HOUSING WEALTH CONVERSATIONS

7 Ways Reverse Mortgages Improve Social Security

Innovative Approaches to Strengthen Retirement Outcomes

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Executive Summary

Don Graves, President of The Housing Wealth Institute, highlights the strategic use of reverse mortgages, particularly Home Equity Conversion Mortgages (HECMs), to enhance retirement income and delay Social Security benefits. Leveraging home equity through HECMs provides retirees with tax-free funds, offering financial stability without depleting savings. HECMs can bridge income gaps, avoid the "Tax Torpedo," support surviving spouses, manage Medicare costs by reducing taxable income, and address cost of living adjustments. Graves advocates for financial advisors to incorporate reverse mortgages into retirement planning to augment income, manage taxes and healthcare expenses, safeguard assets, and ultimately enhance retirees' financial security and quality of life.

Meet Jack and Diane

Picture Jack and Diane, a 65-year-old couple on the brink of retirement, seeking help from their financial advisor to navigate the uncertainties of their golden years. Facing the unpredictable ebb and flow of financial markets and unforeseen expenses, they are filled with questions: Will our savings endure amidst potential emergencies, long-term care needs, inflation, unknown future tax rates, another paralyzing pandemic, or an unprecedented crisis?

Amidst this maze of anxiety, their primary concern revolves around income and out flows. Will our pre-retirement financial assets and post-retirement streams of cash flow sustain our accustomed lifestyle? Should we claim Social Security benefits sooner for immediate financial support, or later to secure larger lifelong payouts?

This is where knowledgeable financial advisors can truly add value. They can alert seniors to another valuable asset they possess: their home equity, which may amount to six or even seven figures. A new realm of possibilities unfolds as homeowners contemplate how this asset could be leveraged specifically, whether the strategic integration of a modern reverse mortgage might provide solutions to possible retirement problems.

This article explores seven strategic reverse mortgage conversations aimed at enhancing and fortifying Social Security planning for a more secure retirement.

Understanding Reverse Mortgages: Key Features and Benefits

Reverse mortgages have evolved over decades as a solution for retirees outliving their savings. Today, around twenty countries including the United States, offer variations of equity release programs. In the U.S., with 87% of retirees owning their homes, reverse mortgages provide a viable option to tap into this valuable asset for financial security.

Reverse mortgages allow homeowners aged 62 and above to convert a portion of their home equity into accessible funds. Jumbo reverse mortgage programs also enable homeowners with higher home values to benefit, starting at age 55. Eligible properties include; most single-family homes, specific multi-unit properties, some condominiums, and certain manufactured homes, excluding cooperative apartments.

The most popular type of reverse mortgage is the federally insured Home Equity Conversion Mortgage (HECM). This article references HECMs specifically as they offer numerous benefits and protections to homeowners.The amount of available funds depends on factors like borrower age, home value, existing property balances, current interest rates, and chosen product terms. Repayment begins when the last borrower leaves the residence permanently; due to passing away, relocating, or selling the home. At this point, borrowers (if they relocate or sell) or heirs can repay the loan and accrued interest or sell the home to settle the debt, retaining any remaining equity. One key advantage of reverse mortgages is the absence of monthly mortgage payments freeing up cash flow for other expenses. Borrowers also enjoy flexibility in accessing funds through a lump sum, a line of credit, or a combination of both. Crucially, they retain ownership of their home and can continue living there as long as they meet program requirements such as paying property-related charges like taxes, insurance, and HOA fees.

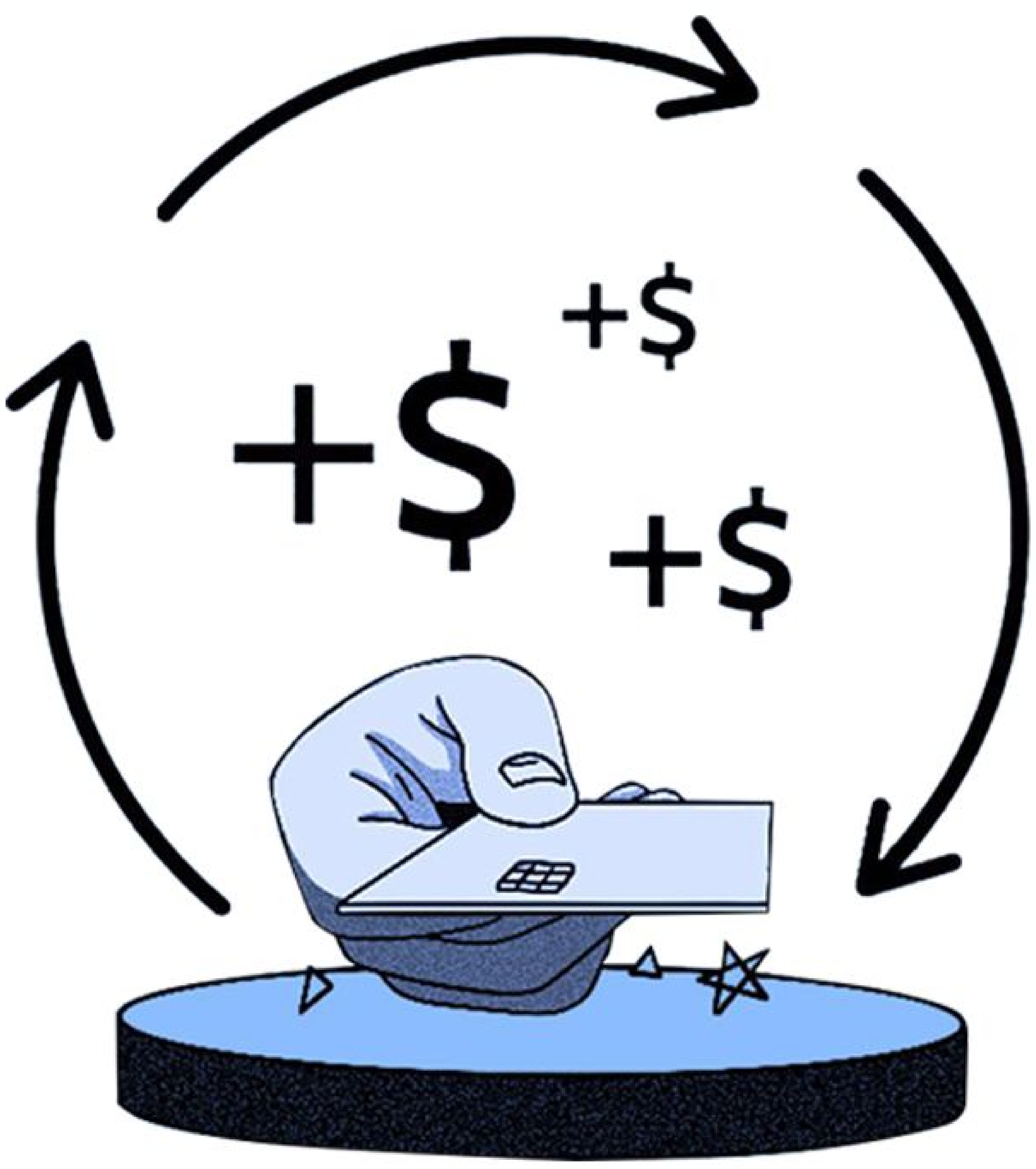
For a comprehensive understanding of reverse mortgages, explore additional resources at **www.itsjustamortgage.com**

Locking in a Growing Line of Credit

One of the unique features of a Home Equity Conversion Mortgage (HECM) is the Growing Line of Credit (LOC). This line of credit, with its embedded growth factor, allows increased borrowing capacity over time. Unlike traditional lines of credit, this LOC is immune to economic fluctuations and cannot be frozen, capped, canceled, or reduced, as long as at least one borrower occupies and maintains the home while paying the taxes and insurance premiums.

The chart below shows an initial reverse mortgage line of credit of $199,200 for a 65 -year-old in a $600,000 home. The Tenure column shows the amount of equal monthly payments that would be available as long as at least one borrower lives and continues to occupy the property as a principal residence.

The following two columns show term payment plans: equal monthly payments for a fixed time period of either 5 or 10 years. A borrower might use this cash flow for interim expenses until Social Security benefits reach their maximum with an age 70 claim.



With the background provided above, seniors and their advisors can see how reverse mortgages can bolster vital federal retirement programs—Social Security and Medicare. The flexibility and growth potential of the HECM LOC make it an invaluable tool in managing r etirement income and ensuring financial stability.

Age	LOC Amount	Tenure Payment	5 Year Term	10 Year Term
65	$199,200	$1,221	$3,893	$2,268
70	$277,175	$1,775	$5,416	$3,155
75	$385,672	$2,633	$7,537	$4,390
80	$536,639	$4,036	$10,487	$6,109
85	$746,701	$6,542	$14,592	$8,500
90	$1,038,990	$11,827	$20,304	
95	$1,445,692	$28,251		

$600,000 House | Expected Interest Rate: 6.18%

Seven Social Security Conversations Using Reverse Mortages

1. Supplementing Social Security

Social Security benefits, while valuable, may not always cover the full spectrum of the expenses that retirees encounter. In 2024, the average monthly payment is $1,907, under $25,000 a year. Even the largest current payout ($4,873 a month, under $60,000 a year) may be less than some retirees desire for retirement expenses. Reverse mortgages can provide the funds needed to enrich retirement in ways that range from funding home repairs and healthcare costs to fulfilling personal interests or travel aspirations.

2. Deferring Benefits while Replacing Income

Delaying Social Security until reaching age 70 results in a maximum benefit for retirees and surviving spouses. However, statistics reveal that fewer than 10% of individuals wait beyond the age of 66 to commence their benefits. The prevailing reason is often the immediate need for income from Social Security.

Instead of claiming early and locking in reduced Social Security benefits, retirees can leverage tax-free funds from a HECM. As illustrated above, Joan Smith might retire at age 65. Instead of filing for Social Security then, Joan uses her $600,000 home to get a 5-year term HECM, paying her nearly $50,000 a year, tax-free. Once the HECM payments end, Joan can apply for maximum Social Security benefits at age 70. A bridging -to-70 HECM might be supplemented by IRA withdrawals in a low tax bracket, further boosting cash flow after the paychecks cease.

In addition to this strategy, another common approach involves using a reverse mortgage to eliminate existing mortgage payments. According to recent surveys, most retirees today will be carrying some sort of house payment when they reach Social Security claiming age. Although they may wish to delay taking benefits, the money they need to cover their loan payments may prohibit this strategy. Using the reverse mortgage to eliminate their existing mortgage and payments allows them to use those liberated funds to supplement their income while deferring taking benefits.

3. Addressing Cost of Living Adjustments (COLA)

Social Security will usually issue a Cost of Living Adjustment (COLA) averaging around 2%. Some years it may be higher if the previous year's inflation was significant, while in other years, the COLA might be zero. However, the calculation used for the COLA . often does not reflect the actual increase in living expenses that retirees experience. For example, the Social Security Administration might calculate a 2% increase, but in reality, retirees might face an 8% rise in their personal living costs.

This discrepancy means that retirees often need more money in their checks than what the COLA provides. This is where a reverse mortgage can be incredibly useful. For instance, if your COLA increased your Social Security payment by $75 a month but you actually needed an additional $150 a month to cover your expenses, you could simply pull the extra $75 from your growing reverse mortgage line of credit. This strategy allows retirees to bridge the gap between the COLA and their actual cost of living increases, ensuring financial stability despite inflation.

4. Avoiding the “Tax Torpedo”

The term "Tax Torpedo" refers to the financial impact on seniors who may owe little or no tax on their Social Security benefits but choose to start receiving them early while simultaneously withdrawing from their traditional IRAs. This phenomenon also affects retirees with high taxable income. The more income derived from tax-deferred IRAs, the higher the potential tax liability on Social Security income, leading to marginal tax rates reported to be as high as 185% of the listed tax bracket.

Such results occur because the income tax on Social Security benefits is determined by "combined income," also called provisional income: the total of a taxpayer's adjusted gross income, tax-exempt interest, and half of Social Security benefits. Drawing down a pre-tax IRA increases provisional income, possibly causing more Social Security benefits to be taxed as well as increasing income tax from the IRA distributions.

One practical workaround is to use a HECM to supplement Social Security benefits. Cash flow from a HECM is tax-free, so it won't increase AGI and thus won't cause provisional income to rise. This approach minimizes the portion of Social Security benefits subject to income tax.

For individuals still grappling with high taxable income, the instinct may be to draw more from taxable IRAs, to cover income needs created by larger taxation. However, this approach inevitably leads to premature depletion of these funds. A more prudent approach would be to utilize the HECM line of credit to meet income needs, thereby safeguarding retirement assets and fortifying long-term financial security.

5. Spousal Support

The passing of a spouse can be emotionally devastating while bringing significant financial challenges. Losing the Social Security income of a deceased spouse may create a sudden and substantial gap in household finances, leaving the surviving partner vulnerable to budgetary strain. In such circumstances, cash from a reverse mortgage can help ensure that the surviving spouse can remain in the home and maintain his or her standard of living when the widow(er) receives one Social Security check instead of two.

6. Managing Medicare

Savvy use of a HECM not only pairs well with Social Security but also can play a significant role in stabilizing Medicare costs. Medicare beneficiaries with higher incomes, including those receiving Social Security benefits, may be subject to Income-Related Monthly Adjustment Amount (IRMAA) premiums for Part B (medical care) and Part D (prescription drugs).

For Part B alone, in 2024 IRMAA premiums can boost the standard monthly amount from $174.70 a month ($2,096 a year) to as high as $594 a month ($7,128 a year) for the same health insurance coverage. High-income married couples on Medicare could owe double that amount.

Again, by lowering their taxable income through the judicious use of a reverse mortgage rather than taxable IRA withdrawals, retirees might reduce or even avoid IRMAA surcharges, leading to substantial savings on healthcare costs. This strategic maneuver not only preserves more of retirees' retirement income but also ensures that they can access the healthcare services they need without undue financial burden. In this way, reverse mortgages can offer retirees a powerful tool for navigating the complexities of taxation and healthcare expenses in retirement, ultimately enhancing their overall financial well-being and quality of life.

7. Enhancing Emergency Funds

Retirees often face unexpected expenses such as medical emergencies, home repairs, or other unforeseen costs. Having a readily accessible source of funds is crucial in such situations. A reverse mortgage, particularly a Home Equity Conversion Mortgage (HECM), offers a practical solution by providing a reliable and growing line of credit that can serve as an emergency fund, tying directly into strategic Social Security planning.

Unlike traditional emergency funds, which can be depleted quickly, the HECM line of credit grows over time, ensuring that retirees have an increasing amount available for emergencies. This feature provides a robust financial safety net that adapts to their needs as they age, allowing them to manage unexpected expenses without prematurely claiming Social Security benefits. For example if a retiree needs $5,000 for an unexpected home repair, they can draw from their HECM line of credit without depleting their savings or impacting their monthly budget, thereby preserving their Social Security strategy.

Additionally, since the funds from a HECM are tax-free, using the line of credit for emergencies does not increase taxable income or affect other benefits. This strategic use of a reverse mortgage gives retirees peace of mind, knowing they have a dependable and growing source of funds to handle life's unexpected challenges. By integrating a HECM into their financial plan, retirees can better manage their Social Security benefits and maintain financial stability in the face of unforeseen expenses.

The Strategic Advantage of Reverse Mortgages

As these examples illustrate, reverse mortgages offer retirees versatile solutions to supplement income, bridge financial gaps, mitigate taxation as well as healthcare expenses, and safeguard retirement assets. Additionally, using a HECM can help to manage housing wealth while optimizing overall financial confidence.

By incorporating reverse mortgages into retirement planning conversations, financial advisors can provide their clients with new avenues for maximizing retirement security. As retirees navigate the complexities of financial planning, the strategic use of reverse mortgages offers a pathway to a more secure and fulfilling post-career life.

Action Plan

- As clients approach retirement and begin to show increased interest in Social Security as well as Medicare, introduce the idea of home equity as an asset to help finance a comfortable retirement.
- Explain the basic principles of reverse mortgages and provide specific details on federally insured HECMs. Have them view
- For clients with substantial net equity in their primary residence, develop some projections as to how much they might receive with various forms of HECMs, at different ages.
- Reveal how much income they might be able to expect in retirement from conventional sources, including Social Security, after-tax.
- Show how untaxed income from a HECM could augment retirement cash flow
- Develop specific plans, where appropriate, for the circumstances described above: delaying Social Security until 70, avoiding the tax torpedo, providing for widow(er)'s needs, and avoiding IRMAA premiums.

Advisor Resources

- Subscribe to Don's Weekly 60 Second Email : www.HousingWealthInsights.com
- Request a Customized 4-Column Illustration: www.HousingWealthPro.com
- View Don's Consumer Masterclass:www.HousingWealthMasterClass.com
- My Personal Social Security Guru: Heather Schreiber heather@hlsretirementconsulting.com | https://hlsretirementconsulting.com

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Is the president and founder of the Housing Wealth Institute and an Adjunct Instructor of Retirement Income at The American College of Financial Services. With 25 years of experience in the reverse mortgage industry, Don has educated over 30,000 financial professionals and served nearly 3,000 clients. He is an accomplished author of three books on reverse mortgages and retirement strategies, and a sought-after speaker. Don is dedicated to empowering consumers and financial professionals on the strategic benefits of reverse mortgages for enhanced retirement security.

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