Tuesday, July 3, 2012

CFPB: Next Up, Reverse Mortgages!

In a June 28, 2012 Report to Congress, the Consumer Financial Protection Bureau (the CFPB or the Bureau) published its study of reverse mortgage transactions. This study was required by Section 1076 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).

The Report surmised that reverse mortgages are not being used as Congress originally intended, because, rather than provide income for borrowers during retirement, reverse mortgages are being provided to consumers at younger ages, thereby increasing the risk that these borrowers will go broke later in life. The study found that almost half of reverse mortgage borrowers in fiscal year 2011 were younger than 70 years of age.

Furthermore, the Report concluded that 70% of reverse mortgage borrowers withdrew all the available funds at once in lump-sum payments, which the CFPB claims can be squandered quickly, leaving borrowers with the potential to face foreclosure due to the reduced ability to pay property taxes. According to the study, nearly 10% of reverse mortgagors (as of February 2012) were at risk of foreclosure.

In its 231 page Report, the CFPB stated the following "emerging concerns":

1. Reverse mortgages are complex products and difficult for consumers to understand.

2. Reverse mortgage borrowers are using the loans in different ways than in the past, which increase risks to consumers.

3. Product features, market dynamics, and industry practices also create risks for consumers.

4. Counseling, while designed to help consumers understand the risks associated with reverse mortgages, needs improvement in order to be able to meet these challenges.

5. Some risks to consumers appear to have been adequately addressed by regulation, but remain a matter for supervision and enforcement, while other risks still require regulatory attention.

The study identified four major topics "where additional research would help determine if additional consumer education or regulatory action is needed."

Those topics are:

(a) Factors influencing consumer decisions;
(b) consumer use of reverse mortgage proceeds;
(c) the longer-term outcomes of reverse mortgages; and
(d) the differences in market dynamics and business practices among the broker, correspondent, and retail channels.

On July 2, 2012, the CFPB began the process of investigating the consumer use of reverse mortgages. This procedure begins with a Notice and Request for Information. In effect, that CFPB now seeks comment and information from the public on the aforementioned topics.

In this review of reverse mortgages, the CFPB will undertake, among other things, to identify any practice as unfair, deceptive, or abusive, and may provide for an integrated disclosure standard and model disclosures. Additionally, it will seek detailed information from the public on the factors that influence reverse mortgage consumers' decision-making, consumers' use of reverse mortgage loan proceeds, longer-term consumer outcomes of a decision to obtain a reverse mortgage, and differences in market dynamics and business practices among the broker, correspondent, and retail channels for reverse mortgages.

In this article, I will outline the scope of information that the CFPB is seeking from the public, including consumers, housing counselors, financial institutions, and others, regarding consumer use of reverse mortgages and consumer experiences during the reverse mortgage shopping process.*

Factors Influencing Consumer Decisions

The CFPB asks the following questions regarding the factors that influence consumer decisions:

1. What factors are most important to consumers in deciding whether to get a reverse mortgage?

2. What factors are most important to consumers in choosing among products? Among other things, comments could address the choice between fixed-rate, lump-sum reverse mortgages and adjustable-rate, line-of-credit or monthly disbursement reverse mortgages.

3. What factors are most important to consumers in choosing among potential lenders?

Consumer Use of Reverse Mortgage Proceeds

4. Nearly 75% of recent reverse mortgage consumers took out all of their available funds upfront in a lump sum.

a. What do consumers do with these funds?
b. Where do consumers place loan money that they do not use immediately? (i.e., in a savings account, an investment account, a certificate of deposit (CD), et cetera).

5. Some reverse mortgage consumers use reverse mortgage loan funds to refinance a traditional mortgage or home equity loan/line of credit.

a. What proportion of consumers are using reverse mortgage loan funds to refinance a traditional mortgage or home equity loan/line of credit?
b. What proportion of the loan funds are typically spent on paying off an existing mortgage?
c. Do consumers using a reverse mortgage to refinance an existing mortgage typically consider other options first (e.g. moving to a different home or a traditional refinancing)? If not, why not? If so, what factors lead them to choose a reverse mortgage instead?

6. Some reverse mortgage consumers use reverse mortgage loan funds to consolidate non-housing debts.

a. What proportion of borrowers use reverse mortgage loan funds to consolidate non-housing debts?
b. What proportion of the loan funds are typically spent on consolidating non-housing debts?
c. What types of non-housing debts are typically consolidated (i.e., credit card, auto, medical-related debt, et cetera)?

Longer-term Outcomes for Reverse Mortgages Borrowers

7. Consumers typically pay off their reverse mortgage loans earlier than would be expected based on underlying mortality rates.

a. Why do consumers typically pay off their reverse mortgage loans early?
b. Do consumers anticipate being able to pay off a reverse mortgage at a specific time (e.g. upon receiving a pension or retirement benefit) when taking the reverse mortgage loan?
c. Do consumers who pay off their loans early typically feel that the loan was a good choice? Are there things they wish they had done differently?

8. Some consumers pay off a reverse mortgage upon moving out of a home.

a. Why do consumers decide to move? Are such moves typically because the move is planned in advance or because the move is required for health or other reasons?
b. How do reverse mortgage borrowers finance a later move?

9. What are the typical outcomes for borrowers who still have the loan after 5 years or more?

a. Does the loan continue to meet borrowers' financial needs 5 or more years after origination?

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b. If borrowers have drawn all of their available funds, what financial resources do they use to meet new or unexpected expenses?
c. Do borrowers who still have the loan after 5 or more years typically feel that the loan was a good choice? Are there things they wish they had done differently?

Market Dynamics and Business Practices

10. How are brokers, correspondent lenders, and retail loan officers typically compensated?

a. How does this compensation differ by channel?
b. How do compensation structures and regulatory requirements (i.e., mortgage loan originator compensation rules) affect the business practices of lenders and brokers?
c. How do these factors affect the choices presented to consumers?

11. The Bureau has observed that major large bank originators of reverse mortgages tended to originate a far higher percentage of adjustable-rate, line-of-credit (or monthly-installment) loans than the nonbank originators. What explains this difference?

The CFPB has the authority to implement regulations on reverse mortgage transactions. Specifically, it has the authority to implement federal consumer financial laws, including the Truth in Lending Act and the Real Estate Settlement Procedures Act, which already impose requirements on reverse mortgage transactions.

The Report and the Notice and Request for Information, taken together, indicate the CFPB's objectives to (1) provide an authoritative resource on reverse mortgage products, consumers, and markets; (2) identify and assess consumer protection concerns; and (3) explore "critical unanswered questions" and update the public body of knowledge to reflect market realities.

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Labels: CFPB, Consumer Financial Protection Bureau, Dodd-Frank Act, HECM, Loan Officer Compensation, Loan Originator Compensation, Mortgage Compliance, RESPA, Reverse Mortgages, TILA, UDAAP

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