> ***Angels come from everywhere with lots of jack***
> ***And when you lose it, there's no attack***
> ***Where could you get money that you don't give back?***
> ***Let's go on with the show!***
>
> There's No Business Like Show Business, Irving Berlin (1946).

Reverse Mortgages In Overdrive: Practical Uses on the Legal Aid and Elder Law Expressway

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1. Overview.

   A. What's a reverse mortgage?

A reverse mortgage is a loan in which the borrower's equity is used to fund a loan to the borrower. It is a highly flexible device which assures that, as long as the borrower lives in and maintains the home (pays taxes, insurance, and ordinary maintenance), the loan requires no repayment. At the time of repayment (usually death), the home itself is the only estate asset of the borrower which can be attached for repayment.

As developed in the outline, there are a number of cases in which low income SSI and Medicaid beneficiaries may find these devices attractive, if not transformative.

The core reason that the legal aid and elder law practitioner should keep this arrow in the quiver is based upon two simple rules:

The home of a Supplemental Security Income[1] or Medicaid[2] recipient is an exempt resource.

Proceeds which a recipient receives from a loan are excluded from the definition of income by SSI[3] and Medicaid.[4]

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* The writer thanks his friend of many years and expert in this practice area, Mr. Jim Warns, for his many contributions to this brief work. Jim will co-present this paper at the 2014 Annual Statewide Legal Aid Conference in October, 2014, in Portsmouth Virginia. Any errors are entirely the responsibility of R. Shawn Majette, and the good ideas found here have been improved by Mr. Warns' thoughtful, deft and patient suggestions. Jim's contact information is James Warns, NMLS # 506555, Security 1 Lending, 7400 Beaufont Springs Drive, Suite 300, Richmond, Virginia 23225, 804-714-8007 (voice) 804-441-9520 (fax), jwarns@S1L.com.

[1] POMS SI 01130.100. "Home serving as the principal place of residence, including the land on which the home stands and other buildings on that land, is exempt."

[2] Va. Medicaid Manual § S 1130.100. "Ownership of a dwelling occupied by the applicant as his home does not affect [Medicaid] eligibility."

B. This presentation only addresses HECM Reverse Mortgages.

   i. A HUD overseen and insured program in existence for many years.

   ii. Easily customizable and modifiable (see below)

   iii. Competitive marketplace in which lenders are monitored and overseen by HUD.[5]

C. Basic structure.

   i. Borrower requirements. The borrower must:

      1. Be 62 years of age or older.

      2. Own the property outright or paid-down a considerable amount.

      3. Occupy the property as principal residence.

      4. Not be delinquent on any federal debt.[6]

      5. Have access to sufficient financial resources[7] to continue to make timely payment of ongoing property charges such as property taxes, insurance and Homeowner Association fees, etc.

      6. Participate in a consumer information session given by a HUD-approved HECM counselor.[8]

      7. Three day rescission period.[9]

   ii. Property requirements.

      1. Type.

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[3]POMS SI 00815.350. "Money that a person borrows under a bona fide loan agreement is not income. Money received as repayment of the principal of a bona fide loan is not income. A bona fide agreement is an agreement that is legally valid and made in good faith."

[4] Va. Medicaid Manual § M 0815.350. "Money that a person borrows or money received as repayment of the principal of a loan is not income."

[5] Link: http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmlenders.

[6] It is unclear whether this would include a SSI overpayment *when* an accommodation has been reached. See POMS SI 02220.015 SSI *Overpayment - Recovery By Adjustment*, and the limit of adjustment of the SSI benefit, and POMS SI 02220.016 SSI *Overpayment - The 10 Percent Rate of Adjustment*, discussed at footnote 29, regarding overpayment recoupment.

[7] This may include "resources" for SSI / Medicaid purposes or unencumbered income.

[8] http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmabou.

[9] Handbook, 6.11 (K), citing 12 CFR 226.15.

a. Single family home or 2-4 unit home with one unit occupied by the borrower

b. HUD-approved condominium project

c. Manufactured home that meets FHA requirements

2. Value (limit amount for loan): Lesser of
   a. appraised value;
   b. HECM FHA mortgage limit of $625,500; or
   c. the sales price.

iii. Loan Payment Options.
   1. Tenure - equal monthly payments as long as at least one borrower lives and continues to occupy the property as a principal residence.
   2. Term - equal monthly payments for a fixed period of months selected.
   3. Line of Credit - unscheduled payments or in installments, at times and in an amount of the borrower's choosing until the line of credit is exhausted.
   4. Modified Tenure - combination of line of credit and scheduled monthly payments for as long as the borrower remains in the home.
   5. Modified Term - combination of line of credit plus monthly payments for a fixed period of months selected by the borrower.

iv. Repayment.[10]
   1. Debt (with interest) falls due at death, vacation from the home (for more than 12 months), material breach (*i.e.*, insurance, taxes, and maintenance).
   2. Debt is non-recourse.[11] Only the home (and if insufficient, the mortgage insurance policy which is required in the settlement of the loan process) stands as collateral for the home.

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[10] The Promissory Note provides an exhaustive listing of the events that may trigger payment obligations. Handbook, Appendix 2, *Model Fixed Rate Note Form*, § 6.

2. Links.

A. HECM Law and Policy.

i. The HECM Portal[12] is the source for how these loans are offered and administered.

ii. Lender's portal.

1. The Handbook[13] publishes the policy and addresses the beginning, middle and end of the HECM Reverse Mortgage process.

a. Not client friendly.

b. The appendices include the official settlement forms and are worth reviewing well in advance of any settlement.

2. Mortgagee letters[14] interpret and update the Handbook.

a. Highly technical.

b. Useful principally to the lender or broker in placing the loan.

3. Irritants and caveats.

a. As of the time of publication, no resource integrates Mortgagee Letters with

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[11] Link: http://portal.hud.gov/hudportal/documents/huddoc?id=OHC_HECMNR061213.pdf. "Borrower shall have no personal liability for payment of this Note. Lender shall enforce the debt only through sale of the Property covered by the Security Instrument ("Property"). If the Note is assigned to the Secretary, the Borrower shall not be liable for any difference between the mortgage insurance benefits paid to Lender and the outstanding indebtedness, including accrued interest, owed by Borrower at the time of the assignment." *Id.*, § 4 (C).

[12] Link: http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmhome.

[13] Link: http://portal.hud.gov/hudportal/HUD?src=/program_offices/administration/hudclips/handbooks/hsgh/4235.1.

[14] Link: http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmml.

Handbook annotations in real time. Consequently, it is useful to have a consultant / broker whose business it is to know the current policy and especially limit amounts.

b. Moreover, the HUD Handbook and ML's establish minimum requirements. Lenders often may have additional requirements which are more stringent and should be known before embarking.

iii. Consumer's portal.[15]

1. Most useful official client materials on the portal.
    a. Use Your Home to Stay at Home (28 pages), a layperson's handbook.[16]
    b. General HECM Frequently Asked Questions.[17]
2. See writer's attached ***unofficial*** "Reverse Mortgage Screening: Simple Client Questions," suggested by the co-presenter, Mr. Warns.[18]

B. SSI POMS specific exemption reference.[19]

Reverse mortgage.

Situation: Eleanor Jones, an eligible individual who owns her home, enters into a mortgage contract with a local bank. Under this contract, the bank provides her with monthly payments which do not have to be repaid as long as she lives in the home. These payments are actually a loan against her equity in the home and must be repaid when she dies, sells the home, or moves.

Analysis: Since Ms. Jones is the borrower, the mortgage contract itself is not a resource to her. Since she lives in the home, it continues to be excluded from resource counting. The payments she receives from the reverse mortgage are loan proceeds so they are not counted as income.

[15] Link: http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm/hecmhome.
[16] Link: http://www.ncoa.org/RMBooklet.
[17] Link: http://portal.hud.gov/hudportal/HUD/program_offices/housing/sfh/hecm/rmtopten.
[18] Appendix.
[19] SI 01140.300, *Promissory Notes and Property Agreements*, (E)(3). Link: https://secure.ssa.gov/apps10/poms.nsf/lnx/0501140300.

C. Virginia Medicaid Manual specific exemption reference.[20]

M1120.225 Reverse Mortgages.

A. Definition. A reverse mortgage is a contract with a bank or other lending institution whereby the bank provides the borrower with monthly payments which do not have to be repaid as long as the individual lives in the home. These payments are a loan against the equity in the home and must be repaid when the individual dies, sells his home, or moves.

B. Policy. The payments from a reverse mortgage are loan proceeds and are not income to the borrower. Proceeds retained after the month of receipt are a resource.

3. Uses and Strategies.
   A. General HECM uses.
      i. Continuation or enhancement of client's housing specific needs (handicap modifications).
      ii. Protection of the home from financial abuse (the lien will discourage fly-by-night home improvement schemers; a monthly or term of years option will limit fraud losses).
      iii. Funds for enhancement of client's non-housing needs / wishes (the new car, the child's education[21]).
      iv. Source for contingency funds[22] (the leaking roof, the broken toilet, the unexpected medical bill, in-home nursing services when Medicaid is not a desirable option).
   B. Debt specific uses.
      i. Foreclosure avoidance.[23]
      ii. Creditor avoidance.[24]

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[20] Link: http://www.dss.virginia.gov/files/division/bp/medical_assistance/manual_transmittals/manual/s11.pdf, Adobe page 55 (10/22/2014 11:12 AM).
[21] ***Caveat***: Medicaid asset transfer of assets analysis.
[22] Consider making at least part of the loan a line of credit to keep this option open.
[23] The HECM can be used to pay off the residue of the mortgage on the house and encumber it. This encumbrance can protect a homeowner from his own spendthrift tendencies – there will be increasingly reduced equity left in the line of credit reserve.
[24] Subject to certain preferential creditor issues in federal bankruptcy law (not likely to be a material consideration for legal aid clients), the home can be rendered unattractive to potential judgment creditors by using a HECM to encumber the same while guaranteeing a residence for the client. For example, a homeowner might use a HECM to

C. Public entitlement uses.

i. Increase Community Spouse Protected Resource Amount for community spouse.[25]

ii. Source of funds in conjunction with SSI / Medicaid to supplement disability or retirement income.[26]

iii. Eating everything on your plate: managing the Medicaid Estate Recovery Program.[27]

iv. Avoiding Medicaid in the first place: long term care insurance retention and proxy.[28]

v. Overpayment and penalty mitigation for SSI / Medicaid.[29]

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pay off (or even purchase) a home which, post transaction, has no equity. A creditor will be unlikely to pursue a creditor's bill to execute on the home.

[25] When total countable resources are less than two hundred percent of the "maximum spousal resource standard" (Va. Medicaid Manual § M 1480.231, presently $117,240), the community spouse can borrow whatever is necessary to increase the allowance to this value. Example: H and W own home and have $140,000 in a bank account.

Case A: No loan before the month of H's institutionalization. W's Community Spouse Protected Resource Amount is only $70,000. She spends $70,000.

Case B: W borrows $94,480 before the month of institutionalization. Total assets on first day of month of institutionalization: $234,480. ½ = maximum Community Spouse Protected Resource Amount ($117,240). Excess resources = $234,480 minus $117,240 = $117,240 to spend. Community spouse repays loan (here in whole) with $94,480, leaving $22,760 to spend, protecting $117,240 instead of $70,000 and protecting only $70,000. Community spouse may spend $22,760 on nursing home care or a brand spanking new Subaru Impreza Sedan for $21,390, leaving $1,300 for taxes, gas, and thank you cards.

Any loan arrangement is effective. However, HECM adds value by providing a continuing source of funds for the community spouse, who can borrow again and again from the home as she needs it.

[26] Client receives an inheritance of $300,000. She lives in an apartment and she is on EDCD Community Based Care waiver. She could buy a home and place a HECM to borrow funds from the home for the rest of her life, placing unused funds back in the system (by partial repayments) before the end of the calendar month in which she borrows, or the month succeeding the month in which she borrows. The home is exempt, the proceeds of the loan are exempt until the following month, and the client can use the funds (or pay them to the mortgagee) at any time in that month without losing eligibility.

[27] Medicaid is required to recover its charges against estates, including homes in which there is not an exempt surviving resident, for services after age 55. 42 USC 1396p; 12 VAC 30-20-141, *Estate recoveries*. Using the loan proceeds during lifetime avoids Medicaid estate recovery. Moreover, after considering possible transfer of assets penalties, borrowing and transferring line of credit funds just prior to death (including to certain trusts) may be useful to provide for the client's wishes and favored beneficiaries.

[28] Lapse happens when the client has long term care insurance which cannot be sustained by reason of premium increases. This can be avoided by using HECM proceeds to pay the premium costs.

[29] Example: long term care penalty mitigation. Harry paid $59,330 for Sam's law school tuition. Four years later, Harry has a stroke and enters a nursing home, leaving Wanda at home with a home worth $400,000, a car, and $20,000 in cash. Harry files for long term care benefits under Medicaid and is granted eligibility except for long term care services by reason of a penalty (10 months, Va. Medicaid Manual § M 1450.630 (D, E)). On Sam's advice (from his elder law class), Wanda borrows under the HECM and pays monthly for ten months, at which point Harry is eligible.

D. Second to die protection (parent and over 62 child, December - May unions).

E. New home acquisitions.

i. HECM for Purchase allows seniors, age 62 or older, to purchase a new principal residence using loan proceeds from the reverse mortgage. Eligible borrowers might purchase a *new* principal residence and obtain a reverse mortgage within a single transaction. The program was also designed to enable senior homeowners to relocate to other geographical areas to be closer to family members or downsize to homes that meet their physical needs, i.e., handrails, one level properties, ramps, wider doorways, etc.

ii. In the Legal Aid area, helpful when there is a Supplemental Security Income / Medicaid "lump sum income" event (e.g., personal injury settlement, unexpected inheritance, etc.) which is insufficient to pay for a new home in full, especially when the client over the age of 65 resides in a substandard owned home or rental property.[30]

4. Teamwork: the HECM Consultant[31] and the lawyer.

A. Why the lawyer needs a consultant.

i. Lists and relationships with qualified lenders.

ii. Knowledge of rates, points, qualified counselors and timing issues.

iii. Knowledge of mathematical modeling.

SSI Overpayment analysis is the same, except less likely to be useful or necessary, see POMS SI 02220.015 SSI *Overpayment - Recovery By Adjustment*, and the limit of adjustment of the SSI benefit, and POMS SI 02220.016 SSI *Overpayment - The 10 Percent Rate of Adjustment*. Section 1631(b)(1)(B) of the Act provides that "the rate of adjustment of payment to recover SSI overpayments will be the lesser of ten percent of the recipient's total monthly income (countable income plus SSI and State supplementary payment) or the recipient's entire monthly benefit."

[30] For disabled borrowers over 62 and but *less* than 65, consider this in conjunction with or as an alternative to a special needs trust to pay (or lend the beneficiary to pay) the maintenance, taxes and insurance costs. As to taxes, consult Virginia Attorney General opinion AG Op. Taxation: Real Property Tax, 2013 Va. AG S-96 (13-070) "Taxation: Real Property Tax— Exemption For Disabled Veterans" ("[t]he exemption from, or deferral of, real property taxes authorized in Article X, § 6(b) for persons not less than 65 years of age or disabled does not extend to a person who has placed title to the real property in any form of trust, but it does extend to a person who otherwise qualifies for the exemption and who holds a life estate in the real property. Further, the exemption for disabled veterans provided in Article X, § 6-A does extend to a qualifying veteran who holds a life estate in the real property.").

[31] A word of definition is in order. The consultant is likely to be an agent of one or more HECM lenders, akin to an independent insurance agent representing multiple carriers. It is important to understand to whom the consultant owes the duty of allegiance.

B. Why the consultant needs the lawyer.

   i. Exposure.

   ii. Potential borrowers can be reasonably screened.

REVERSE MORTGAGE SCREENING: SIMPLE CLIENT QUESTIONS

1) ARE YOU, OR IS THE FAMILY MEMBER, AT LEAST 62? ***IF YES…***

2) DO YOU, OR DOES THE FAMILY MEMBER, OWN A HOME AS A PRIMARY RESIDENCE? ***IF YES…***

3) DOES AT LEAST ONE HOMEOWNER PLAN TO CONTINUE LIVING IN THE HOME? ***IF YES…***

(A <u>NO</u> ANSWER TO 1) – 3): STOP. NOT A PLANNING OPTION)

4) IS THERE A MORTGAGE ON THE HOME? ***IF NO, SKIP TO QUESTION 6. IF YES:***

5) IS THE EXISTING MORTGAGE LESS THAN 50% OF THE VALUE OF THE HOME? IF NO, SKIP TO **LAST TWO QUESTIONS (A and B).**

   IF YES:

6) **<u>BASED ON THE ABOVE ANSWERS A REVERSE MORTGAGE MAY BE A GOOD PLAN.</u>** WOULD YOU LIKE TO TALK WITH SOMEONE ABOUT GETTING CASH FROM THE HOME TO HELP WITH EXPENSES WITHOUT HAVING TO MAKE MONTHLY PAYMENTS?

LAST TWO QUESTIONS

A. CAN YOU ESTIMATE THE MORTGAGE AS A PERCENTAGE OF THE VALUE OF THE HOME: 25%.....50%....75% ETC.? **IF THE ESTIMATE IS 75% OR LESS:**

B. <u>BASED ON YOUR ANSWERS IT IS POSSIBLE THAT YOU MAY QUALIFY</u>. WOULD YOU BE INTERESTED IN SPEAKING WITH SOMEONE ABOUT PROVIDING CASH FROM THE EQUITY IN THE HOME TO HELP WITH LONG-TERM CARE EXPENSES WITHOUT BEING REQUIRED TO MAKE ANY MONTHLY PAYMENTS?