

Case Studies



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Couple's Dream Retirement Within Reach Thanks to Reverse Mortgage Line of Credit

Borrower Profile

Like many couples in their 60s, Tim and Cate were both excited and nervous as they approached retirement. They had always dreamed of traveling as much as possible in the first decade of their retirement — while they were still healthy and physically able to do so — but they knew that to make their dream a reality, they would need to balance the expense of travel against more practical financial considerations. "We wanted to maintain our current home and standard of living while still setting aside a nest egg for the healthcare and long-term care expenses that might crop up later in retirement," said Tim.

Even after delaying Social Security, Tim and Cate would deplete their savings and fall short of their expected cost of living before age 80.

Challenge

First, the couple reached out to their financial planner, who helped Tim and Cate take a hard look at just how much money they would need at different points in retirement — bearing in mind a 50% chance that one of the two would live past age 90. For example, even though the couple planned to travel extensively only during the first decade of their retirement, they wouldn't necessarily need less income later in life. The planner advised Tim and Cate to plan for greater health care needs and inflation of around three percent a year as they aged. Because of this steady increase in their expected cost of living, the couple should probably plan to spend just as much money in the latter part of their retirement as they would during the first ten years of travel.

The planner also advised Tim and Cate to delay drawing on their Social Security benefits until age 70. Those who wait 48 months beyond age 66 to draw on Social Security receive 132% of the benefit to which they're otherwise entitled. In Tim and Cate's case, the extra 32% benefit would mean thousands of dollars a year in additional income — or tens of thousands of dollars over the course of their lives.

Finally, the couple's planner helped them calculate how much their other funds — like IRA, 401(k) and personal savings — might contribute to their retirement income. Now Tim and Cate found themselves in the prickly situation so many Americans face when planning for retirement: even after delaying Social Security, Tim and Cate would deplete their savings and fall short of their expected cost of living before age 80. "The biggest fear for most baby boomers," said Tim, "is running out of money before running out of life."

Solution

Fortunately, the couple's financial planner was familiar with a special type of home equity loan, called a "reverse mortgage," that is specifically designed for older homeowners like Tim and Cate. Reverse mortgages allow homeowners to receive the equity they've built in their own homes as a line of credit, lump sum cash payment or monthly cash advance. In other words, a reverse mortgage could provide Tim

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and Cate a source of income that would support their desired retirement lifestyle and prevent them from having to deplete their IRA and personal savings too early in retirement or during an economic downturn.

A reverse mortgage is a special type of home equity loan specifically designed for older homeowners.

The planner introduced the couple to a reverse mortgage specialist accredited with the Certified Reverse Mortgage Professional (CRMP) designation. The specialist helped Tim and Cate understand how a reverse mortgage might work best for their specific situation. Because they had sufficient income to cover the first several years of retirement expenses, Tim and Cate opted for a reverse mortgage line of credit instead of a cash payment. If they needed to tap into that line of credit, they could do so at any time. Until then, the loan would accrue very little interest with a minimal loan balance — and better yet, the line of credit would grow at a rate of about 5%* a year, meaning even more financial security down the road.

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Amounts borrowed against the line of credit would not be due for repayment unless the couple decided to move or failed to pay their property taxes and insurance — or until Tim and Cate's death. At that time, Tim and Cate's children would have the option to refinance the home and keep it, or sell it and cash out any remaining equity.

"The perfect time to get a reverse mortgage is as young as you can and when interest rates are low. Low interest rates not only save on costs, they actually give the borrower access to more money down the road," said Tim.

Results

Now well into retirement, Tim and Cate are grateful for the financial security and peace of mind provided by their reverse mortgage. "To me, a line of credit is better than having money in the bank, because it's tax-free and I don't have to pay anybody to manage it," said Tim. "It's there if I need it and not accruing interest on my loan if I don't." The line of credit allowed Tim to feel confident delaying his Social Security benefits until age 70 and enabled him to make more strategic decisions about managing his investments. So far, Tim and Cate have checked several destinations off their bucket list and look forward to many more adventures over the course of their retirement.

Tim's advice for others considering a reverse mortgage? "The perfect time to get a reverse mortgage is as young as you can and when interest rates are low. Low interest rates not only save on costs, they actually give the borrower access to more money down the road," said Tim, referring to the inverse relationship between interest rate and line-of-credit size for reverse mortgages. Borrowers get a smaller line of credit when interest rates are high and a larger line of credit when interest rates are low. "Eventually, the line of credit can grow to exceed the value of the home," Tim advised. Reverse mortgage lines of credit grow at a rate equal to the loan's interest rate plus annual mortgage insurance. This means that, unlike traditional mortgage holders, reverse mortgage borrowers actually benefit when interest rates increase because the line of credit grows at an accelerated rate.

"Plus, if you wait to use a reverse mortgage as a last resort, you may not qualify." Reverse mortgages are generally available to homeowners beginning at age 62, and it can become more difficult to qualify for a reverse mortgage over time. "Your credit could be hurt, you could lose a spouse or maybe you don't have the income to qualify for a reverse mortgage anymore," Tim warned. "It's better to get the line of credit and not need it than to need it and not have it."

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* 5% in 2020