

## HECM Changes: Two risks remain

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Lenders and originators alike were blindsided with the announcement of the [Collateral Risk Assessment](#). This process reviews every HECM file and requires a second appraisal when the FHA's automated valuation model determines the values are inflated. In normal times one could fairly say I have egg on my face. The truth is these are far from normal times.

Unlike previous mortgagee letters [Mortgagee Letter 2018-06](#) includes a sunset provision. It states an evaluation of the new protocol will be made six and nine months after enactment to "determine if the goals of the guidance have been met". This would leave many to believe if the policy is deemed to be ineffective in stemming losses it would be repealed. However, how the agency will measure the effectiveness eliminating inflated appraisals for loans that were only endorsed merely months before remains to be seen.

Few are asking an underlying question that will shape every effort to curb future losses or HECM claims against the Federal Housing Administration's Mutual Mortgage Insurance Fund. That question is if the Home Equity Conversion Mortgage is a true mortgage loan or a social program. On its face many would answer- of course, it's a mortgage loan. Mortgage loans by their very nature are designed to mitigate risk over time. The reverse mortgage being a collateralized loan solely dependent on the remaining equity at loan termination seeks to reduce risk of losses by adjusting loan proceeds based on the age or life expectancy of the youngest borrower. But there are two other risk factors that may be eroding the economic value of the Home Equity Conversion Mortgage: the assumed annual 4% appreciation rate and deferred property maintenance.

### Home Appreciation & Geo-Centric PLFs

While homes values have appreciated significantly in recent years there remain several regions of the country where historic annual appreciation rates rarely reach 4%. HECM loans originated in these areas are much more likely to result in an insurance claim having values insufficient to offset the ending loan balance at loan termination. A pure mortgage loan risk management approach would advocate reducing this risk by reducing principal limit factors for homes in these areas. A social program approach would avoid any such adjustments to account for future risk by seeing such a policy as discriminatory. Traditional mortgage loans discriminate between borrowers with low or high credit scores, too much debt or acceptable debt levels. Each is afforded a certain amount of available funds accordingly. In addition, home appreciation rates are expected to slow in the coming years as the Federal Reserve continues raising the benchmark interest rate. The longer we apply national PLFs despite a property's appreciation rate the more likely we are to see losses from such properties.

### Deferred Maintenance & MMI Claims

Another risk is deferred maintenance leading to HECM properties being in poor condition at the time of sale. While there is a provision that the property must be maintained in good condition meeting HUD's standards, what measures are in place today to ensure properties retain their economic value when the last borrower moves or passes away? As homeowners age keeping the home in good repair becomes problematic often leading to deferred maintenance which impacts the home's ultimate value. The issue is what resources and staffing would be required to make monitoring properties practical or for that matter even realistic.

The value proposition of the reverse mortgage remains strong, however, measures to prevent future insurance claims or losses should target problematic properties, not all future borrowers.