fees and the interest on them must be paid off when the loan is paid off. Closing costs also have an impact on the amount of the loan.

Another consideration is how much money is available to the homeowner from the loan. This number is dependent on the homeowner's age and the fair market value of the home. As a rule of thumb, an older client with a greater value in his or her home would receive more than a younger person with less equity in their home.

Another issue is that if the senior is using the proceeds received from a reverse mortgage to attempt to increase the earnings on the equity from the house, many times the yield on whatever the funds are invested in are less than the senior thought or have substantial penalties to draw the funds out until some years out.

Despite all of these issues, in some cases, the reverse mortgage is the only way out for a senior who may have been caught by an adjustable rate-type mortgage loan that adjusted above the means of the senior to pay the monthly payments. It may also be the only way for the senior to stay in his or her home for the rest of his or her life when the money runs out, even though it becomes difficult for the homeowner to leave any property to their heirs.

Denice Gierach is a lawyer and owner of The Gierach Law Firm in Naperville. She is a certified public accountant and has a master's degree in management. She may be reached at deniceg@gierachlawfirm.com or 630-756-1160.