The Golden Years *Dilemma*


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The year 2008 is a milestone for Kathleen Casey-Kirschling. Born January 1, 1946, and considered the first U.S. baby boomer, she retired this year and is now living mostly on a fixed income stream. Another 3.2 million boomers are eligible to retire this year, with about half choosing early retirement instead of waiting until age 65.[1]

The New England region could be strongly affected by the growing wave of retirements, as its population is older than the rest of the country's. The 2000 census indicates that only four of the region's 67 counties had a median age lower than the national level. Moreover, the median age has been growing twice as fast as the nation's since 2000, reaching 39 years of age in 2006. The population cohort aged 65 years and over should become increasingly prominent in New England. It is expected to grow from 13 percent of the population in 2006 to nearly 20 percent in 2025. (See "Percentage of Population Aged 65 Years and Above.")

Rich in Equity, Poor in Income

Casey-Kirschling is fortunate compared with many of her boomer peers. She and her family bought a new villa and moved to Florida with their yacht upon retirement. Many New England seniors do not

Balancing Homeownership and Financial Needs

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have such financial freedom. Although more than 70 percent of New England senior households own their own homes—the highest homeownership rate among all age groups—one in 10 also live in poverty. That's a higher poverty rate than for other householder age groups.

Senior homeowners often epitomize the unique dichotomy of being rich in home equity but poor in income. (See "Home Equity and Median Household Income by Age Group.") With the constraint of relatively limited income streams, senior homeowners often struggle to balance preserving home equity and meeting their financial needs.

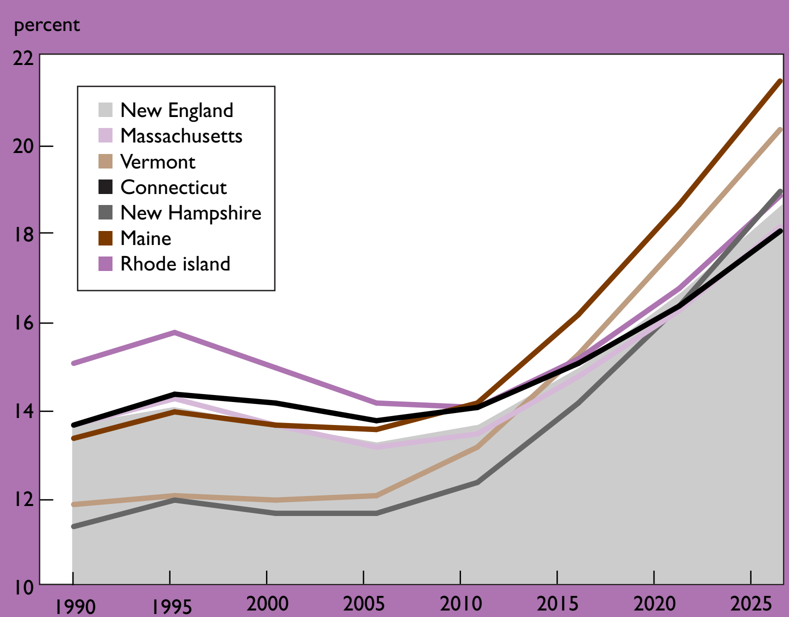
According to Len Raymond, executive director of Homeowner Options for Massachusetts Elders (HOME), seniors' financial burdens have grown over the years, driving their desire to convert home equity into income streams. Continuous increases in health-care costs, energy expenses, and property taxes often disproportionately affect seniors and erode any financial cushion that might have guarded against limited income. For instance, the share of health-care expenses for an elder's budget is usually almost three times that of the general public's, and this gap continues to widen. (See "Percentage of After-Tax Income Spent on Health Care.") So even though medical costs rise for all, seniors' financial cushions are the most vulnerable. That is especially true in New England, where medical costs are increasing faster. Bureau of Labor Statistics data suggest that the real medical-care cost in New England's urban areas increased by 63 percent between 1996 and 2006, outpacing the national level (about a 46 percent increase) as well as the New England region's cost of basic consumer goods (about a 37 percent increase).

Furthermore, seniors' life expectancy is increasing, so they may not have saved enough for retirement. Many elders are not financially prepared for the loss of a spouse, which often results in a 40 percent to 60 percent decline in household income and further reduces their ability to absorb increases in routine costs.

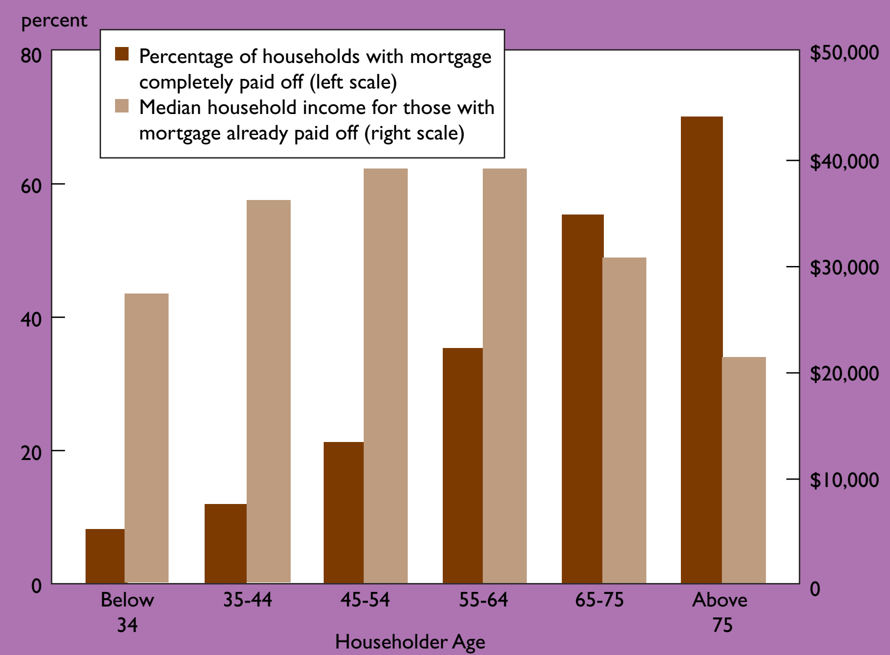
The Gerontology Institute of the University of Massachusetts, Boston, estimates that a one-person senior household with a paid-off mortgage typically would need to spend $17,683 annually to maintain a basic living standard in Middlesex County, Massachusetts. A two-person household would need $27,245. However, 2006 Social Security payments—a major income source for low- and moderate-income senior homeowners—averaged only $12,024 and $19,776 for these households, respectively.[2]

The challenge of preserving homeownership and meeting financial needs becomes clearer when seniors' financial characteristics are considered in the context of their high home-equity level. Raymond explains that the dichotomy often makes seniors more receptive to aggressive lenders who

Percentage of Population Aged 65 Years and Above, 1990-2025



Source: State Population Projection, U.S. Census Bureau



Home Equity and Median Household Income by Age Group, New England Region, 2006

Source: PUMS 2006 American Community Survey

encourage them to tap into home equity to make up for financial shortfalls. Reverse mortgages are increasingly the financial product seniors choose when seeking to convert equity into income.

Reverse Mortgages

The Federal Trade Commission lists three primary types of reverse mortgages: reverse mortgages that are federally insured and commonly known as Home Equity Conversion Mortgages (HECM); the ones offered by some state and local government agencies and nonprofit organizations; and proprietary reverse mortgages backed by private companies.[3] The National Reverse Mortgage Lenders Association estimates that HECMs have about 90 percent of the U.S. reverse mortgage market.[4] The volume of HECMs has grown exponentially, from merely 5,208 a decade ago to 107,558 in fiscal year 2007. (See "Originations of Home Equity Conversion Mortgages.")

Senior homeowners 62 and older can use an HECM to convert their primary residence's equity into monthly income and/or a line of credit to be repaid when they no longer occupy the home. The actual amount of a reverse mortgage depends on factors such as the age of the youngest borrower, the current interest rate, and the property's appraised value. Generally speaking, a homeowner can get more from a reverse mortgage if her home is more valuable, she is older, and the interest rate is low. To ensure that homeowners understand HECM complexities, applicants must attend a consumer information session before their application can be approved. Some states have additional regulations: Massachusetts, for example, has extra licensing requirements for HECM lenders.

Before reverse mortgages became common, senior homeowners had two primary ways to convert home equity into income. One was to sell their properties and relocate. The other was to borrow against the home. Borrowing required monthly loan repayments, which many seniors either did not want or could not afford.

Reverse mortgages provided an alternative that allowed senior homeowners to convert their equities into income while remaining in their homes without making regular repayments. An earlier study suggested that reverse mortgages could lift as many as 29 percent of poor, elderly homeowners out of poverty.[5] Despite their advantages, reverse mortgages are not necessarily the right option for every senior homeowner. Raymond notes the high upfront costs, monthly service fees, adjustable rates, and other costs, and advises senior homeowners to examine all options carefully and choose a strategy that balances both homeownership and financial needs.

Striking the Right Balance

Given recent financial innovations and the housing market's complexity, it is often challenging for seniors to strike the right balance between preserving equity and meeting financial needs. Laura Henze Russell, founding director of the Elder Economic Security Standard Project at the Gerontology Institute and current director of the institute's Elders on the Edge program, recommends that senior homeowners first examine whether they have exhausted all available assistance and tax exemptions before seeking out equity conversion.

Current assistance programs include property tax relief and deferral, home repair assistance, fuel assistance, and utility discounts. Massachusetts seniors who claimed local property tax exemptions in 2004 typically received $500, the equivalent of about one-fifth of the median Massachusetts property tax bill.[6] By minimizing housing-associated costs, the programs help elder homeowners stretch their discretionary spending to other critical areas. However, as Russell stresses, low participation rates for programs like property tax deferral show that many senior homeowners are not taking full advantage of the options.

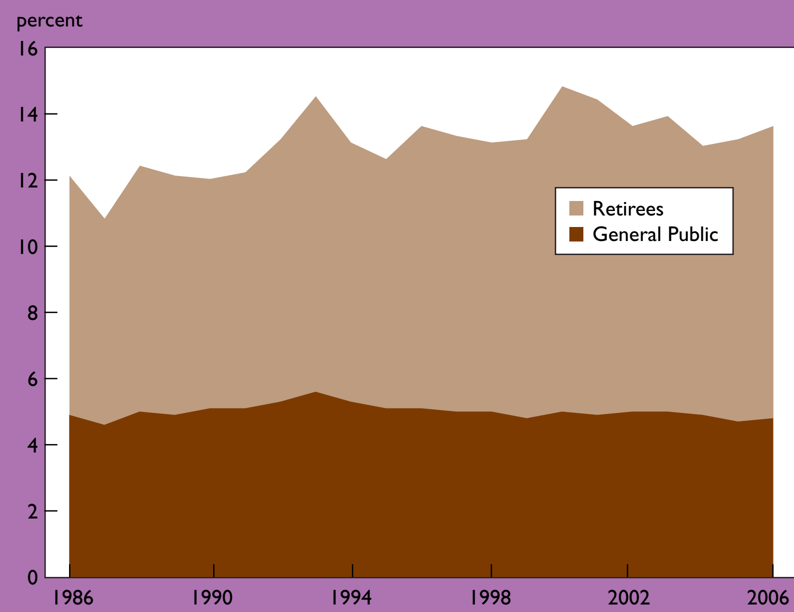
Susan Jacobs, director of the Council on Aging in Dalton, Massachusetts, emphasizes that local agencies need to cooperate with one another while remaining closely engaged with seniors who struggle with property taxes and other housing difficulties.

She adds that seniors should seek help early. Local agencies often have knowledge and access to resources that can alleviate elder homeowners' financial burdens without depleting their equity.

Numerous nonprofit organizations also help senior homeowners strike the right balance. For instance, Homeowner Options for Massachusetts Elders has provided on-site counseling at seniors' homes to more than 23,000 Massachusetts elders since 1984. Most were single women from low- and moderate-income families. Although the group focuses on homeownership preservation counseling, it has partnered with about 70 lending institutions for low-cost reverse-mortgage loans and equity lines of credit for seniors who need to tap into equity.

Proper planning and adequate knowledge about the many kinds of assistance available can help boomers navigate the ever changing terrain of personal finance and homeownership. In doing so, they can strike the right balance between preserving equity and meeting financial needs for their Golden Years.

Percentage of After-Tax Income Spent on Health Care, 1987-2006



Source: Consumer Expenditure Survey, U.S. Bureau of Labor Statistics

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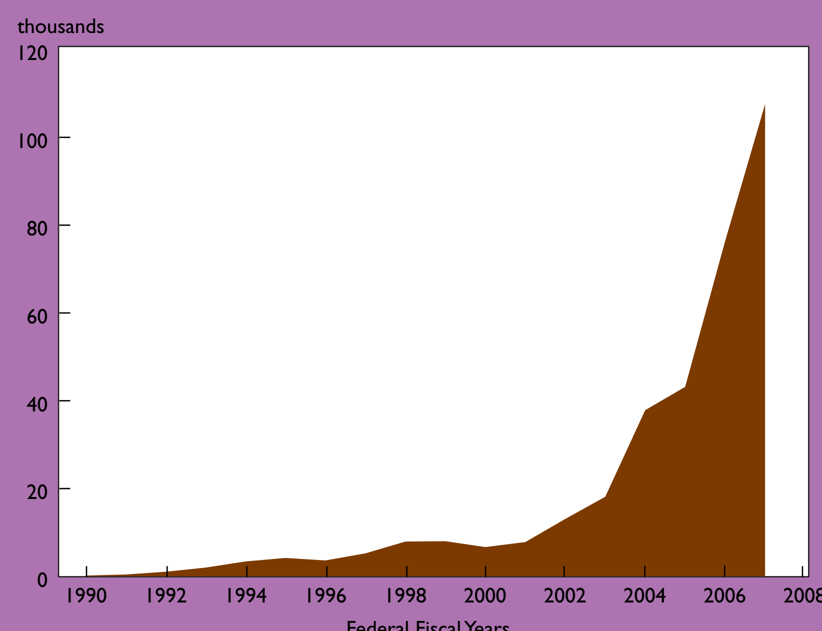
Originations of Home Equity Conversion Mortgages, 1990-2007



Source: Department of Housing and Urban Development (HUD)

Endnotes

[1] R. Wolf, "Social Security Hits First Wave of Boomers," USA Today, Oct. 8, 2007.

[2] Laura Henze Russell et al., *Elder Economic Security Initiative: The Elder Economic Security Standard for Massachusetts* (The Gerontology Institute of the University of Massachusetts: Boston, 2006), 8.

[3] See http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea13.shtm.

[4] See http://www.nrmla.org/rms/statistics/default.aspx?article_id=601.

[5] Nandinee K. Kutty, "The Scope for Poverty Alleviation among Elderly Homeowners in the United States through Reverse Mortgages," *Urban Studies* 35, no. 1 (1998): 113-129.

[6] *The State Auditor's Report on the Local Financial Impact of Property Tax Exemptions for Senior Citizens* (Auditor of the Commonwealth: Boston, 2005), ii.