SUBPRIME REVISITED

How Reverse Mortgage Lenders Put Older Homeowners' Equity at Risk

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Subprime Revisited: How Reverse Mortgage Lenders Put Older Homeowners' Equity at Risk

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I. Introduction

The U.S. Office of the Comptroller of the Currency and other federal regulators that oversee banks were slow to recognize the threat posed by the recent boom in subprime mortgage lending, and slow to act. So it was noteworthy when, in June 2009, Comptroller John C. Dugan, went before a gathering of bankers and warned of a danger growing in a market designed to serve the nation's seniors: "While reverse mortgages can provide real benefit, they also have some of the same characteristics as the riskiest types of subprime mortgages—and that should set off alarm bells."[1]

During 2008 more than 100,000 seniors used reverse mortgages to tap more than $17 billion in home equity.[2] Within the mortgage industry, reverse mortgages continue to grow despite the economic downturn, with volume more than doubling between 2005 and 2008.[3] Despite a summer slowdown in originations, 2009 still appears to be on pace for a record year.

Certainly, the continuing availability of reverse mortgages is good news for seniors who need to cash out some of their housing wealth to supplement Social Security, to meet unexpected medical costs, or to make needed home repairs. But growth in the reverse mortgage market has unleashed other, more malign forces.

Many of the same players that fueled the subprime mortgage boom—ultimately with disastrous consequences—have turned their attention to the reverse market. Lenders, including some of the nation's largest banks, view that market as a source of profits that have dried up elsewhere. Mortgage brokers see it as a new source of rich fees. Predators who once reaped profits from exotic loans have now focused on wresting more wealth from vulnerable seniors. And securitization, which allowed subprime loan originators to disassociate themselves from the downside risks of abusive lending, is becoming commonplace in the reverse mortgage industry.

Reverse mortgages are complicated. The opportunities for abuse abound. Seniors, many of whom lack experience with complex financial products, often depend upon lenders and brokers for expertise and guidance. Reverse mortgage lenders, like subprime lenders, emphasize the benefits that they provide to borrowers and often tout their commitment to responsible lending principles. However, such claims are undermined by a growing public record of how subprime lenders—including some now active in the reverse mortgage market—profited from acting irresponsibly during the recent mortgage boom.

In addition, reverse mortgage lenders have followed in the footsteps of their subprime counterparts by using financial incentives to reward brokers for arranging deals that boost lenders' profits and raise the costs paid by borrowers. By adjusting reverse mortgage loan terms, such as interest rates, servicing fees, rate adjustment intervals and distributions, brokers and lenders can maximize their profits at the expense of senior homeowners.

Seniors are also vulnerable to other abuses associated with reverse mortgages. Some seniors have been persuaded to sink proceeds from reverse mortgages into complicated annuity contracts or expensive long-term care insurance products. These products generate large commissions for sellers, but frequently prove financially toxic for senior homeowners.

While counseling is required for all borrowers of *federally insured* reverse mortgages, only a handful of states require counseling for all types of reverse mortgages. And while quality counseling can be helpful to seniors, counseling remains inconsistent and underfunded.

There is now an urgent need for more safeguards at the federal and state level to protect consumers from reverse mortgage abuse, to help seniors preserve their home equity, and to ensure that reasonably priced and fairly structured reverse mortgages are available for those who truly need them. To strengthen protections, states and the federal government should:

- Create suitability standards for reverse mortgages and other equity conversion products requiring lenders and brokers to only arrange deals that do not harm the financial well-being of seniors;
- Strengthen borrower counseling, which to date remains inconsistent and underfunded;
- Ban yield spread premiums, which incent brokers to make loans more profitable for lenders and investors at the expense of borrowers;
- Regulate proprietary reverse mortgages and other equity conversion products, which are not federally insured and not subject to existing federal reverse mortgage regulations; and
- Improve data collection on reverse mortgages and other equity conversion products that are not currently reportable under the Home Mortgage Disclosure Act.

II. Reverse Mortgage Basics

Reverse mortgages enable senior homeowners to convert equity in their homes into cash without having to move out. Under a traditional "forward" mortgage, the lender advances the principal at the origination of the loan, and the borrower pays off the balance of the loan with monthly payments. Under a reverse mortgage, the lender advances funds to a borrower as a lump sum, in monthly payments, through a line of credit, or a combination of these options. The borrower does not make monthly payments on this loan. Instead, over time, the reverse mortgage balance rises as a result of additional advances, accruing interest, and fees. Seniors generally use reverse mortgages to tap home equity while remaining in their homes, but some programs allow borrowers to purchase homes with a reverse mortgage.

Reverse mortgage borrowers must be at least 62 years of age and must generally own their own homes free and clear or with a minimal amount of outstanding liens. Because reverse mortgages are essentially equity-based transactions, there are no income or credit qualifications.

The entire balance for a reverse mortgage loan is due at maturity. When the loan matures depends on whether the loan is a "tenure loan" or a "term loan." For tenure loans maturity occurs when the borrower dies, sells, or fails to continue to occupy the home for at least a year. Term reverse mortgages mature after a fixed term of years.

There are two principal types of reverse mortgages: Home Equity Conversion Mortgages (HECMs) and proprietary reverse mortgages. HECM loans, which are discussed below, are federally insured and make up the vast majority of the reverse mortgage market. HUD promulgates regulations with respect to HECM loans, some of which are intended to curb abusive lending. Proprietary reverse mortgages, which are discussed in section VIII, are equity conversion products that are developed and backed solely by private financial institutions. Proprietary reverse mortgages lack even the basic federal consumer protections that apply to HECM loans.

HECM Loans

The Home Equity Conversion Mortgage (HECM) program was designed to meet the needs of senior homeowners by reducing economic hardship that results from increasing costs of health, housing, and subsistence needs at a time of reduced income.[4] The program is one of many single-family mortgage insurance programs administered by the Department of Housing and Urban Development.[5] As with all HUD-insurance programs, borrowers pay premiums for the insurance and HUD guarantees that the lender will be repaid, up to specified limits, for extending credit to the homeowner.[6] Under the HECM program, the senior homeowner is also protected by HUD in the event the lender is unable to fulfill its payment obligation.[7] The HECM loan is only available through HUD-approved lenders.

Under the HECM program borrowers have a choice of receiving mortgage payments through five basic payment plans: tenure, term, line-of-credit, modified tenure, and modified term.[8] The amount that can be borrowed is based on the maximum claim amount, the age of the youngest borrower, and expected average mortgage interest rates. The maximum claim amount is the lesser of the appraised value of the home or the maximum amount that HUD will insure. The Housing and Economic Recovery Act of 2008 set the maximum claim amount for HECM loans at $417,000.[9] The limit has been temporarily increased for 2009 to $625,500.[10]

Because interest is generally the largest single cost of any reverse mortgage, the expected interest rate is an important factor in calculating the funds available to senior homeowners. While some fixed-rate HECM loans have been available, most come with adjustable rates, as allowed by statute.[11]

HECMs were designed to be "non-recourse" loans, which means that the borrower (or his or her estate) is never supposed to owe more than the loan balance or the value of the property, whichever is less.[12] HECM loans may be prepaid, in whole or in part, without penalty.[13] Borrowers are generally required to keep the property in good repair and pay property taxes and hazard insurance premiums in a timely manner.[14]

HECM loans have a number of costs and fees that are borne by the borrower. Borrowers may be charged for document preparation, appraisals, title and tax searches, flood zone searches, inspection fees, tax reporting services, attorney's fees, and origination fees. Origination fees are limited to the greater of 1) $2,500 or 2) two percent of the maximum claim amount up to $200,000, plus one percent of any portion of the maximum claim amount that is greater than $200,000.[15] Notwithstanding this formula, origination fees are capped at $6,000.[16] For example, the maximum origination fee for a $300,000 HECM loan would be $5,000 ($200,000 × .02 + $100,000 × .01). In addition, HECM borrowers must pay mortgage insurance premiums (MIP) and a monthly servicing fee. The upfront MIP for an HECM loan is equal to 2% of the maximum claim amount. The upfront MIP on a $300,000 HECM loan is $6,000. The initial mortgage insurance premium and other costs commonly are financed with the proceeds of the loan itself.

After the closing, a monthly MIP accrues daily on the mortgage balance at a rate of 0.5% a year and is paid by the lender to HUD. Borrowers also are typically charged a fixed monthly servicing fee, ranging from $25 to $35. MIP amounts and servicing fees are added monthly to the borrower's mortgage balance.

HECM loans have been the workhorse of the reverse mortgage industry since they were created. The enabling statute and subsequent amendments have attempted to stem abusive practices by providing borrowers with some basic consumer protections. For example, Congress has mandated that HECM borrowers obtain "adequate counseling" by an independent third party before entering into a reverse mortgage transaction.[17] Congress has capped the origination fee that lenders can charge to borrowers. More recently, Congress has banned the selling of other financial and insurance products, such as annuities, in conjunction with HECM loans. While these statutory requirements provide important protections to borrowers, they are unlikely to counteract the market forces that drive inappropriate or abusive lending.

III. Origins and Evolution of Reverse Mortgages

Equity conversion products such as reverse mortgages have been around since the early 1960s. Initially offered on a very limited basis by private financial institutions, equity conversion loans varied widely and were largely unregulated. Early products included shared appreciation mortgages, reverse annuity mortgages, deferred payment loans, and sale/leaseback arrangements.

Through the early 1980s, financial institutions, eager to take advantage of home equity growth among seniors, attempted to expand the reverse mortgage market. In 1980, a group of California banks created a nonprofit reverse mortgage joint venture. [18] In 1983, the nation's first for-profit reverse mortgage company, American Homestead Mortgage Co., was launched.[19] Despite the potential for reverse mortgages to open up a new source of income for millions of Americans, these early efforts faltered. By mid-1988, American Homestead had underwritten only 1,200 loans.[20] The California venture collapsed within a decade. [21]

While private lenders were interested in exploiting new business opportunities, senior advocates and academics championed reverse mortgages as a way to reduce the impact of poverty upon elderly homeowners. Advocates pushed policymakers to create a standard equity conversion product that would be widely accepted by the lending industry and that would provide basic consumer protections for potentially vulnerable senior homeowners.

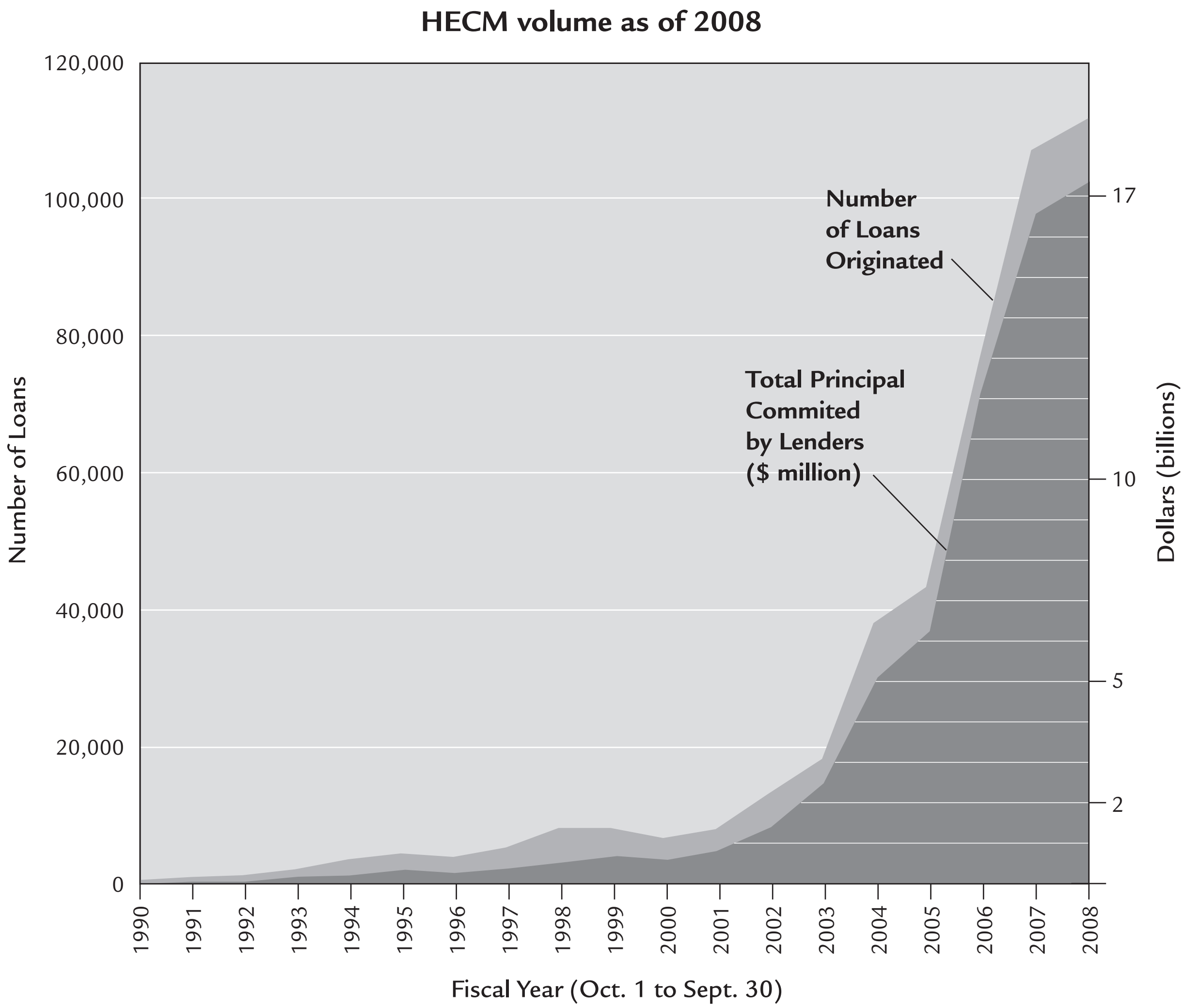
Congress responded in 1988 by authorizing a demonstration program through which the Federal Housing Administration would provide reverse mortgage insurance.[22] Originally limited to 2,500 mortgages, the total number of insured mortgages under the government's Home Equity Conversion Mortgage (HECM) program now exceeds 425,000.[23] The annual volume of HECM loans has climbed rapidly over the past ten years.[24] In fiscal year 2001, 7,781 HECM loans were originated. By the end of fiscal year 2008, the annual volume of HECM loans topped 112,000, representing an incredible 1,300% increase in loan volume in just six years. The monthly HECM volume reached a record high in April 2009, with 11,660 HECM loans originated.[25]

The HECM program has dominated the reverse mortgage market since its inception, but there have been alternatives. In 1996, Fannie Mae developed its own reverse mortgage—the Home Keeper—to serve borrowers with higher property values, condominium owners, and seniors wish-

A DEARTH OF DATA

Currently, there is a dearth of publicly available information on proprietary reverse mortgages. While HUD provides monthly reports describing basic loan and borrower characteristics for HECM loans, no comparable information is available for non-HECM loans. The Home Mortgage Disclosure Act (HMDA),[27] which provides extensive information on home mortgage applications, including approval rate, socioeconomic characteristics of applicants, and some mortgage pricing information, covers few, if any, reverse mortgage transactions.

Under HMDA, reverse mortgages are subject to the general rule that lenders must report applications or loans that meet the definition of a home purchase loan, a home improvement loan, or a refinancing. However, the definition of refinancing is limited to "a new obligation that satisfies and replaces an existing obligation by the same borrower."[28] As a result, lenders would not need to report reverse mortgage transactions where borrowers' homes are owned free and clear prior to the transaction. Additionally, reporting is optional if the reverse mortgage includes a line of credit for home improvement or home purchase.[29] These two exceptions eliminate required reporting of most reverse mortgages. Even in cases where reverse mortgages are required to be reported, HMDA currently provides no way to distinguish them from traditional forward mortgages.



Source: U.S. Department of Housing and Urban Development, "HECM cases endorsed for insurance by fiscal year," posted on-line at www.hud.gov/offices/hsg/comp/rpts/hecm/hecm0908.xls

ing to use a reverse mortgage to purchase a new home. The Home Keeper reverse mortgage was discontinued as of December 31, 2008.

Private financial institutions also have offered a variety of equity conversion products, such as shared appreciation mortgages and proprietary reverse mortgages. A widely held view is that proprietary reverse mortgages make up approximately 5–10% of all reverse mortgages originated.[26] With today's sagging housing prices, frozen capital markets, and new higher loan limits for the HECM program, the percentage of proprietary reverse mortgages is probably significantly smaller. However, economic recovery over the next few years is likely to reinvigorate proprietary reverse mortgage products, which to date remain almost entirely unregulated.

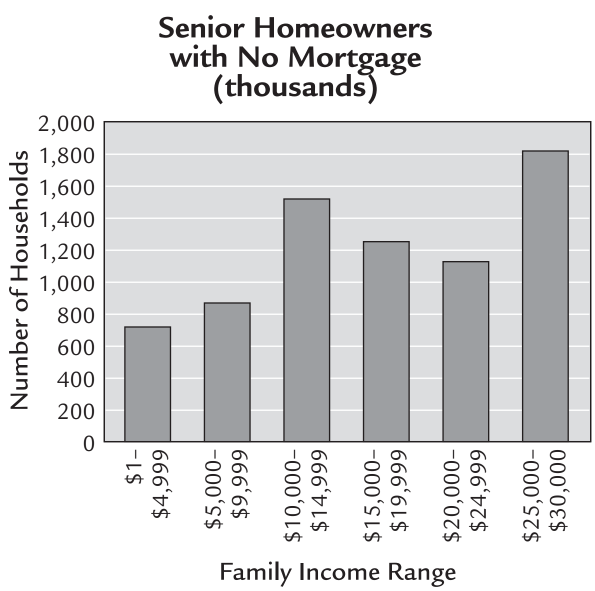
IV. "[T]he Senior Market is a Goldmine"[30]

The senior population of the United States is expected to grow rapidly, from 35 million in 2000 to 64 million by 2025.[31] Seniors are also expected to account for a growing share of the population—about 18 percent in 2025, up from 12 percent in 2000.[32]

At first glance, seniors may not seem to constitute a rich market. In 2007, the median annual income of those aged 65 and older was $17,382, or just under $1,500 per month.[33] But a closer look reveals that seniors do, in fact, possess considerable wealth. As one study noted, "Residential real estate has grown to become the largest single asset class held by households with heads aged 65 or older."[34] Data from the most recent American Housing Survey reveals that over 18 million seniors (65 and over) own their homes.[35] Approximately 15 million of those homeowners are potential reverse mortgage borrowers, including more than 12.4 million with no mortgage debt and 2.6 million with mortgage debt of less than 40 percent of the value of their house.[36]

Reverse mortgage lenders have estimated that seniors hold as much as $4 trillion in home equity.[37] Data from the American Housing Survey supports a more conservative figure, $2.8 trillion.[38] Regardless of where in the range the true value lies, there is no question that seniors—even many of the poorest—have significant home equity available to be tapped by the reverse mortgage industry. In 2007, the American Housing Survey found that more than 700,000 seniors with annual incomes below $5,000 owned their houses free and clear, while another 2.4 million with annual incomes below $15,000 had no mortgages.[39] All told, more than 7 million seniors with annual incomes below $30,000 owned their homes outright.[40]

That treasure trove of home equity has not escaped the notice of lenders, brokers, and Wall Street investors.



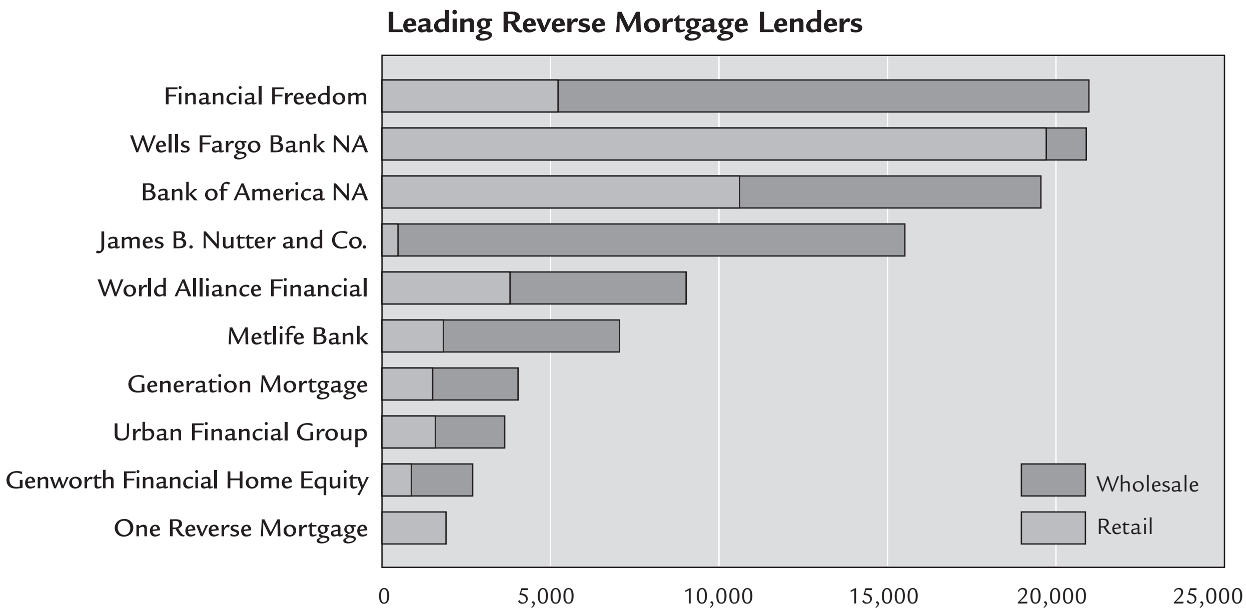
V. A Multi-Billion Dollar Opportunity

> *"The potential origination fees for Reverse Mortgages today are in excess of $42-Billion. How will you get your share?"*[41]

While reverse mortgage lending remains a niche in the multi-trillion dollar banking industry, it has begun to attract the interest of banks, insurance companies, mortgage brokers, and Wall Street investors looking for new profit centers in the wake of the subprime mortgage meltdown. The growing presence of these players in this once overlooked submarket highlights the need for safeguards to protect vulnerable seniors and to prevent a recurrence of abuses that were widespread during the subprime frenzy.

The Lenders

In today's mortgage markets, lenders' profits are driven by loan volume, loan amounts, and interest rates. Reverse mortgage lenders are no exception. As in the forward mortgage business, most reverse mortgage loans have been sold to Fannie Mae or into the secondary market rather than held by lenders for investment purposes.[42] The sale of the loans allows lenders to replenish their capital so that they can make more loans. Each loan generates transaction fees, based in large part on the size of the loan. Loans with higher interest rates garner a higher sales price in the secondary market. Larger loan amounts generally



Note: Figures are for 12-month period that ended May 31, 2009.
Source: Reverse Mortgage Insight

produce larger fees, and greater loan volume translates into greater profits.

The subprime debacle showed that loan originators too frequently sacrificed responsible lending in the name of greater volume, higher fees, higher interest rates, and more profits. Many industry analysts agree that the subprime bust resulted from "lenders chasing volume by relaxing underwriting standards."[43] And, the so-called "vigorous competition" among subprime originators was, in fact, a race to the bottom—a race that led to improvident lending on a massive scale.

The same forces once at work in the subprime market are now growing in the reverse mortgage market. Competition in the reverse market is heating up, with more than 2,700 lenders offering HECMs.[44] According to a recent GAO report, more than 1,500 lenders originated their first HECM loans in 2008.[45] The combination of increased competition, volume-generated profits, and the vast number of potential reverse mortgage borrowers is a recipe for inappropriate and abusive reverse mortgage lending.

Leading reverse mortgage lenders often tout their commitments to responsible lending. But with so much money to be made in the reverse mortgage market, policymakers and future reverse mortgage borrowers need to weigh lenders' claims against their past lending practices.

Some major lenders in the subprime market have emerged as significant players in the reverse mortgage niche. For example, in 2006 Wells Fargo was a leading subprime lender, according to industry publications.[46] Today they are a leader in the reverse mortgage market, originating nearly 20,000 HECM loans in 2008.[47] Wells Fargo espouses its responsible mortgage lending principles such as only making loans that demonstrate benefit to the borrower and a commitment to provide consumers with information necessary to make fully informed decisions about the loan terms.[48]

Yet Wells Fargo failed to adhere to those responsible lending practices in the subprime market, according to a lawsuit filed by the City of Baltimore. The lawsuit claims that Wells Fargo had a systemic practice of steering subprime borrowers into bad loans.[49] An affidavit from a former loan officer and sales manager describes a system in which commissions and referrals were "set up in a way that made it more profitable for a loan officer to refer a prime customer for a subprime loan than make the prime loan directly to the customer."[50] Similarly, the Illinois Attorney General recently filed a complaint against Wells Fargo alleging that the company "provided significant incentives for its employees to steer borrowers into subprime mortgages" and that its fair lending policies "were only on paper."[51]

Other reverse mortgage lenders have also put themselves forward as responsible lenders. James B. Nutter, the second largest wholesale originator of reverse mortgages,[52] claims a pristine record of responsible lending. In December 2007, George Lopez, a Nutter executive, told the U.S. Senate Special Committee on Aging that in the previous year his firm "received no complaints of any kind related to unscrupulous third parties taking advantage of our seniors."[53] Because of sound lending principles, Lopez claimed that "the evils of mortgage fraud and deceptive advertising practices have not yet crept into the mainstream of the reverse mortgage industry." Finally, Lopez assured the panel that "'fly-by-night' brokers are effectively prevented from entering the market" because they must be FHA-approved.[54]

Just weeks before Lopez' testimony, however, his company underwrote a reverse mortgage that was used to siphon multiple high fees from the equity of a vulnerable senior, according to a lawsuit filed by the victim's family. The lawsuit describes how the loan was used by 87-year-old Creighton Collins, a retired truck driver with an eighth grade education, to cash out $274,000 of home equity, and how Collins paid the high costs typical of reverse mortgages, including a $7,225 fee to the broker who arranged the loan, a $7,225 insurance premium to the federal government, and $1,600 in charges to verify the title of the house he had owned for decades. As part of the deal, Collins was convinced to invest the loan proceeds, which he had borrowed at 5.74%, in an annuity contract that was guaranteed to pay 3%. Collins embarked on this costly series of transactions after receiving counseling that, according to his loan documents, lasted only 47 minutes and was done over the telephone. Five months after taking out the loan, Collins was declared incompetent by local adult protective authorities.[55]

Lopez said in June 2009 that he had not heard about the Collins family lawsuit, and that he stood by his Senate testimony, although he had later heard of some instances where reverse mortgage loans were used to buy annuities. "That sort of stuff makes us really angry," he said. "One thing we don't want to see is loan officers working in cahoots with financial planners."[56]

Claims by lenders that they will protect the interest of consumers in the lending process should be approached with caution. Without effective regulation, abuses are likely to occur in the lending process.

The Brokers

Historically, mortgage brokers served as intermediaries who brought mortgage borrowers and lenders together. Over time, brokers' roles have become more complicated. Today their compensation and financial incentives are often hidden behind a smokescreen of confusing and obtuse disclosures.

During the subprime mortgage boom, a small army of mortgage brokers pushed inappropriate mortgage loans on borrowers without regard for whether borrowers needed the loans or could afford the payments. The subprime bust has sent many of these mortgage brokers flocking to the reverse mortgage business where many seniors depend upon them for guidance through a market that offers a welter of "educational" resources and presents complex product and financial choices.

Seniors often assume that brokers have a duty to look out for the borrower's best interest. But that is not true. Because mortgage loans are considered business transactions where each party ostensibly protects its own economic interest, in many states brokers and lenders owe no fiduciary duty to borrowers. Brokers and lenders typically disavow the existence of any relationship of trust and confidence between them and borrowers.

However, their marketing material is designed to build trust and often uses impressive-sounding credentials to imply special knowledge and expertise.

For example, American Reverse Mortgage Corp. proclaims on its website that it has "thirty-one (31) Certified Senior Advisors (CSA) on our staff."[57] As of December 2007, Wells Fargo claimed to have 750 "certified reverse mortgage consultants" to assist borrowers with reverse mortgage products.[58] These designations reflect expertise with respect to senior financial matters and reverse mortgages.[59] They inspire trust and confidence from seniors who may later be surprised to find out that the certified advisor or consultant, in fact, was not obligated to look out for their best interest.

While brokers' marketing materials are geared toward building trust and inspiring confidence, the agenda for a recent gathering of reverse mortgage lenders warned that "it will not be long before fraudsters develop schemes to exploit seniors and lenders" in the reverse mortgage market.[60] But there have always been thieves willing to take advantage of vulnerable seniors. For example, in November 2003, Detroit broker Anthony James showed up on the doorstep of Shirley Schultz after she called Financial Freedom Senior Funding Corp., seeking information about a reverse mortgage. In January 2004, Schultz, who was over 80 years old, took out a reverse mortgage against her Belleville, Mich., home and received a check for $61,325. Unknown to Schultz, James had directed the closing agent to issue a second check payable to Schultz in the amount of $42,667. James took the second check, forged the endorsement on it, and deposited it into his bank account.[62]

Outright criminal conduct represents the extreme example of bad broker behavior. More often, however, brokers take advantage of seniors in less obvious ways, such as by selling them reverse mortgages that they do not need or getting them into more costly loans that increase the brokers' own compensation.

As in the subprime mortgage market, brokers in the reverse mortgage market have a financial incentive to originate as many loans as possible. Brokers do not get paid if they do not close deals. The same origination fees that drive lenders to sacrifice responsible lending to profits also influence brokers. In addition, brokers earn more money, often through yield spread premiums, when they sell reverse mortgages that will garner more profits for lenders and investors. In unguarded moments, even brokers themselves sometimes acknowledge that their financial incentives can work against the interests of the seniors that they are "guiding." "Needless to say, there are some products that will pay you more, and pay your customers less, while increasing overall costs."[63] When brokers sell seniors more costly and less favorable reverse mortgages in order to increase their own compensation, the value of the senior's lost equity can end up in the pockets of brokers and lenders.

A SENIOR'S "NEW BEST FRIEND"

At a hearing before the Senate Special Committee of Aging, Carol Anthony summed up the promises made to persuade her 80-year-old mother to take out a reverse mortgage:

"There would be no risk of losing her home. But there was. She would receive independent counseling. But she didn't. All loan options available to her would be reviewed. They weren't. She would never be rushed into signing anything she did not fully understand or was not ready to sign. But she was. She would not be incurring a mortgage. But she did. All loan terms would be carefully explained. But they weren't. When mom signed on the dotted line, she felt the salesman was her new best friend. But he wasn't."[61]

Wall Street and the Securitization Spigot

Rocket fuel for the recent mortgage lending boom came from the deals in which Wall Street investment banks assembled thousands of home mortgage loans into portfolios, and sold investors securities backed by promised returns from those portfolios. The investment banks raked in billions of dollars of fees assembling and administering these portfolios. Wall Street's insatiable appetite for more loans to securitize prompted lenders to offer incentives to brokers and other intermediaries to make more loans and load them up with terms that made those loans more profitable to investors and more costly to borrowers.

Reverse mortgage lenders are also looking to securitization to supply a steady stream of capital to meet the growing demand for reverse mortgage products. The idea is one that has been nurtured by policy makers and academics. In 1998, economist Dr. Nandinee K. Kutty wrote that "[a] healthy secondary market for reverse mortgages would greatly reduce risk premiums and result in higher payments to borrowers, which in turn, would increase market acceptance."[64] The following year Lehman Brothers underwrote the first securitization of reverse mortgages in a $317 million deal that used proprietary reverse mortgages originated by Financial Freedom as assets. More recently, HUD policy analysts noted that, "the long-term success of HECM as a more mainstream loan product may require the eventual development of a more efficient secondary market for these loans."[65] Not surprisingly, the securitization of HECM loans is becoming more common.

Historically, most HECM mortgages were purchased by Fannie Mae, the giant government sponsored mortgage finance company, which kept those reverse mortgages in its own investment portfolio.[66] The first securitization of HECM loans came in August 2006.[67] From that point through the end of 2007, private financial institutions issued about $2.2 billion in securities backed by HECMs.[68]

In 2006, the Government National Mortgage Association, also known as Ginnie Mae, announced plans to create a securitization program for HECM loans. In November 2007, Ginnie Mae guaranteed its first issuance of securities collateralized by HECMs. Since then Ginnie Mae has securitized more than $1.7 billion in HECM loans.[69]

The growth of reverse mortgage securitization is potentially a boon for an increasing number of seniors who may need to cash out some of their housing wealth to supplement Social Security, to meet unexpected medical costs, or to make needed home repairs. But it is also, conceivably, a curse. Seniors, especially those with low incomes, are hard-pressed to find knowledgeable and trustworthy advisors. On the other hand, they can ex-

UNNEEDED REVERSE MORTGAGES

Miguel and Laura Posada were both over 80 when, in 2005, they were convinced to take out a $100,000 reverse mortgage secured by the home that they had bought with cash two years earlier, according to a lawsuit they filed. As retirees who had each worked in blue-collar jobs for over 40 years, the Posadas both had pensions and were living comfortably. They had no need to cash out their equity. But Miguel Posada saw an advertisement for a reverse mortgage and sent away a post card seeking more information. He forgot about it until a month later when a man showed up at his door holding the post card. After the salesman "sat down and explained everything," the Posadas decided to take it. Now they're sorry they did.

The Posadas believe they wasted thousands of dollars on fees taking out a loan they did not need. The salesman also persuaded the couple to pay $20,500 to a local attorney that they never met to purportedly "pre-qualify" them for Medi-Cal, California's medical insurance program for low-income people. The salesman also sold them a 15-year deferred annuity paying interest at 3.5%. The interest rate on the reverse mortgage started at 6%. So the couple borrowed money at 6% and invested it (in the deferred annuity) to earn interest at 3.5%. They paid over $20,000 to be pre-qualified for an insurance program that has no prequalifications. When the Posadas realized they had a bad deal, the lawyer refused to return their money. The Posadas have a lawsuit pending against the salesman and the lawyer.[70]

pect to receive lots of encouragement to take out reverse mortgage loans. Unfortunately, much of that encouragement comes from a cast of characters eerily familiar from the subprime mortgage boom and bust: aggressive brokers eager to rake in large fees and giant financial institutions hungry for profits that come from maximizing loan volume. In an effort to generate a steady stream of borrowers, seniors are likely to be pushed into reverse mortgages that they do not need. Without adequate borrower protections, the securitization of reverse mortgages and the push for greater loan volume could lead to abusive lending that will sap the equity of senior homeowners.

VI. The Marketing Machine

The growth of the reverse mortgage industry has been spurred by broad marketing efforts aimed at generating a steady supply of prospective borrowers, thus boosting loan volume and profits. It is well known that "push" marketing was a staple of the subprime market.[71] Using high-pressure sales tactics, lenders and brokers pushed more home-secured debt on homeowners than they needed or desired. Today reverse mortgage lenders and brokers continue that push marketing tradition.

Pushing Reverse Mortgages

Advertising for reverse mortgages can be found on TV and on the Internet. Seniors looking in their mailboxes or picking up their phones may be plied with the virtues of a reverse mortgage. Also common are old-fashioned marketing techniques such as advertisements in senior newsletters and "educational" programs at senior centers.

Sellers have enlisted celebrities as spokesmen to reassure seniors about these complicated and unfamiliar loans and to emphasize the pleasures that can be had with cashed out equity. Marketing strategies promote reverse mortgages, not as a lifeline for retirees with low incomes, but as a tool to increase consumption on items that are not necessities.[72] A list of 25 ways to use loan proceeds recently posted on a reverse mortgage promotion web site includes "Take a dream vacation," "Go on a cruise," or "Travel around the world."[73] Also on the list at number 19 is:

> ***Lifestyle enhancement****—If you always dreamed of living a rich and famous life, but your finances did not give room to it, you can use the money from a reverse mortgage to enhance your living style. You will have more money which you can spend on luxury items to decorate your home and for personal luxury items like Rolex watches, etc.*[74]

According to the National Reverse Mortgage Lenders Association, "the only limit on how you use a reverse mortgage is your imagination."[75] One borrower profiled on the NRMLA website took out a reverse mortgage against his Florida home and used the proceeds to build a single-engine, two-seat airplane.[76]

The reality is that reverse mortgages are probably not the most cost effective way for well-off seniors to purchase airplanes or other big-ticket items. But at least seniors able to make such expensive purchases can probably absorb the expense of sub-optimal financing without jeopardizing their access to basic necessities such as shelter, food, and medicine. The same is not true of low-income seniors. Urging these seniors to cash out home equity to go on a "Shopping Spree" or purchase a "Dream Car" exposes them to the danger of having nowhere to turn to raise money for future financial emergencies.

While reverse mortgages are often pitched as "free money" to use as the borrower pleases, sellers also have sought to exploit seniors' unfamiliarity with reverse mortgages by implying that the money comes from the federal government. Recently, Massachusetts authorities stepped in to prohibit American Advisors Group of Irvine, CA from mailing reverse mortgage solicitations under the heading "notice of 2008 government benefits."[77] Undeterred by the Consent Order entered into with the Massachusetts Division of Banks in 2008, American Advisors Group sent

Exhibit 1

2009 ECONOMIC STIMULUS PLAN – HECM PROGRAM

Property ID#: 903837374

ADMINISTRATIVE OFFICES
AMERICAN ADVISORS GROUP
16808 Armstrong Ave Ste 220
Irvine, CA 92606

[redacted]

MA11-05007

IMPORTANT INFORMATION PLEASE READ

YOUR ESTIMATED QUALIFICATION BASED ON FHA LENDING LIMITS	
Age(1): (Approximate)	80
Monthly Disbursement(1): (Available For Life)	$2,158
Lump Sum(1):	$301,283
Credit Line(1):	$301,283

County: MIDDLESEX 2009 Increased Lending Limit: $417,000

Current Property: [redacted]

Property ID#: [redacted]

[redacted]

President Obama has signed the $787 billion American Recovery and Reinvestment Act which raises the national loan limit for HECMs. This higher limit is only available for the remainder of 2009.

As part of United States Federal Law [12 U.S.C. 1715z-20], the Federally-Insured HECM Program was created to meet the special needs of senior homeowners by reducing the effects of economic hardship caused by the increasing costs of meeting health, housing, and subsistence needs at a time of reduced income and assets.

This Federally Insured Program, which is backed by HUD (1) eliminates your current mortgage payment (if any); (2) requires you to make NO MONTHLY PAYMENTS of any kind on proceeds distributed to you during your lifetime and (3) enables you to stay in your home for the rest of your life(2). Additionally, an important feature of the HECM is that you, and not the lender, continue to own your home.

Based on current FHA lending limits, a borrower your approximate age could receive a lifetime monthly check of $2,158 or a lump sum of $301,283 or have $301,283 available.

There are no income or minimum credit requirements to qualify. In order to learn more about this federally insured program please call now toll free 1-800-466-0572 to speak with a consultant and verify that your home meets minimum standards.

FOR MORE INFORMATION OR TO SCHEDULE AN ASSESMENT (FREE OF CHARGE)
CONTACT THIS FHA APPROVED LOAN CORRESPONDENT BY 4/24/2009
American Advisors Group, Inc.
CALL 1-800-466-0572
Additional information is being offered to you, without risk or obligation
by the HUD Authorized Loan Correspondent above when requested before 4/24/2009

* See reverse for specific disclosures and license information.

American Advisors Group Solicitation

(1) Estimates are based on monthly-adjusting interest rates in the HECM program, maximum origination and servicing fees, and an approximate national average closing cost total. Actual loan amounts available depend on the rates in effect when a loan is closed and the actual origination fee and closing costs charged. Actual loan amounts available also depend on your age, the appraised value of your home, and current program limits. Current estimated property value was determined using Automated Valuation Models (AVMs) which evaluate multiple aspects and assign unique nonlinear appreciation factors to each aspect of property. An FHA approved appraisal will need to be ordered and completed to determine current fair market value.

(2) Subject to complying with the terms of your loan.

(3) Your unused net principal limit grows at a rate equal to the note rate of interest.

(4) Consult your tax advisor.

American Advisors Group (AAG) is headquartered at 16811 Hale Ave., Suite A, Irvine, CA 92606. 1-866- 948-0003. AAG conducts business in the following states: AL, AZ (MB-0908260), CA (Loans will be arranged pursuant to Department of Corporations California Finance Lenders License 603 F324). CO (MB 100018671; to check the license status of your mortgage broker, visit http://www.dora.state.co.us/realestate/index.htm). DE, FL, GA (Residential Mortgage Licensee #22849), IL (Illinois Residential Mortgage Licensee), IN (Loan Broker), LA, MD,MA (Mortgage Broker #89877), NM, NY (Registered Mortgage Broker - NYS Banking Department), OR, TN, VA (licensed by the Virginia State Corporation Commission MB-4155), WA (#510-MB-47260).
We arrange but do not make loans.

Our company, American Advisors Group, is a private company. It is not a government agency and is not affiliated with any government agency.

the solicitation on page 12 to consumers in 2009 which again referenced government benefits.[78]

Aggressive marketing by subprime lenders landed many borrowers in inappropriate loans that they could not afford. Those marketing efforts have moved to the reverse mortgage market where many seniors may be drawn into reverse mortgages that they do not need.

VII. More Payouts

Yield Spread Premiums

The subprime mortgage crisis remains a stark reminder of the damage that can be done when the promise of easy money harnesses brokers to the interest of distant Wall Street. In the subprime boom, that promise often took the form of something unhelpfully labeled a "yield spread premium." The premiums were paid to brokers as an incentive to increase the interest rates or add prepayment penalties to mortgage loans thereby making those loans more profitable for lenders and investors.

Although rarely discussed with borrowers, payments of yield spread premiums were common in the subprime mortgage market. While federal law required an obscure disclosure of these premiums on the HUD-1 settlement statement, few borrowers understood that these payments rewarded brokers for originating loans that generated maximum yields to lenders and investors.[79] Nor did borrowers realize that those higher yields resulted from higher fees and interest rates that they themselves would have to pay.

In an effort to curb profiteering in the reverse mortgage market, HUD has established caps on origination fees.[80] Brokers are not permitted to

Pricing Memo

Effective immediately we will be accepting the CMT 225. We feel this is a necessary step for brokers to make some additional income during this current down cycle in pricing. Please be aware we have also made some changes to our CMT 150 pricing.

Sincerely,

Betsy Clinard
Operations Manager
Wholesale Division

REVERSE IT.
REVERSE MORTGAGE EXPERTS

Pricing Memo

Pricing Memo

Effective on loans closed AFTER August 20, 2008

CMT Pricing	$25	$30	$35
150	-.75	-.60	-.45
175	.20	.35	.50
200	.80	.95	1.10
225	1.45	1.60	1.75

Libor Pricing	$25	$30	$35
125	-.30	-.15	Par
130	-.15	Par	.15
150	.30	.45	.60
175	.90	1.05	1.20

collect any additional origination fees of any kind from borrowers. However, the regulations do not prohibit lenders from paying additional fees—yield spread premiums to brokers.

The industry has taken advantage of this loophole to increase its profits. For example, reverse mortgage wholesaler Urban Financial Group, which operates under the ReverseIt.org brand, recently sent out a "pricing memo" that describes the rebates paid to brokers based on the margin and monthly service fees of a loan. Not surprisingly, the higher the margin and higher the monthly service fee, the higher the rebate paid from the lender to the broker.[81]

Urban Financial Group is not alone in its use of yield spread premiums. W.L. Pulsipher, President of American Reverse Mortgage, said with respect to reverse mortgage wholesalers, "everybody is offering that."[82]

Yield Spread Premiums in the reverse mortgage market pose a serious threat to consumers. Deft brokers can use "pricing memos," and similar incentives as a guide for juggling multiple variables in a reverse mortgage transaction to take bigger and bigger bites out of consumers' equity. Senior borrowers are unlikely to understand the dizzying cost menu that brokers and loan originators use to generate the greatest benefits to themselves and potential investors.

The Annuity Trap

One of the greatest abuses of reverse mortgages comes when loans are used to cash out seniors' home equity and that cash is used to buy expensive and complicated insurance policies, annuities, or other financial products. Many of these products provide insurance agents with hefty commissions, sometimes as high as 12 percent.[83] While the terms, financial restrictions, timing, and special features of contracts vary widely, they usually involve payments to an insurance company that then promises to make future payments to the borrower.

A link to an annuity sale signals danger in any reverse mortgage transaction. The combined front-end expenses of the reverse mortgage loan and the annuity contract create a hybrid deal that would have to yield astronomical returns to benefit the borrower. In addition, the complexity of both products makes seniors especially vulnerable to the misrepresentations of unscrupulous brokers and lenders.

The chance to sell annuity contracts is a potent attraction to intermediaries in a position to urge seniors into reverse mortgages. The Housing and Economic Recovery Act of 2008 included a prohibition on lenders' ties to sellers of other financial products.[85] HUD has yet to issue a final rule with respect to the cross-selling ban. However, cross-selling restrictions are likely to prove ineffectual when weighed against the hefty commissions that await those who circumvent such prohibitions and find ways to use reverse mortgages to tap home equity to fund annuity sales. As one insurance agent put it, "All that's going to do is ferret out the stupid players."[86] Lax enforcement by HUD and state insurance regulators[87] combined with the absence of a private right of action for injured borrowers reduce the chances of getting caught and limit the effectiveness of the ban.

> In 2006, reverse mortgage sellers got their hooks into 80-year-old Betty Adcock. According to a lawsuit filed by her daughter, Adcock had enough money to pay her bills, owned various investments, and had an existing home equity line of credit that she had tapped for $19,000. Despite her financial stability, she was persuaded to take out a reverse mortgage and to purchase a 20-year, $125,000 deferred annuity contract. The annuity contract prohibited Mrs. Adcock from withdrawing the money without penalty for 10 years. And, while the annuity had a guaranteed rate of 4.15% for the first ten years, the starting adjustable rate on her reverse mortgage was 6%. In essence, Mrs. Adcock was convinced to borrow money at a 6% interest rate and invest the money in an annuity that paid just over 4%. She paid $16,800 in closing costs for a loan that had a higher principal balance than her existing home equity line of credit, that had a higher interest rate than her existing HELOC, and that limited access to her money for ten years.[84]

VIII. Proprietary Equity Conversion Products

Proprietary equity conversion products have been around for decades. They come in a myriad of forms including proprietary reverse mortgages and shared appreciation mortgages. The reach of these products has been greatest in geographic areas with high property values or rapid property appreciation.

As in the past, proprietary equity conversion products continue to be largely unregulated at the federal level. Among states, nearly half have laws related to reverse mortgages though these state statutes vary dramatically. Some states merely define reverse mortgages, while others provide more substantive protections. For example, many states with reverse mortgage laws mandate certain disclosures and ban prepayment penalties. Some impose a waiting period, require mandatory counseling, or limit the fees that may be charged to the borrowers.

Proprietary Reverse Mortgages

Proprietary reverse mortgages are developed and backed solely by private financial institutions. Prior to the recent credit crunch many of these loans—also known as jumbo reverse mortgages—were made to property owners whose property values exceeded the HECM loan limits.

Financial Freedom Senior Funding Corp. with its Cash Account Plan dominated the proprietary reverse mortgage market for many years. Introduced in July 2006, Financial Freedom's Cash Account Advantage Plan was targeted at consumers whose home value exceeded HECM's limits or whose type of property was excluded from the HECM program.[88] Some of the key features of the plan were: its higher loan limits as compared to other reverse mortgages; lump sum, line of credit, or combination payment options; adjustable rate; and origination fee of 2% of the maximum amount that was available to the borrower on the loan or $2,500, whichever was greater.[89]

Growth in Financial Freedom's proprietary product was driven in part by securitization of these loans by Lehman Brothers. The mortgage crisis precipitated the collapse of Financial Freedom's parent company, IndyMac Corp. (now OneWest Bank), which was taken over by the Federal Deposit Insurance Corp. in July 2008. Subsequently, the failure of Lehman Brothers brought the securitization of proprietary mortgages to an abrupt halt. As a result, few proprietary reverse mortgages are being offered today.

One product that remains available is Bank of America's Senior Equity Reverse Mortgage. That product is aimed at borrowers with houses valued over the FHA limit (now $625,500) and up to $10 million, according to Bank of America's web site.[90]

Despite the low numbers of proprietary reverse mortgages being made today, there is good reason to anticipate growth in the future. The growing senior population and its need for income will likely reinvigorate these loan products in the not too distant future.[91] While most of these products do not vary significantly from HECMs, borrowers have none of the basic consumer protections that are guaranteed to HECM borrowers. Moving forward efforts should be made to provide at least the same level of protection to all reverse mortgage borrowers.

Equity Sharing Deals

Like reverse mortgages, the equity conversion products known as "shared equity agreements" have been around for a while. Such deals entitle lenders to a certain share of any appreciation in a home's value between the time a loan is made and the time it reaches maturity. While the financial crisis has left sales of these products in the doldrums, lenders say they plan to revive them when conditions in the capital and real estate markets permit.

REX & Co., a San Francisco-based lender backed by controversial insurance giant American International Group (AIG), at one point offered owners in at least 14 states cash in exchange for stakes in rising house prices but announced in October 2008 that it would stop making new deals.[92] "We're hoping that that's not a permanent situation," a company spokesman said.[93]

Another outfit called EquityKey offered similar deals to senior homeowners in at least 10 states, and reported that it had received more than 500 applications through May 2008.[94] However, by January 2009 founder Jeffrey Nash said that the company had implemented a "temporary funding freeze" but was still continuing to accept applications. "We anticipate starting funding again soon."[95]

Equity sharing deals lack even the minimal consumer protection provided by a counseling requirement. Past abuses of equity sharing deals signal that a new generation of these arrangements could chew up seniors' equity with costs they do not expect or understand. They involve financial calculations that are even more complex and uncertain than the cost-benefit estimates for reverse mortgages.

VARIATIONS ON A THEME

Laverne Kidwiler was 71 years old and newly widowed in 1993 when she decided to give herself some financial breathing room by using her house to secure a loan from something called the Providential Home Income Plan. According to her son, Kidwiler received a monthly payment of $525 and paid an interest rate of 11. 5% on the money she received from the plan, which by 2008 was nearly $120,000. But that year, when Kidwiler, with the aid of her son, sought to refinance, the loan servicer sent her a payoff demand for $600,000.

How did this happen? According to Kidwiler's son, when she did the deal, she hadn't noticed that it came with an annual percentage rate of 14.92%.[97] The actual rate of interest was so much higher than the nominal rate because Kidwiler was obligated to pay interest not only on the money she received but also on the increased value of her house.[98]

IX. Disclosure and Counseling: The Bulwark Against Abuse?

Existing federal laws and rules rely on loan cost disclosures and homeowner counseling as the primary bulwark against reverse mortgage abuses. Unfortunately, the subprime crisis showed that reliance on disclosure and informed consumer decision-making is fundamentally flawed as a strategy for consumer protection.

Stacks of papers that must be signed or initialed to certify that information has been "disclosed" are too often overlooked or misunderstood by consumers. A receipt of counseling certificate signed by a counselor does not even guarantee that all the required disclosures have been made or that all the counseling topics have been covered.

Two main provisions of existing laws aim to protect consumers. Under the Truth in Lending Act lenders must disclose to borrowers the Total Annual Loan Cost (TALC) for reverse mortgages. All HECM borrowers must obtain "adequate counseling" before entering into a reverse mortgage transaction.

Total Annual Loan Cost

The Total Annual Loan Cost (TALC) is the projected annual average cost of a reverse mortgage including all itemized costs. TALC was developed to facilitate comparison of the costs of various loan products to provide consumers with an "apples to apples" way of evaluating and comparing the cost of reverse mortgage alternatives.

The total annual loan cost rates are expressed as a matrix based on various projected appreciation rates and loan terms. TALC costs must be projected based on at least three loan terms: a two year term, a period equal to the youngest consumer's life expectancy, and a period equal to 1.4 times the youngest consumer's life expectancy.[99] In addition to the loan term, TALC rates must also be based on assumed annual property appreciation rates of 0 percent, 4 percent, and 8 percent.

In general, the TALC depends on how long the elder lives in their home, what happens to the home's value during that time, and the type of loan advances. The cost is greatest when the loan is repaid within a few years after closing. The cost is lowest if the elder lives beyond his or her projected life span.

While TALC disclosures must be provided to all reverse mortgage borrowers, including those with non-HECM loans, some key assumptions may limit the value of a TALC disclosure for consumers. For example, in fiscal year 2008 approximately 89% of HECM borrowers used the line of credit option.[100] But, if the consumer has a credit line, the disclosures will be based on an assumption that 50 percent of the principal loan amount is advanced and that no further advances are made during the remaining term of the loan. While this assumption provides a convenient way to compare different credit lines, it masks the true cost of the loan that depends in large part on the size and timing of the cash advances requested by the borrower. And absent an estimate of the true cost of a loan, the TALC remains a highly flawed instrument for consumer protection.

HECM Counseling Requirement

To be eligible for an HECM loan, the borrower must obtain "adequate counseling" by an independent third party that is neither directly or indirectly associated with the mortgage transaction.[101] Lenders are required to provide every potential HECM borrower with a list of at least ten HUD-approved counseling agencies.[102] Five of these counseling agencies must be in the borrower's local area or state and at least one agency must be located within a reasonable driving distance. The other five referrals must be to national intermediaries and multi-state organizations which are specified by HUD.

In order to ensure the independence of the counselor, borrowers must initiate communication with a counseling agency on their own. In a 2009 Mortgagee Letter,[103] HUD indicated that lenders who dial a counseling agency's phone number and hand the phone to the borrower to schedule counseling violate the directive requiring borrowers to initiate contact. Similarly, lenders are not permitted to enter information into a web-based system that then automatically puts the borrower's name in a queue to be called by a counselor.

The HECM enabling statute details information that must be discussed with the borrower during the counseling session.[104] Specifically, counselors are required to:

- Review options other than an HECM that are available to the homeowner, including other housing, social service, health, and financial options;
- Discuss other home equity conversion options that are or may become available to the homeowner, such as sale-leaseback financing, deferred payment loans, and property tax deferral;
- Disclose that an HECM may have tax consequences, affect eligibility for assistance under federal and state programs, and have an impact on the estate and heirs of the homeowner; and
- Review the financial implications of entering into an HECM loan.

In order to evaluate possible alternatives to a HECM loan, counselors must perform a budget analysis based on the borrower's income, assets, debts, and monthly expenses.[105]

Counseling agencies may charge up to $125 for the counseling session.[106] The fee may be paid directly to the agency, or it may be paid from the borrower's HECM proceeds at closing. Lenders are not permitted to pay HUD-approved counseling agencies directly or indirectly for counseling services.[107]

Responsible government officials have pointed to counseling as the best possible protection for borrowers. "HUD believes that our frontline protection against predatory lending is an informed customer," said John Weicher, a HUD Assistant Secretary. "Housing counseling has proven to be an extremely important activity to educate consumers about how to avoid abusive lending practices."[108]

However, as a recent GAO report on reverse mortgages demonstrates, counseling provides, at best, limited protection for senior homeowners. Importantly, the GAO found that during limited testing of HECM counseling sessions, counselors did not cover all the information required by HUD, including alternatives to HECMs and the financial implications of reverse mortgages.[109] Additionally, the GAO discovered that 40% of the counselors overstated the length of the counseling sessions on the counseling certificate. For counselors that accurately recorded their time, counseling sessions typically lasted 30 minutes to just over an hour. By contrast, an AARP funded survey in 2006 found that counseling sessions by exam-tested counselors who followed detailed counseling protocols took on average two to three hours.[110]

Lenders, a major source of funding for HECM counseling in recent years, have complained that the counseling requirement is a bottleneck that reduces loan volume. In 2005, Peter Bell, president of NRMLA, told Home Equity Wire that volume had been pinched because borrowers waited four to six weeks for mandatory counseling: "Put simply, there aren't enough counselors to handle the high volume of requests."[111]

Undoubtedly, the effectiveness of counseling has been undermined by inadequate funding and the limited availability of trained counselors. While the volume of HECM loans tripled from 2004 to 2007, in the latter year HUD directed only $3 million in funding for reverse mortgage counseling.[112] In June 2009, HUD announced that it had allocated $8 million for reverse mortgage counseling as part of an overall counseling budget that was up 23 percent over the previous year.[113] While helpful, the money for reverse mortgage guidance still amounted to less than $80 per reverse mortgage, too little to pay for several hours of in-person advice from a skilled financial professional.

Even with sufficient funding and well-trained counselors, the existing counseling program would be hard-pressed to provide adequate guidance to seniors. With the focus on reverse mortgage mechanics and comparisons, counseling sessions, as presently designed, fail to address the broad financial, legal, and estate-planning consequences of most decisions regarding whether to take out a reverse mortgage.

Counseling may improve disclosure, but it cannot be relied upon to effectively prepare a consumer to understand and navigate the complexities of a reverse mortgage deal or place it sensibly in the context of his or her own financial needs. While the counseling attempts to empower seniors to avoid abuses, it is no match for the powerful market forces at play in the reverse mortgage industry.

X. Recommendations: Making the Reverse Mortgage Market Safe

Steps must be taken now to protect the interests of low-income seniors and prevent the reverse mortgage boom from becoming a reprise of the subprime fiasco. To that end, this report recommends the following changes:

Create a suitability standard for all reverse mortgages and equity conversion products. Only a fundamental shift in responsibility can level the reverse mortgage playing field for financially strapped seniors who need to tap their home equity. Seniors, who most likely will only take out one reverse mortgage in their lifetimes, frequently rely on brokers and lenders for guidance in navigating the complex choices associated with reverse mortgages. Brokers and lenders routinely use impressive sounding credentials to imply special knowledge and expertise. In fact, the training of reverse mortgage sellers emphasizes the importance of building trust with potential customers. But because mortgage loans are considered business transactions where each party ostensibly protects his or her own economic interests, in many states brokers and lenders owe no fiduciary duty to borrowers, and when problems arise brokers and lenders disavow any relationship of trust and confidence with borrowers.

Some of the same market forces that rewarded volume business with huge profits in the subprime market are growing in the reverse market. The subprime mortgage crisis was driven by profiteering among all players in the industry, who operated without regard to their impact on the lives of millions of Americans saddled with inappropriate mortgages. A standard of conduct that would require brokers and lenders to have reasonable grounds for believing that a reverse mortgage is suitable for the borrower is necessary to counteract market forces that favor profitability over responsible lending.

No doubt the mortgage industry will react negatively to any suggested suitability standard. Policy makers, however, should be wary of industry claims that the "sky will fall" if such a standard is imposed. Industry arguments that undefined risks created by a suitability standard would lead to higher credit costs and a narrowing of credit options, even if true, must be weighed against the consequences of doing nothing. For example, in August 2006, advocates from the National Consumer Law Center recommended the imposition of a duty of good faith and fair dealing to address irresponsible underwriting, unsuitable loans, and steering in the nonprime market. The Mortgage Bankers Association responded with a policy paper urging Congress to resist pressure to impose a suitability standard and instead allow the market to offer borrowers "unparalleled choices and competition resulting in lower prices and greater opportunities than ever before to build wealth and wellbeing that homeownership brings." In the wake of heavy industry lobbying, neither Congress nor federal regulators chose to adopt a suitability standard for nonprime mortgages. Partly as a result, the nation is suffering the consequences of widespread improvident lending in the subprime market.

Yield spread premiums must be banned in reverse mortgage transactions. Yield spread premiums—or payments from lenders to brokers in exchange for the broker selling the borrower a loan with a higher interest rate than the borrower could have received—were one of the key drivers of the subprime foreclosure crisis. They encouraged brokers to steer borrowers into risky, expensive loans. In the reverse mortgage context, yield spread premiums incent brokers to make loans more profitable for lenders and investors at the expense of borrowers. Within the HECM program, yield spread premiums provide a gaping loophole in the regulations designed to cap origination fees and limit the costs of reverse mortgages.

HUD has clear authority to ban yield spread premiums in all reverse mortgage transactions, but has refused to do so. To date, HUD has allowed YSPs on the theory that consumers can use them to buy down upfront origination costs. The reality, however, is that this trade-off rarely, if ever occurs. HUD's recent attempt to address YSPs through disclosure ultimately will hurt more than help senior homeowners. The new cost disclosure required by HUD refers to the YSP as a credit, which leads consumers to think they are getting a better deal with a YSP when in fact they are getting a worse deal.

The only way to adequately address abusive YSPs is through substantive change. With seniors relying on brokers to guide them through the reverse mortgage process, incentives for brokers to increase the cost of the loan for the senior homeowner should be prohibited.[114]

Private equity conversion products such as proprietary reverse mortgages and shared equity agreements must be regulated. The use of these products, which are developed and sold by private financial institutions, has slowed to a trickle in these tough economic times. However, economic recovery over the next few years is likely to reinvigorate this market. To date, these products remain almost entirely unregulated at the federal level and subject to widely varying state regulation. HECM requirements including mandatory counseling and the prohibition on cross-selling should be extended to these private products.

Implement data collection on reverse mortgages and other equity conversion products. Other than data on the insurance policies issued by the Federal Housing Administration under the HECM program, there is a dearth of publicly available information on reverse mortgage originations and reverse mortgage borrowers. The primary means of collecting data on mortgages, the Home Mortgage Disclosure Act, generally does not require reporting of information on reverse mortgages. In addition, when information on reverse mortgages is reported under HMDA, the tally is merged with that of traditional forward mortgages, making it impossible to extract and analyze reverse mortgage data separately.

CONCLUSION

Senior advocates and policy makers supported the creation of reverse mortgages as a means to help seniors in need tap home equity that might otherwise remain out of reach. The federally insured Home Equity Conversion Mortgage has been a lifeline to many senior homeowners since its creation two decades ago. But today, the consumer protections built into the program are being eclipsed by the drive to exploit senior home equity by major banks, insurance companies, mortgage brokers, and Wall Street investors. Sophisticated sales campaigns designed to maximize loan volume target senior homeowners. This push—on the Internet, on TV, by direct mail, in senior centers, and over kitchen tables—threatens the financial well-being of America's seniors.

The greatest threat looms over millions of low-income seniors with significant amounts of home equity. While some of these homeowners genuinely need access to their built-up equity, that need can make them especially vulnerable to bad advice from brokers and loan officers out to put the most money in their own pockets, and in the coffers of lenders and investors. Low-income seniors are also vulnerable to predators selling overpriced and inappropriate financial products and services.

Federal and state governments must act now to ensure that reasonably priced and fairly structured reverse mortgages are available for those who truly need them, and that vulnerable seniors are protected from predatory or abusive lending practices.

Notes

[1] John C. Dugan, Comptroller of the Currency, Remarks before the American Bankers Association, Regulatory Compliance Conference: Consumer Protections for Reverse Mortgages (June 8, 2009) at 2, *available at* http://www.occ.treas.gov/ftp/release/2009-61a.pdf.
[2] *See* Dep't of Hous. and Urban Dev., HECM Cases Endorsed for Insurance by Fiscal Year (2009), *available at* www.hud.gov/offices/hsg/comp/rpts/hecm/hecm0509.xls.
[3] *See id.*
[4] 12 U.S.C. § 1715z-20(a) (2009).
[5] *See* 12 U.S.C. §§ 1701 to 1701z-15 (2009).
[6] 12 U.S.C. § 1715z-20(i)(C) (2009).
[7] 12 U.S.C. § 1715z-20(i)(A) (2009).
[8] 12 U.S.C. § 1715z-20(d)(9) (2009); 24 C.F.R. § 206.17 (2009).
[9] Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, § 2122 (July 30, 2008), *amending* 12 U.S.C. § 1715z-20(g). HECM maximum loan limits are tied to the loan limitations established under the Federal Home Loan Mortgage Corporation Act. *See* 12 U.S.C. 1454(a)(2) (2009).
[10] American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, § 1204 (Feb. 17, 2009).
[11] 12 U.S.C § 1715z-20(d)(5); 24 C.F.R. §§ 206.17, 206.21 (2009).
[12] 12 U.S.C. § 1715z-20(d)(7) (2009). This non-recourse feature, however, assumes that the heirs of the reverse mortgage borrower do not want to keep the home. If the borrower or the borrower's family want to retain the home after the reverse mortgage matures and the loan balance is greater than the value of the home, they may still be required to pay the full amount of the debt even though it exceeds the home value.
[13] 12 U.S.C. § 1715z-20(d)(3) (2009); 24 C.F.R. § 206.209 (2009).
[14] 24 C.F.R. § 206.27(b)(5), (6) (2009). The lender may elect to pay property taxes or hazard insurance premiums by withholding funds from monthly payments or charging funds to a line of credit. 24 C.F.R. § 206.205(2009).
[15] 12 U.S.C. § 1715z-20(r) (2009).
[16] 12 U.S.C. § 1715z-20(r)(6) (2009). The $6,000 limit is adjusted in accordance with the Consumer Price Index in $500 increments.
[17] 12 U.S.C. § 1715z-20(d)(2)(B) (2009). Counseling may not be provided by any party that is directly or indirectly associated with 1) originating or servicing the mortgage, 2) funding the loan, or 3) the sale of annuities, investments, long-term care insurance, or any other type of financial or insurance product. *Id.*
[18] Jan Shaw, *Provident Credit Union Introduces Reverse Mortgage*, San Francisco Business Times, Nov. 30, 1990, at 11.
[19] *First For-Profit Reverse Mortgage Company in US Starts Business with Lines of Credit From Six NJ, Pennsylvania Banks and Thrifts*, American Banker, Dec. 22, 1983.
[20] Michael Fritz, *Fine-Tuning the Reverse Mortgage*, Forbes, May 2, 1988, at 116.
[21] *Shaw, supra* note 18.
[22] *See* Home Equity Conversion Mortgage Insurance Demonstration, Housing and Community Development Act of 1987, Pub. L. No. 100-242, § 417 (Feb. 5, 1988). As with all HUD-insurance programs, borrowers pay premiums for the insurance and HUD guarantees that the lender will be repaid, up to specified limits, for extending credit to the homeowner. Under the HECM program, the senior homeowner is also protected by HUD in the event the lender is unable to fulfill its payment obligation.
[23] In 2006, the number of HECM mortgages that HUD is authorized to insure was raised to 275,000. Pub. L. No. 109-289, § 131 (2006). The number of HECM loans now exceeds the 275,000 limit with 424,371 active endorsements as of May 2009. Under the enabling statute HUD does not have the authority to insure additional loans. However, Congress has temporarily extended HUD's authority to insure HECMs notwithstanding the statutory limits. *See* Omnibus Appropriations Act, 2009, Pub. L. No. 111-8, § 217 (Mar. 11, 2009); Consolidated Appropriations Act, 2008, Pub. L. No. 110-161, § 219 (Dec. 26, 2007).
[24] *See Dep't of Housing and Urban Dev., supra* note 2.
[25] *See id.*
[26] *See* John C. Dugan, Comptroller of the Currency, Remarks before the American Bankers Association Regulatory Compliance Conference: Consumer Protections for Reverse Mortgages (June 8, 2009) at 4, *available at* http://www.occ.treas.gov/ftp/release/2009-61a.pdf.
[27] HMDA is codified at 12 U.S.C. §§ 2801–2810.
[28] 12 C.F.R. § 203.2(k) (2009).
[29] 12 C.F.R. § 203.4(c)(3) (2009).
[30] Marketing-to-Seniors.com Home Page, www.marketing-to-seniors.com (last visited July 27, 2009).
[31] Data compiled from U.S. Census Bureau, Age: 2000, a Census 2000 Brief, Oct. 2001, at 6, and U.S. Census Bureau, U.S. National Population Projections (2008) at tables 2, 3, *available at* http://www.census.gov/population/www/projections/summarytables.html, and Frank Hobbs and Nicole Stoops, U.S. Census Bureau, *Demographic Trends in the 20th Century*, November 2002, Table 5, parts C and D.
[32] *Id.*
[33] Patrick Purcell, *Income and Poverty Among Older American in 2007*, Congressional Research Service (Oct. 3, 2008), *available at* http://wikileaks.org/wiki/CRS-RL32697.
[34] William Apgar, Zhu Xiao Di, Joint Center for Housing Studies, Harvard University, *Housing Wealth and Retirement Savings: Enhancing Financial Security for Older Americans* (Sept. 2005) *available at* http://www.jchs.harvard.edu/publications/finance/w05-8.pdf.
[35] U.S. Census Bureau, American Housing Survey, Table7-15: Mortgage Characteristics—Owner-Occupied Units with Elderly Householder (2007), *available at* http://www.census.gov/hhes/www/housing/ahs/ahs07/tab7-15.pdf.
[36] *Id.*
[37] National Reverse Mortgage Lenders Association, 2008 Annual Meeting and Expo "Why Attend," *available at* www.nrmlaonline.org/annual2008/whyattend.aspx.
[38] This estimate, which predates the recent real estate crash,

was calculated using data from the U.S. Census Bureau, American Housing Survey, Tables 7-14, 7-15 (2007), *available at* http://www.census.gov/hhes/www/housing/ahs/ahs07/ahs07.html. The AHS data provides median home value and median outstanding mortgage debt for seniors. The distribution of mean home values for seniors tends to be positively skewed and therefore median values provide a more conservative estimate of total senior home equity.

[39] U.S. Census Bureau, American Housing Survey, Table 7-19: Detailed Tenure by Financial Characteristics—Occupied Units with Elderly Householder (2007), *available at* http://www.census.gov/hhes/www/housing/ahs/ahs07/tab7-19.pdf.

[40] *See id.*

[41] Solicitation to attend a "Reverse Mortgage Success Workshop" from Senior American Funding, Inc., Nov. 2, 2007 (on file with the National Consumer Law Center).

[42] Ed Szymanoski, U.S. Dep't of Housing and Urban Dev., *The U.S. HECM Reverse Mortgage Program: How Far We've Come and the [sic] What the Future May Hold*, July 2008, at 20–21.

[43] Peter Coy, *Why Subprime Lenders Are In Trouble*, BusinessWeek, Mar. 2, 2007, *available at* http://www.businessweek.com/bwdaily/dnflash/content/mar2007/db20070302_477856.htm.

[44] Government Accountability Office, *Reverse Mortgages: Product Complexity and Consumer Protection Issues Underscore Need for Improved Controls over Counseling for Borrower*, GAO-09-606, at 1 (June 29, 2009), *available at* http://www.gao.gov/new.items/d09606.pdf.

[45] *Id.*

[46] *See, e.g.,* Credit Suisse, Equity Research, *Mortgage Liquidity du Jour: Underestimated No More*, March 12, 2007, at 22 (Exhibit 14: Top Subprime Lenders, 2006). *See also* Complaint, Illinois v. Wells Fargo and Company, et al., Cook County No. 09CH26434 (July 31, 2009) at ¶ 35, 37 *available at* http://www.illinoisattorneygeneral.gov/pressroom/2009_07/WELLS%20FARGO%20COMPLAINT_07-31-2009_13-44-30.pdf.

[47] *See* Wholesale Leaders Report, Reverse Market Insight, Inc. (Apr. 2009), *available at* http://www.rminsight.net/hecm-endorsement-archive/WholesaleLeaders_200904.pdf.

[48] *See* "The Vision & Values of Wells Fargo" at p.8, available at www.wellsfargo.com/invest_relations/vision_values (last viewed Aug. 6, 2009).

[49] Complaint, Mayor and City Council of Baltimore v. Wells Fargo Bank, N.A., No. 1:08-cv-62 (D. Md. Jan. 8, 2008).

[50] Declaration of Elizabeth M. Jacobson at ¶8, Mayor and City Council of Baltimore v. Wells Fargo Bank, N.A., No. 1:08-cv-62 (D. Md. June 1, 2009).

[51] *See* Complaint, Illinois v. Wells Fargo and Company, et al., Cook County No. 09CH26434 (July 31, 2009) at ¶ 83, 87, *available at* http://www.illinoisattorneygeneral.gov/pressroom/2009_07/WELLS%20FARGO%20COMPLAINT_07-31-2009_13-44-30.pdf.

[52] *See* Wholesale Leaders Report, April 2009, from Reverse Market Insight Inc.

[53] *Testimony of George B. Lopez, Vice President, James B. Nutter & Company, Before the Special Committee on Aging, United States Senate,* at 4 (Dec. 12, 2007).

[54] *Id.* at 5.

[55] Complaint, Collins v. James B. Nutter & Co., No. RG0945-1455 (Cal. Sup. Ct. Alameda, April 10, 2009). Additional information from interview with and documents supplied by Daniel Murphy, lawyer for Collins' family.

22 Telephone interview by Rick Jurgens with George Lopez, June 2009.

[56] American Reverse Mortgage Corp., www.americanreverse.com/csa.htm (last visited on July 30, 2009). Certified Senior Advisor is a designation offered by the Society of Certified Senior Advisors and requires approximately three to four days of coursework.

[57] *See* Wells Fargo & Wells Fargo Home Mortgage presentation at the American Securitization Forum Conference, Feb. 2008 (noting its 750 Certified Reverse Mortgage Consultants (CRMCs), *available at* www.sec.gov/Archives/edgar/data/1011663/000119312508017741/dfwp.htm. While not included on the list of professional designations tracked by the Financial Industry Regulatory Authority, the "Certified Reverse Mortgage Consultant" designation is offered by the National Reverse Mortgage Training Institute. The requirements to obtain the certification includes 36–40 hours of classroom instruction and 10–20 hours of self-study.

[59] In the insurance and securities industries, federal and state lawmakers have sought to rein in the use of senior designations that misleadingly imply expertise by apparent "experts" who are little more than salespersons. In 2007, an investigation by the U.S. Senate Special Committee on Aging found that many of the senior designations "represent limited or no value with respect to advising seniors on financial matters, and that often these designations are obtained simply by attending a weekend seminar and passing an open-book, multiple choice test. Press Release, Kohl Investigates Use of Questionable Senior Financial Advisor Designations (Sept. 5, 2007), http://aging.senate.gov/record.cfm?id=281803.

[60] Mortgage Bankers Association of America, Agenda for Fall 2008 Mortgage Lending Conference, *available at* http://events.mortgagebankers.org/rmlf2008/agenda.

[61] *Statement of Carol Anthony before the United States Senate Special Committee on Aging,* at 1–2 (Dec. 12, 2007), *available at* http://aging.senate.gov/events/hr185ca.pdf.

[62] Press Release, County of Wayne, MI Office of the Prosecuting Attorney, Prosecutor Worthy of Charges in Connection with Reverse Mortgage Fraud Scheme (June 14, 2006). In February 2007, James was convicted on six counts of larceny and sentenced to state prison. *See* www.state.mi.us/mdoc/asp/otis2profile.asp?mdocNumber=633246 .

[63] Atare E. Agbamu, *Your Mother Was Right: Ethical Issues in Reverse Mortgage Lending*, July 27, 2007, *available at* www.nrmla.org/RMS/GETTING_STARTED.ASPX?article_id=572.

[64] Nandinee K. Kutty, *The Scope for Poverty Alleviation Among Elderly Home-owners in the United States Through Reverse Mortgages*, 35 Urban Studies 113, 127 (1998).

[65] Edward J. Szymanoski, et al., *Home Equity Conversion Mortgage Terminations: Information to Enhance the Developing Secondary Market*, 9 Cityscape 1, 14 (2007), *available at* http://papers

.ssrn.com/sol3/papers.cfm?abstract_id=1089424#.

[66] *See* Fannie Mae Selling and Servicing Guides Announcement 09-16 (Jun. 1, 2009) (Fannie Mae made revisions in its purchase policy to standardize and simplify HECM product offerings and encourage a market shift toward securitization).

[67] American Securitization Forum, *Reverse Mortgages*, at 12, February 5, 2008, *available at* http://www.mortgagebankers.org/files/Conferences/2008/2008ReverseMortgage/RM08CurrentOriginationIssuesPresentation.pdf.

[68] Ed Szymanoski, U.S. Dep't of Housing and Urban Dev., *The U.S. HECM Reverse Mortgage Program: How Far We've Come and the [sic] What the Future May Hold*, July 2008, at 27.

[69] *See* Remarks of Michael Frenz to the National Reverse Mortgage Lenders Association (Nov. 18, 2008), *available at* http://www.ginniemae.gov/media/Natl_Rev_Mrtg_Lenders_Assoc_111808.pdf?Section=Media (noting as of Nov. 2008, Ginnie Mae had securitized $1.3 billion in HECM loans); Reverse Mortgage Daily, *Ginnie Mae Issuance of Reverse Mortgage Securities Holds Steady* (May 14, 2009), *available at* http://reversemortgagedaily.com/2009/05/14/ginne-mae-issuance-of-reverse-mortgage-securities-holds-steady/ (as of end of April, GNMA had issued $437 million in HECM-backed securities

[70] Telephone Interview by Rick Jurgens with Miguel Posada; Complaint, Posada v. Walker, No. S CV 23112 (Cal. Sup. Ct. Placer, June 11, 2008).

[71] Engel, Kathleen C. and McCoy, Patricia A., *A Tale of Three Markets: The Law and Economics of Predatory Lending.* Tex. L. Rev., vol. 80, no. 6, at 1282, May 2005,*available at* http://ssrn.com/abstract=286649 or DOI: 10.2139/ssrn.286649.

[72] A report prepared by Financial Freedom Senior Funding, Corp. for the National Council on Aging stated that, "for a growing group of seniors, reverse mortgages provide a means to live more comfortably and pursue their dreams. For example, the funds have been used to buy everything from a second car, an airplane or recreational vehicle, or taking a dream vacation." Financial Freedom Senior Funding Corp. for the National Council on Aging, *Trends in Reverse Mortgages—A New Option for Senior Homeowners,* http://www.ncoa.org/content.cfm?sectionID=11&detail=1659 (last visited July 30, 2009).

[73] Reverse Mortgage Information Center, *List of 25 Ways to Use Your Reverse Mortgage Payment Money, available at* http://www.reversemortgageadviser.com/blog/reverse-mortgages/list-25-ways-reverse-mortgage-payment-money/ (last visited July 30, 2009).

[74] *Id.*

[75] National Reverse Mortgage Lenders Association, *Just the FAQs Answers to Common Questions About Reverse Mortgages*, 2006, at 8.

[76] *See* National Reverse Mortgage Lenders Association, *Florida Senior Uses Reverse Mortgage to Build Airplane*, *available at* www.reversemortgage.org/BorrowerProfiles/BuildingAnAirplane/tabid/246/Default.aspx (last visited July 30, 2009).

[77] Regulators ruled that the mailing aimed to give the impression that the offer came from a government agency rather than a loan arranger. In a consent order on Oct. 21, 2008, American Advisors did not admit it had violated any laws or rules but agreed to pay a $10,000 administrative penalty and to change its solicitations to eliminate false or misleading statements. *See* Consent Order, Commissioner of Banks, Commonwealth of Massachusetts, *In re* American Advisors Group, No: 2008-022-CO (Oct. 21, 2008). Reza Jahangiri, the president of American Advisors Group, said in a that the mailing mentioned in the October consent order was from "a third party marketing firm" and that the mailing subject to the regulators' action was no longer used by the firm. Telephone Interview by Rick Jurgens with Reza Jahangiri, President, American Advisors Group.

[78] The Massachusetts Division of Banks' Administrative Complaint noted that the information contained in the footnote was located on the reverse side of the solicitation and was in a lighter color text and set in a light background, which made the information difficult to read. *See* Administrative Complaint, Commissioner of Banks, Commonwealth of Massachusetts, In the Matter of American Advisors Group, Docket No. 2009-016-OTSC (June 29, 2009).

[79] Unfortunately, new disclosure rules for yield spread premiums do little to fix this problem. Under the new regulations, yield spread premium will be disclosed as a "credit" to the borrower. *See* 73 Fed. Reg. at 68,249, 68,257, *codified at* 24 C.F.R. pt. 3500, Apps. A, C. In calling it a credit, HUD falsely implies that the lender's payment to the broker necessarily provides borrowers with lower settlement or origination costs. To the contrary total broker compensation and settlement costs appear to increase when the lender pays the broker.

[80] 12 U.S.C.A. § 1717z-20(r).

[81] ReverseIt, Urban Financial Group, Pricing Memo (2009) (on file with the National Consumer Law Center).

[82] Telephone Interview by Rick Jurgens with W.L. Pulsipher, President, American Reverse Mortgage (Jan. 12, 2009).

[83] Lori Swanson, the Attorney General of Minnesota, told the Senate Special Committee on Aging on Sept. 5, 2007 that "some insurance agents make very high commissions for selling some of these long-term deferred annuities of up to 9 to 12 percent, plus other incentives. An agent who sells a $100,000 annuity may receive a commission of $9,000 to $12,000 for just a few hours of work." *Senior Fraud and the Sale of Annuities: Hearing Before the S. Special Comm. on Aging*, 110th Cong. (2007) (testimony of Lori Swanson, Att'y Gen. of Minnesota), *available at* http://www.gpo.gov/fdsys/pkg/CHRG-110shrg301/html/CHRG-110shrg301.htm.

[84] Complaint, Anthony v. Financial Freedom Senior Funding Co., No. M7 § 107 (Cal. Sup. Ct. Monterey, March 28, 2008).

[85] 12 U.S.C.A. 1715z-20(n)(1) ("The mortgagee and any other party that participates in the origination of a mortgage to be insured under this section shall: (A) not participate in, be associated with, or employ any party that participates in or is associated with any other financial or insurance activity; or (B) demonstrate to the Secretary that the mortgagee or other party maintains, or will maintain, firewalls and other safeguards designed to ensure that—(i) individuals participating in the origination of the mortgage shall have no involvement with, or incentive to provide the mortgagor with, any other financial or insurance product; and (ii) the mortgagor shall not be required, directly or indirectly, as a condition of

obtaining a mortgage under this section, to purchase any other financial or insurance product.") 12 U.S.C. 1715z-20(o). ("The mortgagor or any other party shall not be required by the mortgagee or any other party to purchase an insurance, annuity, or other similar product as a requirement or condition of eligibility for insurance…")

[86] Telephone Interview by Rick Jurgens with Neil Granger, Aug. 4, 2009.

[87] The GAO found that "at least 26 states have adopted the National Association of Insurance Commissioners (NAIC) model regulation for suitability in annuity transactions" and that "at least 10 other states have adopted other legislation or regulations related to the suitability of insurance products." However, more than half these states do not provide the consumer with a private right of action to enforce this suitability standard. *See* Government Accountability Office, *supra* note 44, at 28.

[88] *See* Tammy Kraemer and Tyler Kraemer, The Complete Guide to Reverse Mortgages, Adams Media Corporation ch 5 (2007) ("Because Financial Freedom is the largest reverse mortgage specialist, its Cash Account Advantage Plan provides a good example of proprietary jumbo reverse mortgages.")

[89] *Id.* at 63–64. See also Financial Freedom Cash Account Advantage Plan, FAQ, *available at* http://www.financialfreedom.com/Templates/Print_Products.aspx#FF_CASH_ACCOUNT (last visited July 31, 2009).

[90] *See* Bank of America Home Loans, Bank of America Proprietary Product, http://reversemortgage.bankofamerica.com/details/how-reverse-mortgages-work/senior-equity-reverse-mortgage-platinum.aspx (last visited July 31, 2009).

[91] *See Dugan supra* note 1, at 4–5.

[92] Kathleen Pender, *S.F. Firm stopping new deals on equity*, S.F. Chron., Oct. 16, 2008, at C1. *See also* REX & Co. website at www.rexagreement.com/index.php/rex/who_we_are_coverage_map/

[93] Telephone Interview by Rick Jurgens.

[94] *See* EquityKey, Overview, Coverage Map & Timeline, www.equitykey.com/overview (last visited July 30, 2009).

[95] Telephone Interview by Rick Jurgens with Jeffrey Nash, Founder, EquityKey (January 2009). Those prospects seemed to dim in July 2009, after EquityKey's parent company, KBC Group, a large Belgian bank, announced that it was "conducting a company-wide review of its operations and deployment of capital" and shutting down its U.S. reverse mortgage unit. Notice, Senior Lending Network, www.seniorlendingnetwork.com (last visited July 21, 2009).

[96] *Id.*

[97] Telephone interview by Rick Jurgens with Marvin Kidwiler.

[98] Loan Closing Documents provided by Marvin Kidwiler (on file with National Consumer Law Center).

[99] Reg. Z, 12 C.F.R. § 226.33(c)(6) (2009).

[100] *See* Government Accountability Office, *supra* note 44, at 8.

[101] 12 U.S.C. § 1715z-20(d)(2)(B) (2009). Counseling may not be provided by any party that is directly or indirectly associated with 1) originating or servicing the mortgage, 2) funding the loan, or 3) the sale of annuities, investments, long-term care insurance, or any other type of financial or insurance product. *Id.*

[102] *See* 12 U.S.C. 1715z-20(f); Dep't of Housing and Urban Dev., Mortgage Letter 2009-10 (March 27, 2009).

[103] Dep't of Housing and Urban Dev., Mortgagee Letter 2009-10 (Mar. 27, 2009).

[104] 12 U.S.C. 1715z-20(f) (2009).

[105] Dep't of Housing and Urban Dev. Mortgagee Letter 2009-10 (Mar. 27, 2009).

[106] Dep't of Housing and Urban Dev., Mortgagee Letter 2008-12 (May, 6, 2008).

[107] Dep't of Housing and Urban Dev., Mortgagee Letter 2008-28 (Sept. 29, 2008). Lenders previously were permitted to pay for borrower counseling through a lump sum or on a case-by-case basis. However, the independence requirement for counseling imposed by the Housing and Economic Recovery Act of 2008, now precludes such payments.

[108] *Hearing Before the S. Special Comm. on Aging* (2004) (statement of John C. Weicher, Ass't Sec., Dep't of Housing and Urban Dev.). *Statement of John C. Weicher, Assistant Secretary, Department of Housing and Urban Development, before the United States Senate Special Committee on Aging*, (Feb. 24, 2004).

[109] Government Accountability Office, *Reverse Mortgages: Product Complexity and Consumer Protection Issues Underscore Need for Improved Controls over Counseling for Borrower*, GAO-09-606, at 30-47 (June 29, 2009), *available at* http://www.gao.gov/new.items/d09606.pdf.

[110] Donald Redfoot, Ken Scholen and S. Kathi Brown, AARP, *Reverse Mortgages: Niche Product or Mainstream Solution? Report on the 2006 AARP National Survey of Reverse Mortgage Shoppers* (2007), at 90–95, *available at* http://assets.aarp.org/rgcenter/consume/2007_22_revmortgage.pdf.

[111] *2005 Record Year for FHA Reverse Mortgage*, Home Equity Wire, Nov. 15, 2005.

[112] Abt Associates Inc. for Dep't of Housing and Urban Dev., Office of Policy Development and Research, *The State of the Housing Counseling Industry*, September 2008, at 143.

[113] Dep't of Housing and Urban Dev., *HUD Offers $58 Million for Housing Counseling*, New Release HUD No. 09-088, June 16, 2009, *available at* www.hud.gov/news/release.cfm?content=pr09-088.cfm.

[114] A New Hampshire law that took effect July 31, 2009 bans payment of a yield spread premiums in any reverse mortgage transactions.