Look Homeward, Seeker of Liquidity

By Kerry Pechter *Wed, Apr 29, 2020*

During a market crisis, a reverse mortgage home equity line of credit (ReLOC) can be a lifeline of ready cash for homeowners ages 62 and older. Don Graves of HECM Advisors Group explains.

Reverse mortgage lines of credit (ReLOCs) can be cash lifelines for older people left jobless by the COVID-19 pandemic—providing liquidity and relieving the pressure they might feel to sell stocks at distressed prices.

Throughout the pandemic, ReLOCs are also more likely than conventional home equity lines of credit (HELOCs) to remain available. One major bank, JP Morgan Chase, recently said it would temporarily stop offering HELOCs for fear that home values might drop in a roiled economy.

A program of the U.S. Department of Housing and Urban Development (HUD), ReLOCs are not so vulnerable to passing economic storms. “In theory, the government could shut down any of its loan programs, but that would typically require an Act of Congress,” said Don Graves, who educates advisers about reverse mortgages, in an interview with *RIJ* this week.

Don Graves

“HELOCs can be frozen, cancelled or reduced at the banks discretion when certain economic conditions are present. But a ReLOC can’t be arbitrarily cancelled, frozen or reduced," Graves said. He's a principal at **HECM Advisors Group** and has a Retirement Income Certified Professional designation from The American College.

Under the HUD reverse mortgage program, Americans ages 62 and older with even a small amount equity in their home (depending on their age) can borrow against it in several ways. They can convert home equity to a monthly payment, borrow a lump sum, or open a line of credit and use it as needed. If they still have a conventional mortgage, they can refinance with a reverse mortgage and eliminate their monthly mortgage payment.

Reverse mortgages can even be used finance a new home, but that was not the original intent of the program, which was designed to help older people access home equity without selling their homes, thus allowing them to "age in place."

Borrowers have the option of paying down a ReLOC, but they don't have to. The lender will recoup any outstanding loan balance, with interest, when the house is sold (usually at the death of the borrowers). If the proceeds from the sale of the home exceed the loan balance, the excess goes to the borrower's beneficiaries.

"Most of the calls I get are about eliminating a monthly payment," Graves told *RIJ*. "That's been my mantra [when I speak to groups of advisers]. If you're over 62, why have a mandatory payment when you could have a voluntary payment?" He offered an example.

"Let's say the client has a $400,000 home and a $160,000 conventional mortgage with a monthly payment of $1,000. After paying off the existing mortgage with a $160,000 ReLOC, the client still owes $160,000, but he or she doesn't have to make payments," he said.

"The loan balance will go down if he continues to make monthly payments, but he's paying down a line of credit," he added. "So he can still get the money back out. You took a nonproductive payment and restructured with a new loan that can't be frozen, cancelled or reduced." Graves noted that the unused balance of the line of credit rises each year by the amount of the interest rate on the loan plus half a percent.

> ***RIJ*** ran a multi-week series of articles on reverse mortgages in the spring of 2016. Click **here** to read the first installment in that series.

Closing costs are a common objection to opening a ReLOC. They might be $8,000 to $11,000 on a $200,000 reverse mortgage. Closing costs can be added to the loan.

A ReLOC can pay for itself during a financial crisis, Graves tells skeptics, by providing liquidity and preventing the forced sale of depressed assets. "**Wade Pfau, Ph.D**., has told advisers to use the ReLOC as a volatility buffer. His research shows that the benefit of avoiding the impact of just one bad year in the market makes the costs of creating the ReLOC negligible by comparison," he said. Pfau recently published a **book** on reverse mortgages.

Advisers should feel a professional obligation to understand ReLOCs, Graves said. "Advisers who have retiring or retired clients and who hold themselves out to be 'holistic,' should reasonably be expected to say, 'Let's look at all of your assets, including your housing wealth.' Most of my 21 years in this business has been spent convincing advisers how this fits into their clients' plans. I give them a framework for using the reverse mortgage," he told *RIJ*.

Low interest rates may reduce the yields of bonds and payout rates of annuities, but they favor ReLOCs by allowing homeowners to borrow more than they could if mortgage lending rates were higher. "We're seeing a movement that won't go away," Graves told *RIJ*. "Advisers haven't paid attention because the hoof-beats of the bull market drowned out more conservative strategies."