Reverse Mortgage Borrowing and Financial Well-Being of Older Adults

Research Brief

Final

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Executive Summary

Understanding the financial well-being of older adults is increasingly important as concerns about insufficient retirement savings and debt burdens grow. The primary asset for many older adults is the equity in their homes—yet home equity is illiquid and can only be accessed by selling the home or borrowing through a mortgage. Most older adults express a strong desire to remain in their homes, yet some cannot afford monthly payments associated with borrowing through a mortgage. Reverse mortgages allow older adults to access the equity in their homes without repayment until the termination of the loan. The most widely used reverse mortgage product is offered by the Federal Housing Administration's Home Equity Conversion Mortgage (HECM) program, first initiated in the Housing and Community Development Act of 1987 (Pub.L. 100-242). Reverse mortgages are designed to improve the financial stability of adults age 62 and older by providing a way to "supplement Social Security, meet unexpected medical expenses and make home improvements" (HUD, 2006). Despite potential benefits, reverse mortgages have been widely criticized and hold a negative public image. Reasons include the costs associated with obtaining a HECM loan, a general aversion to mortgage debt, a desire to pass the home on to heirs, and the high complexity of this financial product.

The purpose of this study is to explore the financial well-being of older adults who hold reverse mortgages. How does the financial well-being of reverse mortgage borrowers compare to the financial well-being of otherwise similar older adults without reverse mortgages? What borrower characteristics at the time of pre-reverse mortgage counseling are associated with higher and lower levels of financial well-being two to five years after originating the loan? How is the amount of the initial withdrawal from the reverse mortgage related to subsequent financial well-being?

We use several survey and administrative data sets. They include the Aging in Place survey, a national data set of reverse mortgage borrowers collected by the research team from April to July 2017. A total of 380 respondents answered the Financial Well-Being short scale items, which were collected two to five years after loan origination. The Aging in Place survey is merged with HUD reverse mortgage counseling data, the National Council on Aging's Financial Interview Tool data, the borrower's credit score, and HECM loan data from the U.S. Department of Housing and Urban Development. In addition, we use the National Financial Well-Being survey of respondents age 62 and older who own a home.

Key findings are:

- The Financial Well-Being score of older reverse mortgage borrowers is about six points lower than the score of older homeowners of the general population. However, this difference is primarily due to differences in financial and socio-demographic characteristics. Holding constant these characteristics, the Financial Well-Being scores of older reverse mortgage borrowers do not significantly differ from the Financial Well-Being scores of older homeowners in the general population.

- Credit score at the time of required pre-reverse mortgage counseling is positively associated with Financial Well-Being scores two to five years after reverse mortgage origination in the reverse mortgage sample. Other financial indicators at the time of counseling, including those collected as part of the Financial Interview Tool score, are not significantly associated with higher Financial Well-Being scores in later years.

- Withdrawals of reverse mortgage proceeds at loan origination, whether used to pay-off a prior mortgage (mandatory withdrawal) or for other purposes (discretionary withdrawal), do not predict Financial Well-Being scores two to five years later. Two other indicators of reverse mortgage borrowing are associated with higher Financial Well-Being scores: a limit) and lower mortgage debt at origination.

The findings from this study inform both research and practice. This study contributes to an understanding of the longer-term financial wellbeing outcomes of reverse mortgage borrowers. Most national survey samples do not identify reverse mortgages or lack a sufficient sample of reverse mortgage borrowers for meaningful analysis—this being an advantage of the Aging in Place survey. For practice, the findings of this study indicate that credit scores at the time of pre-reverse mortgage counseling can serve as a meaningful tool to predict reverse mortgage borrowers' financial well-being in future years. These lower credit score borrowers may benefit from additional resources and support before and after closing on the reverse mortgage. This support could be provided by counseling agencies, lenders, or the Federal Housing Administration.

1. Background

The primary aim of this study is to understand the financial well-being of older adults who borrow through a reverse mortgage. The most widely used reverse mortgage is the Federal Housing Administration's Home Equity Conversion Mortgage (HECM), with more than 1.13 million loans originated through August of 2019. Although a relatively small share of the eligible population of homeowners holds a reverse mortgage, this is a critical population given the growing levels of debt and limited assets of older adults—the primary form of which is held as home equity among many older adults (Moulton et al., 2017; The Federal Reserve Board, 2016).

Considerable heterogeneity in financial well-being has been identified in a national sample of reverse mortgage borrowers. While the mean standardized Financial Well-Being score of the reverse mortgage borrowers in this sample is 55, scores range from 37 at the 10th percentile of the distribution of respondents to 76 at the 90th percentile. Compared to the general population, a score of 37 is considered a "low" Financial Well-Being score and a score of 76 is considered a "very high" Financial Well-Being score (CFPB, 2019).

In this research study, we estimate the extent to which this variation in financial well-being is associated with demographic and financial characteristics of borrowers at the time of the mandatory pre-reverse mortgage counseling session. Our administrative data at the time of counseling include individual level responses to the National Council on Aging's Financial Interview Tool. Starting in 2010, the Financial Interview Tool was a required part of counseling for almost nine years. The tool was intended to help counselors identify older adults for whom the reverse mortgage may be a poor financial solution based on their housing, health, and financial status. In line with the capability framework (CFPB, 2018), an objective of our study is to identify how these factors at the time of counseling are associated with financial well-being later in life. Our data allow us to examine a range of factors, including detailed reverse mortgage borrowing data, socio-demographic characteristics, financial status, health situation, and housing characteristics. No research to date has analyzed the extent to which these potential factors predict subsequent financial well-being for reverse mortgage borrowers.

Aside from borrower characteristics, we estimate the extent to which the percent of available equity withdrawn up-front on a reverse mortgage is associated with subsequent financial well-being. We consider two separate components of the amount withdrawn—the amount to pay off forward mortgage debt (required withdrawal) and the amount of additional discretionary funds taken as a lump sum at closing (discretionary withdrawal). Prior studies have found that an increase in the initial discretionary withdrawal of the reverse mortgage is associated with an increased risk of default on property taxes and homeowners insurance (IFE, 2014; Moulton et al., 2015).

Taken together, this study provides new, original knowledge to research and practice by contributing to the understanding of the longer-term outcomes of reverse mortgage borrowing. Second, this study introduces the Financial Well-Being scale to researchers in the large fields of aging and housing research. Most importantly, for practice, this study informs about factors identified at the time of the mandatory reverse mortgage counseling session that are associated with subsequent lower levels of financial well-being. These factors can be used to tailor information and resources to prospective borrowers.

2. About the Study

This research informs the following questions:

RQ1: How does the financial well-being of reverse mortgage borrowers compare to the financial well-being of otherwise similar older adults who own their homes and do not have reverse mortgages?

RQ2: How are various financial, housing, health and socio-demographic characteristics of reverse mortgage borrowers at the time of reverse mortgage counseling associated with financial well-being among two to five years later?

RQ3: How is the initial withdrawal (for both mortgage debt and other purposes) from the reverse mortgage related to subsequent financial well-being?

To inform our research questions, we begin with a descriptive comparison of the characteristics of reverse mortgage borrowers relative to older adults in the general population. We then compare the financial well-being of reverse mortgage borrowers to older adults with otherwise similar financial and demographic characteristics. Next, we conduct descriptive comparisons of means and multivariate regression analysis to identify the factors at the time of counseling that are associated with subsequent higher and lower levels of financial well-being. Finally, we estimate the extent to which the amount of the initial withdrawal is associated with subsequent financial well-being, treating the amount of the withdrawal as an endogenous choice.

We use several survey and administrative data sets. First, we use the Aging in Place survey, a national survey of reverse mortgage borrowers conducted by the research team from April to July 2017. This was a second wave of the survey previously administered by the research team in

2014/15 (Moulton et al., 2017). The second wave of the Aging in Place survey data collection started four months after the National Financial Well-Being survey was completed, which was collected from October to December 2016 (CFPB, 2017). The second wave of the Aging in Place sample consists of 411 adults aged 62 and older who obtained a reverse mortgage between two and five years prior to the survey.

Second, the Aging in Place survey is merged with four administrative, client-level data sets collected at counseling and subsequent loan origination: 1) reverse mortgage counseling data from the U.S. Department of Housing and Urban Development; 2) reverse mortgage borrower loan data from the U.S. Department of Housing and Urban Development; 3) the National Council on Aging's Financial Interview Tool; and 3) the reverse mortgage borrowers' credit score at loan origination. For a comparison sample, we use the National Financial Well-Being survey of respondents age 62 and older who own a home.

The Aging in Place sample includes respondents who were counseled for a reverse mortgage by Clearpoint Credit Counseling Solutions, a national, HUD-approved 501(c)(3) nonprofit housing counseling agency. Reverse mortgage borrowers who received pre-reverse mortgage counseling from Clearpoint between January 2012 and April 2015 (n=4,624) are included in the second wave of the Aging in Place survey. Of this group, 3,546 had accurate contact information for the follow-up survey; 411 borrowers completed the survey. Of those, 380 survey respondents had non-missing data for the Financial Well-Being score. The comparison group are respondents of the Financial Well-Being survey age 62 and older who own their home, a total of 1,909 respondents.

3. Findings

3.1. How does the financial well-being of reverse mortgage borrowers compare to the financial well-being of otherwise similar older adults who own their homes and do not have reverse mortgages?

We first compare the Financial Well-Being score of reverse mortgage borrowers two-to-five years after they receive the reverse mortgage to that of older homeowners in the general population. We find that reverse mortgage borrowers have an average score of 56 compared to an average score of 62 for older homeowners in the general population—a difference that is statistically significant. It is not surprising that reverse mortgage borrowers have lower Financial Well-Being scores given that they have lower incomes and financial wealth than older adults in the general population. For example, the median income of reverse mortgage borrowers is $3,477, compared to $6,242 for older homeowners in the general population.

We next measure the Financial Well-Being scores of reverse mortgage borrowers relative to older homeowners in the general population who are similar to reverse mortgage borrowers with regard to key financial and socio-demographic characteristics. To do this, we create weights that represent the likelihood of being in the reverse mortgage sample, and then include these weights in our data so that the respondents in the general population are more similar to respondents in our reverse mortgage sample with regard to gender, age, race, marital status, household size, educational attainment, income, ownership of financial and retirement savings, and home value. After applying the weights, we observe that the Financial Well-Being score of reverse mortgage borrowers is not statistically different from that of older homeowners with similar characteristics who do not hold a reverse mortgage.

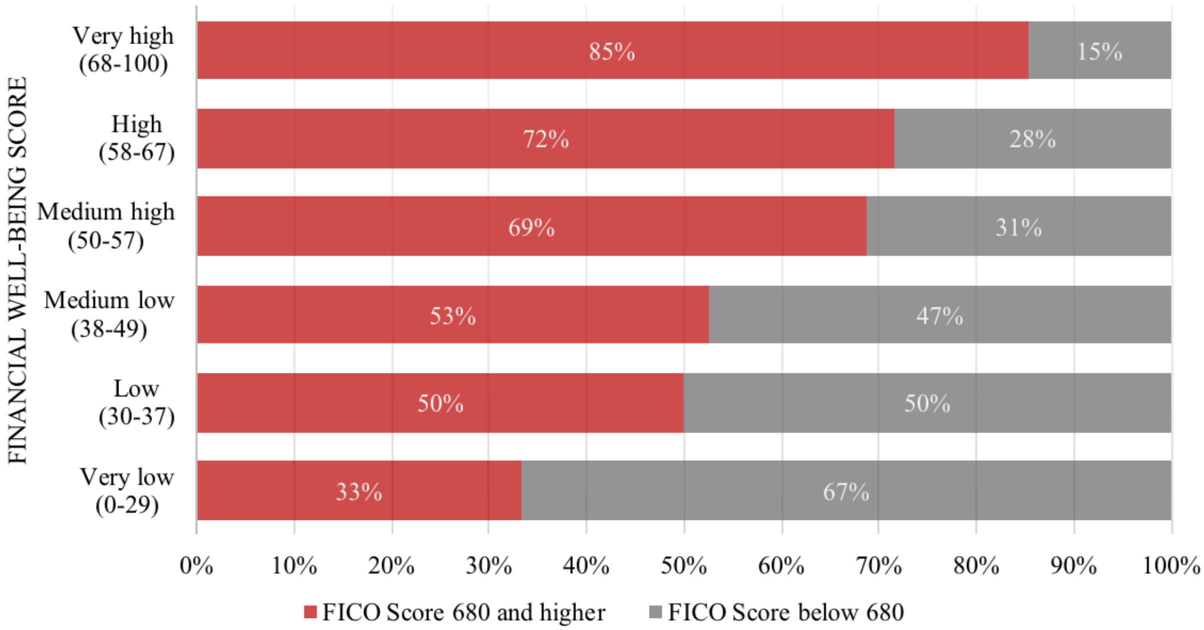
3.2. How are various financial, housing, health and socio-demographic characteristics of reverse mortgage borrowers at the time of reverse mortgage counseling associated with financial well-being two to five years later?

We next present findings on the relationship between characteristics of reverse mortgage borrowers at the time of pre-origination counseling and Financial Well-Being scores two-to-five years after origination. The CFPB defines Financial Well-Being scores below 50 to be indicative of financial vulnerability (CFPB, 2017), and we thus use a score of 50 as the threshold for this comparison. In our sample of reverse mortgage borrowers, 33 percent have Financial Well-Being scores below 50, compared to 67 percent with Financial Well-Being scores of 50 and higher.

First, reverse mortgage borrowers with lower credit scores at the time of origination of the reverse mortgage have lower Financial Well-Being scores two to five years later. The mean difference in credit scores between those with lower to those with higher levels of Financial Well-being is 49 points and it is statistically significant; the significant relationship is confirmed in multivariate regression analysis and aligns with findings for the general population (Nagypál & Tobacman, 2019).

Figure 1 illustrates the association of credit score and Financial Well-Being score. In this figure, Financial Well-Being scores are categorized in buckets, following a recent "toolkit" report of the CFPB (2019). The credit scores are split at the 680 score mark, which represents a threshold frequently used in mortgage underwriting to indicate a good credit score. The figure documents that reverse mortgage borrowers with good credit scores at origination are more likely to have higher Financial Well-Being scores in later years. For example, of the reverse mortgage borrowers in the "high" Financial Well-Being score range of 58 to 67, 72% have a credit score of 680 or higher.

Figure 1: Alignment of Financial Well-Being score and credit score among reverse mortgage borrowers



We next identify the extent to which the responses on the Financial Interview Tool administered at the time of counseling are associated with subsequent financial well-being. The Financial Interview Tool is a 43-item questionnaire that results in an overall risk score. Our results indicate that there was no statistical difference in the average Financial Interview Tool risk score of reverse mortgage borrowers at the time of origination with lower and higher FWB scores two and five years later. Similarly, the Financial Interview Tool score does not predict the Financial Well-Being score in a multivariate regression analysis.

However, in addition to the overall risk score that is assessed by 19 questions of the 43-question Financial Interview Tool, we also looked at the relationship between *individual* items on the Financial Interview Tool and financial well-being. Responses to individual Financial Interview Tool questions show that those with lower health, a greater need to pay off debt with reverse mortgage proceeds, lesser flexibility to invest the reverse mortgage proceeds, and plans to stay in their home at least the next three years at the time of counseling were statistically more likely to have lower financial well-being two-to-five years later.

Third, we investigate the extent to which socio-demographic characteristics are associated with lower and higher subsequent Financial Well-Being scores. Race is the only significantly different demographic indicator, with a larger proportion of borrowers who are black having higher Financial Well-Being scores, despite having lower credit scores (on average, their credit score is 653; the difference is 60 points). This finding is confirmed in multivariate regression analysis.
We observe no significant differences in the financial characteristics of borrowers with lower versus higher Financial Well-Being scores.

3.3. How is the initial withdrawal (for both mortgage debt and other purposes) from the reverse mortgage related to subsequent financial well-being?

The third research question examines the association of required and discretionary withdrawals from the reverse mortgage loan at loan origination with the Financial Well-Being score two to five years past origination. During our study period, HUD initiated a policy change that limited the amount of the up-front withdrawal to 60 percent of available proceeds, with exceptions for higher draw amounts if needed to pay-off a forward mortgage. We model the discretionary withdrawal amount as an endogenous choice variable, using as instruments the policy changes in April and October 2013 that limited the withdrawal amount.

The regression results show that the proportion of funds withdrawn by borrowers at the time of origination is not significantly associated with the Financial Well-Being score two to five years later. This is true regardless of whether the money is withdrawn to pay off a mortgage (mandatory) or for other reasons. However, the regression results show that an overall higher loan limit on the reverse mortgage (the initial principal limit) is associated with a higher subsequent Financial Well-Being score at the 10 percent significance level. Holding a larger amount of mortgage debt prior to originating the reverse mortgage is associated with a lower Financial Well-Being score, this at the 5 percent significance level. It is important to caution that these associations are not causal. For example, we do not observe the financial well-being of reverse mortgage borrowers prior to originating a reverse mortgage, and we thus do not know if those with higher levels of mortgage debt also had lower levels of financial well-being before originating a reverse mortgage.

4. Conclusion

The findings from this study inform both research and practice. First, this study contributes to an understanding of the longer-term financial wellbeing outcomes of reverse mortgage borrowers. Most national survey samples do not identify reverse mortgages or lack a sufficient sample of reverse mortgage borrowers for meaningful analysis—this being an advantage of the Aging in Place survey. For practice, the findings of this study indicate that credit scores at the time of pre-reverse mortgage counseling can serve as a meaningful indicator to predict reverse mortgage borrowers' financial well-being in future years. A secondary indicator of future financial well-being is traditional forward mortgage debt at time of reverse mortgage origination. These lower credit score, higher mortgage debt borrowers may benefit from additional resources and support before and after closing on the reverse mortgage. This support could be provided by counseling agencies, lenders, or even the Federal Housing Administration.

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