Reverse Mortgages with Wade Pfau
Feb. 12, 2020

Hosted by Tom Dickson
Financial Experts Network

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To Get a CE Credit for Today's Session

Today's program is eligible for 1 CE credit for professionals with:
CFP, CLU, RICP, and ChFC.

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A Financial Experts Membership is Best if you….

- Value **live webinars** from best-in-class experts
  - 86% of our attendees rate our webinars EXCELLENT

- Education on a **range of topics** such as: college planning, investments, retirement income, tax planning, Social Security, Medicare, LTCi, HSAs, divorce planning, annuities and MORE.

- Will use tools like webinar transcript and small case study groups

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The EXPERT in Specialized Area

National Figures and **Undiscovered EXPERTS**

The **"Dean"** of Financial Planning

Wade Pfau
Annuity Expert

Kurt Czarnowski
Mr. Social Security

Aaron Zolbrod
Medicare Specialist

The #1 Reason our webinars have a following:

90% of advisors learned something that will help them better serve their client

Financial Planner Feedback

Dear Tom:
Today’s Fafsa webinar plus all the prior ones you have run that I have attended have been excellent. I've been a fee-only NAPFA member for more than 20 years, and yours have been the most useful ones I have ever attended.

Thank you for all that you are doing for your members!

Dorothy Cole
Merrimack NH

Tom:
Great value. Absolutely unbelievable!
Paul Riskus
CFP®, CTFA®, CLU®, RICP®
San Antonio, Texas

Tom:
Your offer a lot of value for $9 a month. Your speakers are of the highest quality.
Kevin H.
Ohio

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Access to **all live** webinars.		Yes
Access to **study group sessions.**		Yes
Ethics CE for CFP and American College designations.		2 Classes
Automated CE Reporting to CFP Board		Yes
Certificates for self-reporting		Yes
Replays of **all webinars**		Yes
Edited Webinar Transcripts with must-know facts		Yes
Financial Expert Tip sheets; ***12 Fafsa Tips.***		Yes
Submit questions, **in advance**, for experts to answer.		Yes
Community Forum		Yes
Submit Case Studies to be considered as part of webinars.		Yes
1-click webinar registration		Yes
Opt-in control		Yes

March 19
Sept. 9

Learn more about Member's program and 2020 Webinars

Info Session: Friday, Feb. 21 11:00 ET

Register Here

BIG Thanks to…

Joe Damo, Reverse Mortgage Specialist, AAG

Cell: 513-939-6034

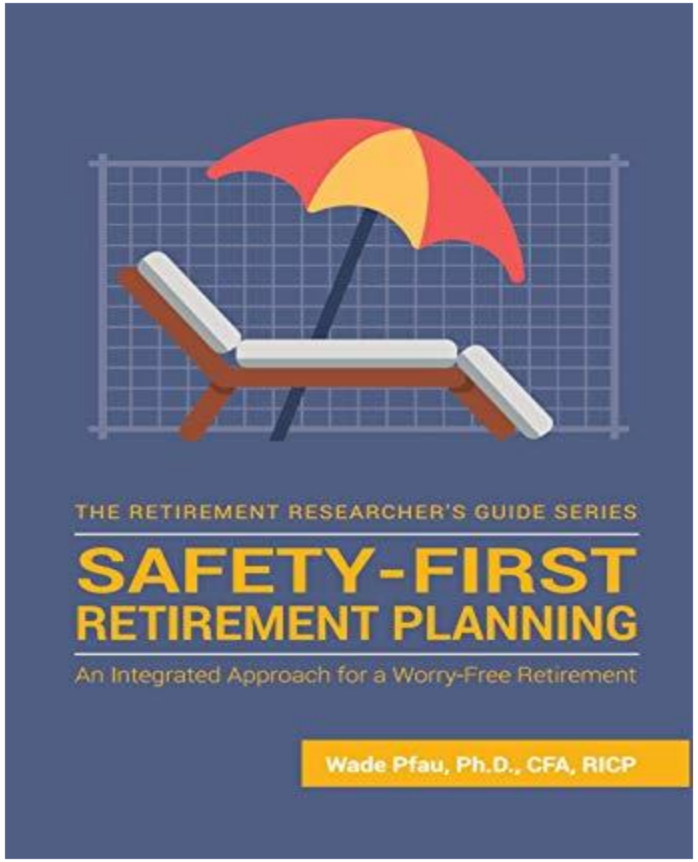
Email: jdamo@aag.com

Caitlin Taylor, Account Manager, MoneyGuidePro

Wade Pfau's New Book: See Amazon.com

Dr. Wade Pfau brings a level of honesty, intellectual rigor and impartiality seldom witnessed in financial product analysis.

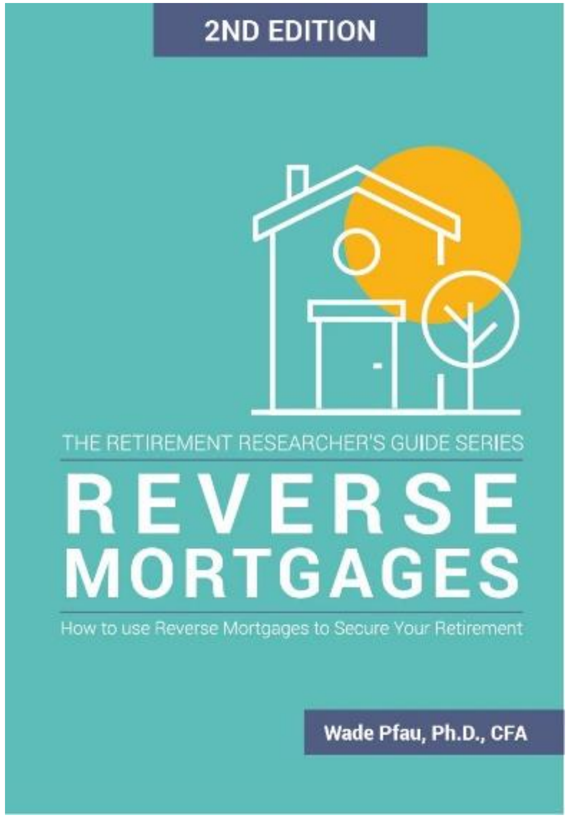
WADE A. DOKKEN, President, WealthVest



Retirement Researcher

RETIREMENT BEGINS WITH A PLAN™

How to use Reverse Mortgages to Secure Your Retirement



Presented by:

Wade Pfau, Ph.D., CFA, RICP

RICP Curriculum Director

The American College for Financial Services & RetirementResearcher.com

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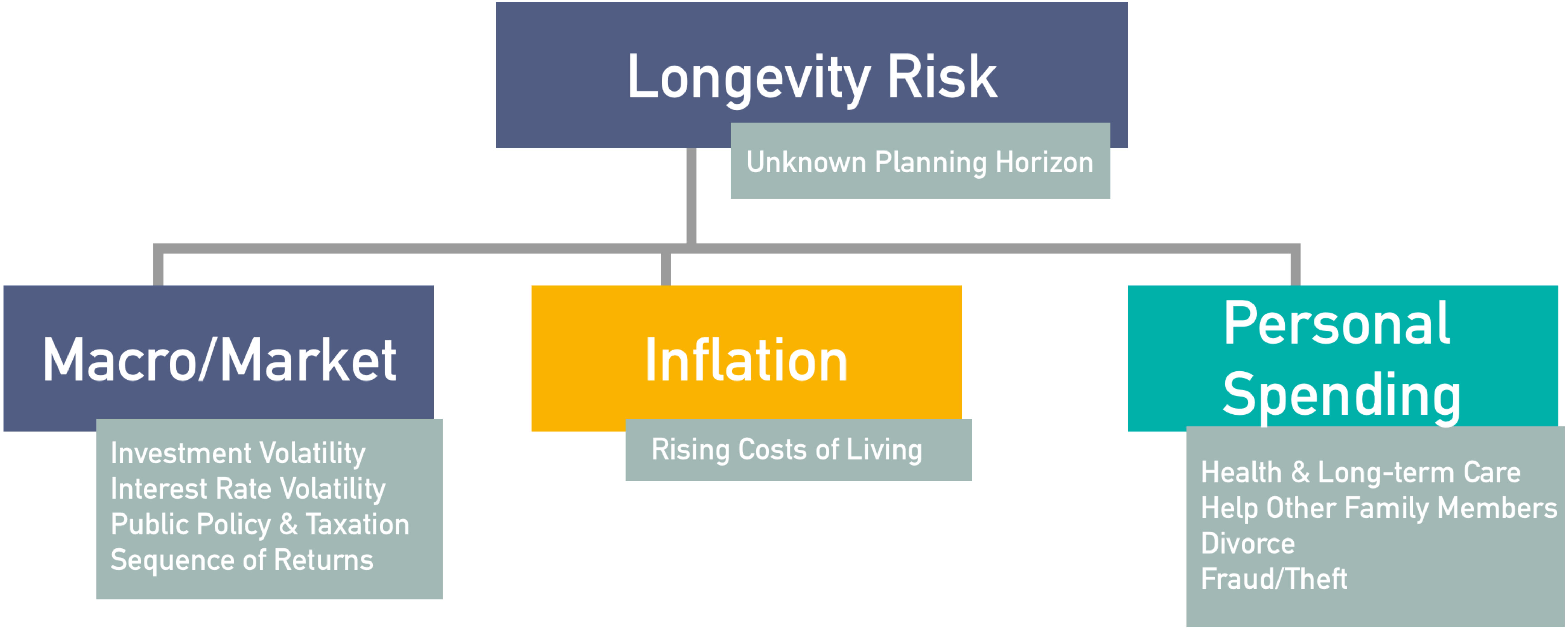
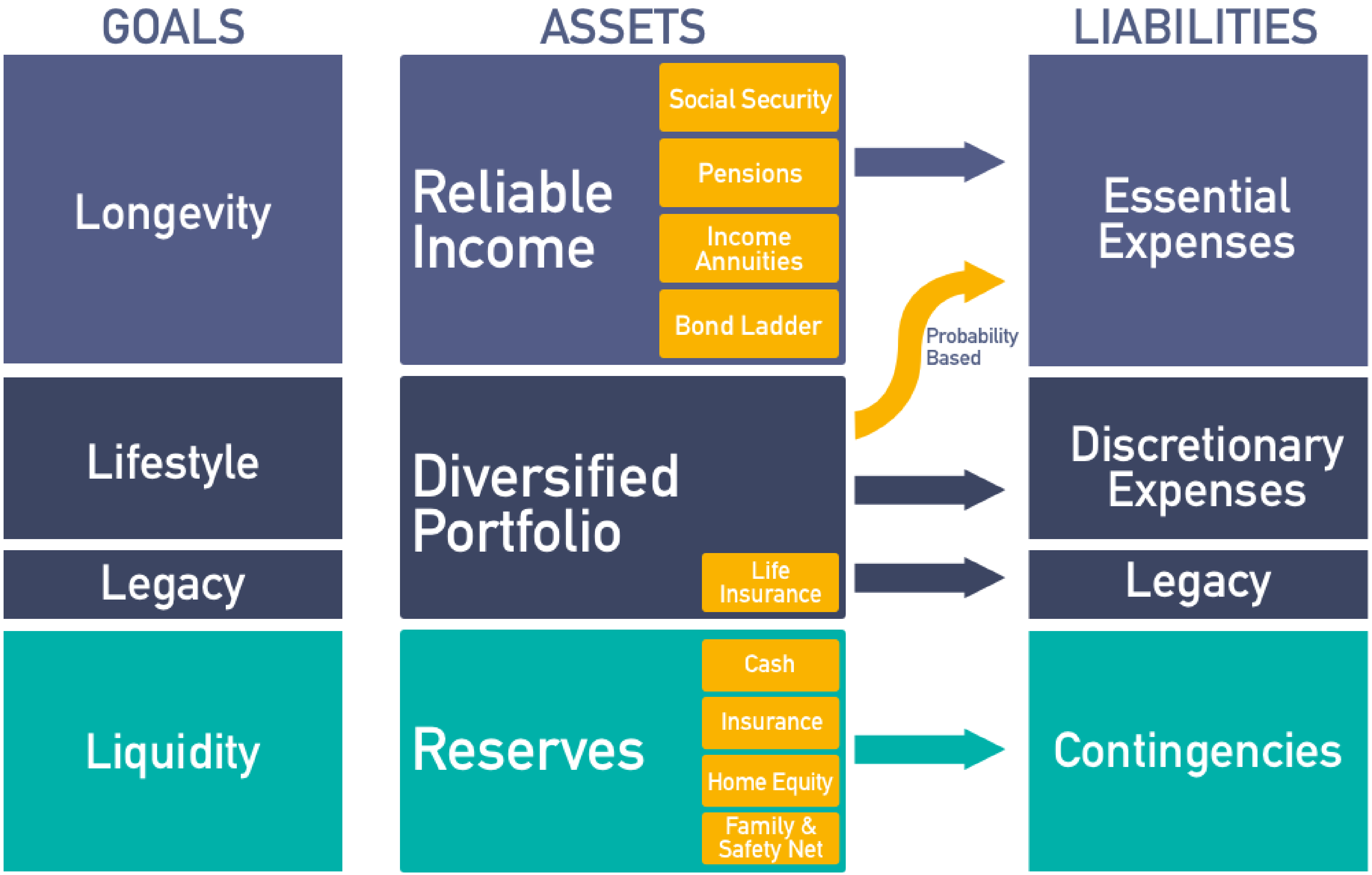
Key Retirement Risks



Retirement Optimization Plan

Retirement Researcher



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Managing Volatility in Retirement

- **Spend Conservatively**

  (tenure payment, refinance mortgage, Social Security delay bridge)

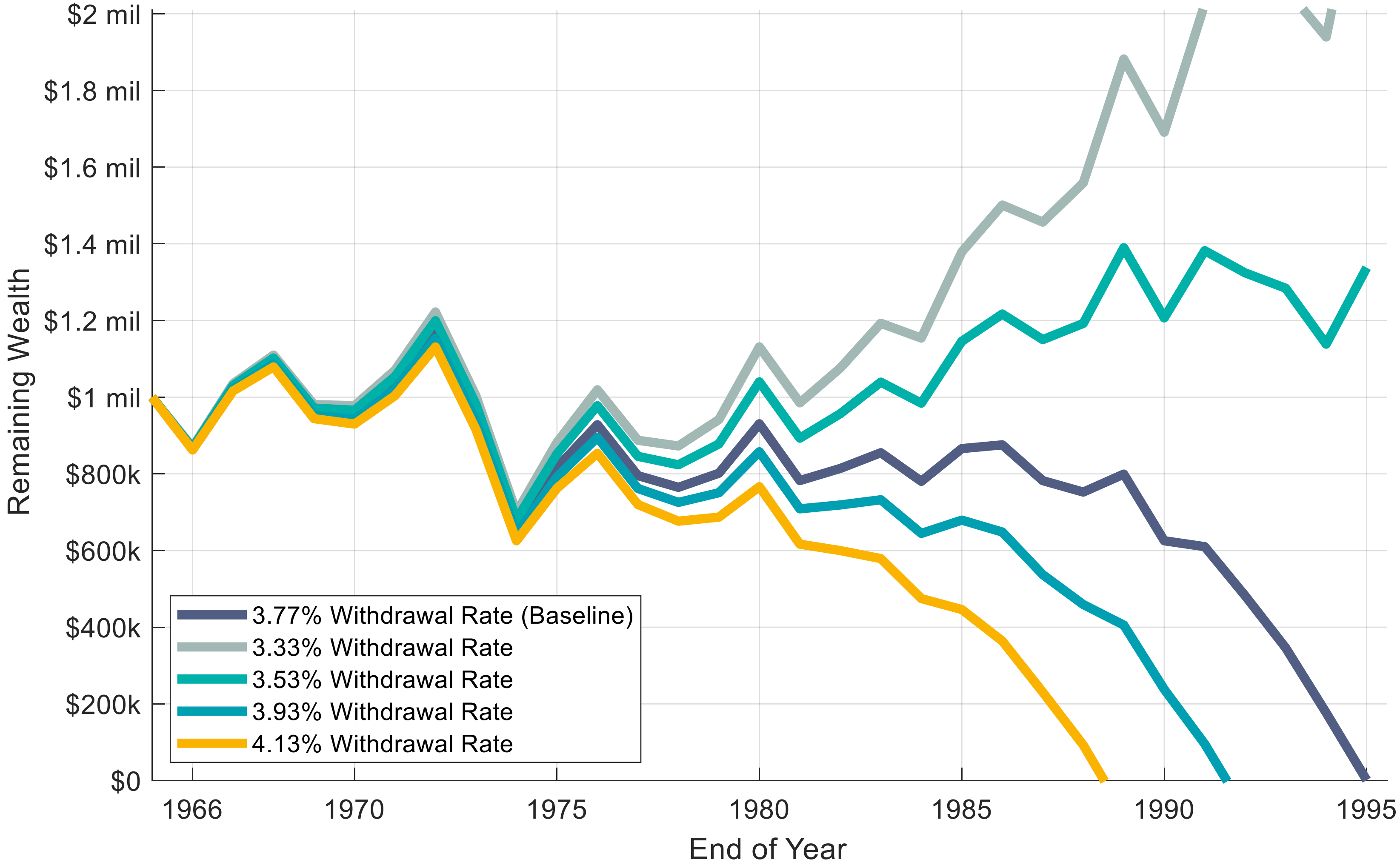
- **Spending Flexibility**

- **Reduce Volatility**

- **Buffer Assets – Avoid Selling at Losses**

  (coordinated spending strategies)

Spend Conservatively



Sequence Risk and the Portfolio Impact of Spending Levels
Inflation-Adjusted Spending Defined as a Percentage of Retirement Date Assets, No Fees
Using SBBI Data, 1966-1995, S&P 500

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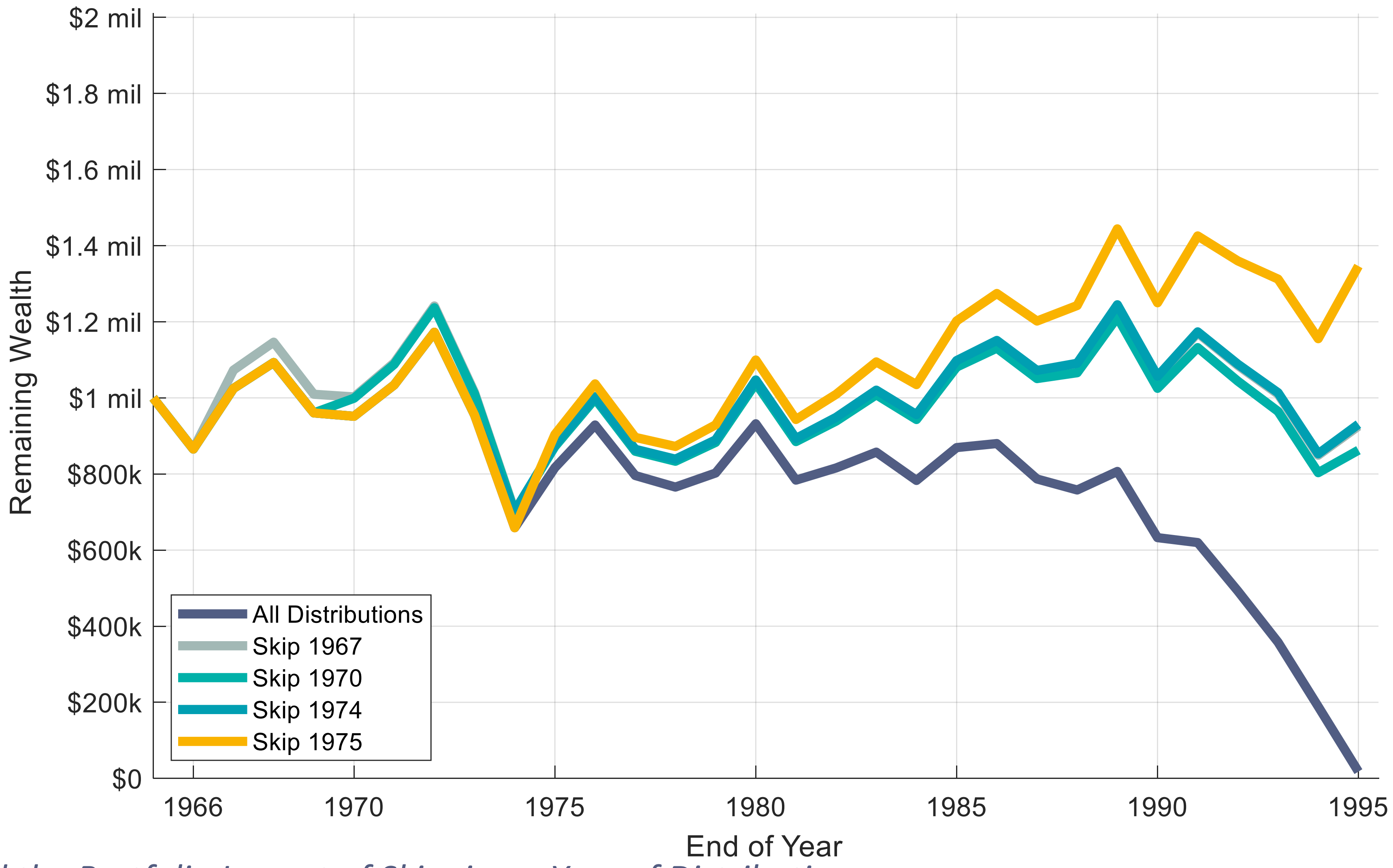
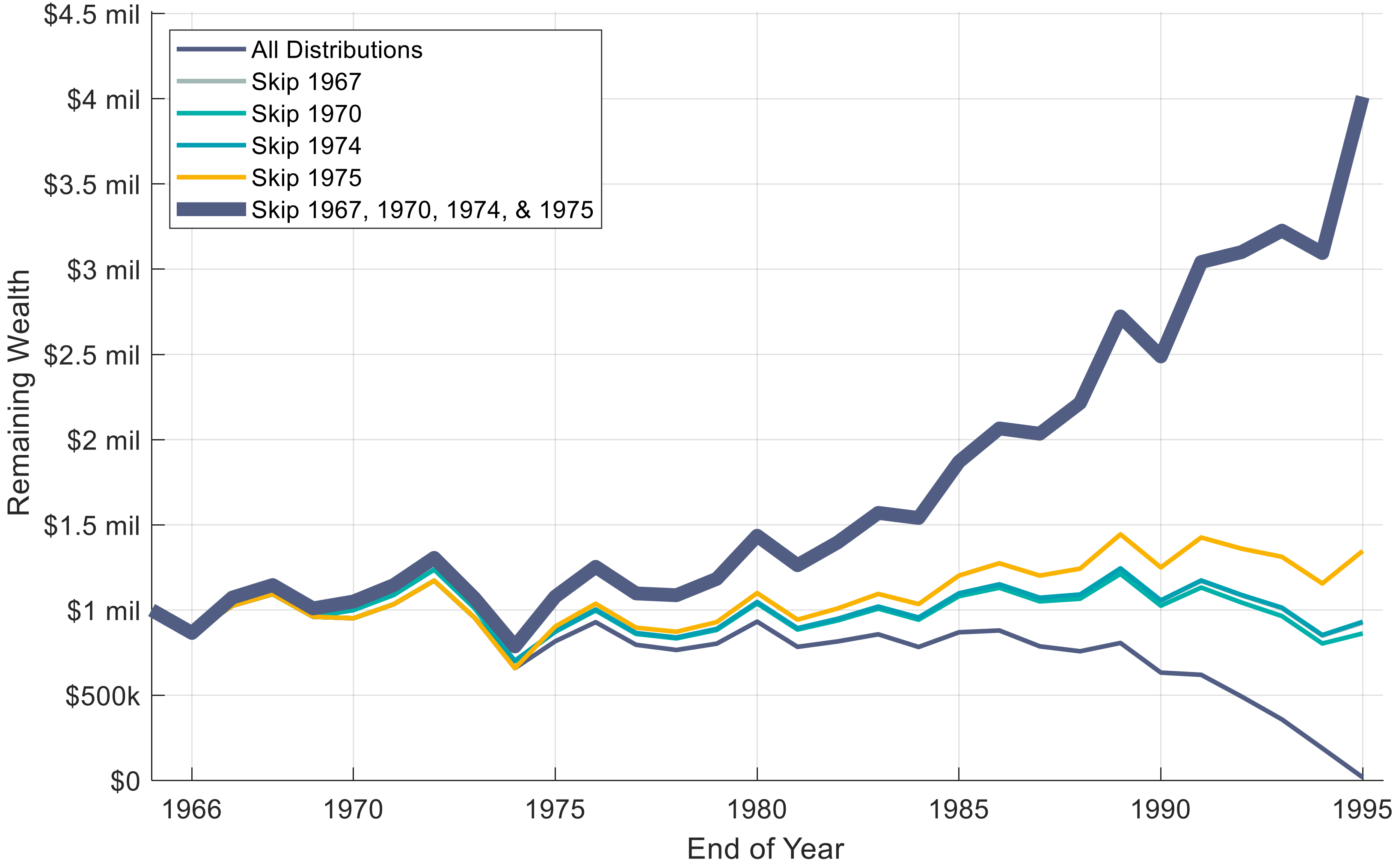
Buffer Asset Concept



Sequence Risk and the Portfolio Impact of Skipping a Year of Distributions
Using SBBI Data, 1966-1995, S&P 500

Buffer Assets



Sequence Risk and the Portfolio Impact of Skipping a Year of Distributions Using SBBI Data, 1966-1995, S&P 500

Uses for Reverse Mortgages

The Spectrum of Potential Reverse Mortgage Uses

Portfolio/Debt Coordination for Housing	**Refinance an Existing Mortgage** **Transition from Traditional Mortgage to Reverse Mortgage** **Fund Home Renovations to Allow for Aging in Place** **HECM for Purchase for New Home**
Portfolio Coordination for Retirement Spending	**Spend Home Equity First to Leverage Portfolio Upside Potential** **Coordinate HECM Spending to Mitigate Sequence Risk** **Use Tenure Payments to Reduce Portfolio Withdrawals**
Funding Source for Retirement Efficiency Improvements	**Tenure Payments as Annuity Alternative** **Social Security Delay Bridge** **Tax Bracket Management & Taxes for Roth Conversions** **Premiums for Existing Long-Term Care Insurance Policies**
Preserve Credit as Insurance Policy	**Support Retirement Spending After Portfolio Depletion** **Protective Hedge for Home Value** **Provides Contingency Fund for Spending Shocks** **(In home care, health expenses, divorce settlement)**

Understanding How Reverse Mortgages Work

Addressing the Negative Image

Misconceptions	Now Addressed	Remaining Issues
Home Title Family Misunderstandings	Desperate Borrowers & Foreclosure Risk Non-borrowing Spouses Taxpayer Risk Quickly Deplete Home Equity for Questionable Reasons	Stigma About Using Debt Direct-to-consumer TV commercials

Eligibility Requirements for HECMs

- Borrowers: 62 and older
- Equity in the home
- Financial resources to cover property taxes, homeowner's insurance, and home maintenance
- Counseling session with FHA-approved counselor
- FHA Home Appraisal
- Primary residency
- FHA Lending limit: $765,600

Essential Jargon

1. Principal Limit / Principal Limit Factor (PLF)

2. Expected Rate

3. Effective Rate

Reverse Mortgage Interest Rates (After October 2, 2017)

Type	Components	Applies to:
Expected Rate	10-year LIBOR Swap Rate + Lender’s Margin	Initial Principal Limit Factor Set-Asides for Servicing Costs in Old Mortgages
Effective Rate	1-month LIBOR Rate + Lender's Margin + Mortgage Insurance Premium (0.5%)	Ongoing Principal Limit Growth Rate Loan Balance Growth Rate Line of Credit Growth Rate Post-2014 Set Asides for Financially Strained

Expected and Effective Rates: Example

One-month LIBOR rate: 1.25%

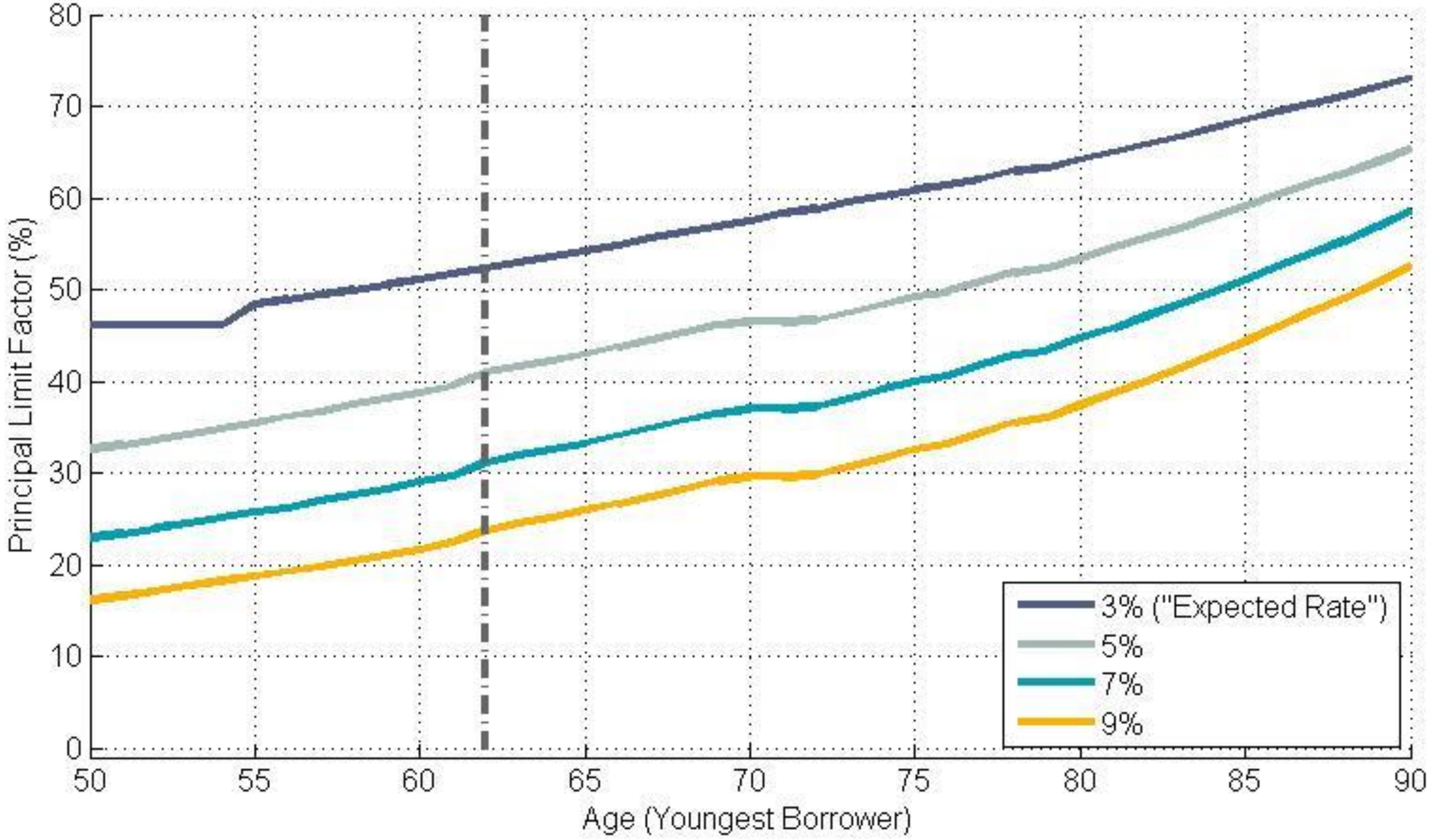
10-year LIBOR swap rate: 2.25%

Lenders margin: 2.75%

Expected Rate = 2.25% + 2.75% = **5%**

Effective Rate: = 1.25% + 2.75% + 0.5% = **4.5%**

Initial Principal Limit
(Principal Limit Factor)



Expected rate = 10-year Libor Swap Rate + Lender's Margin

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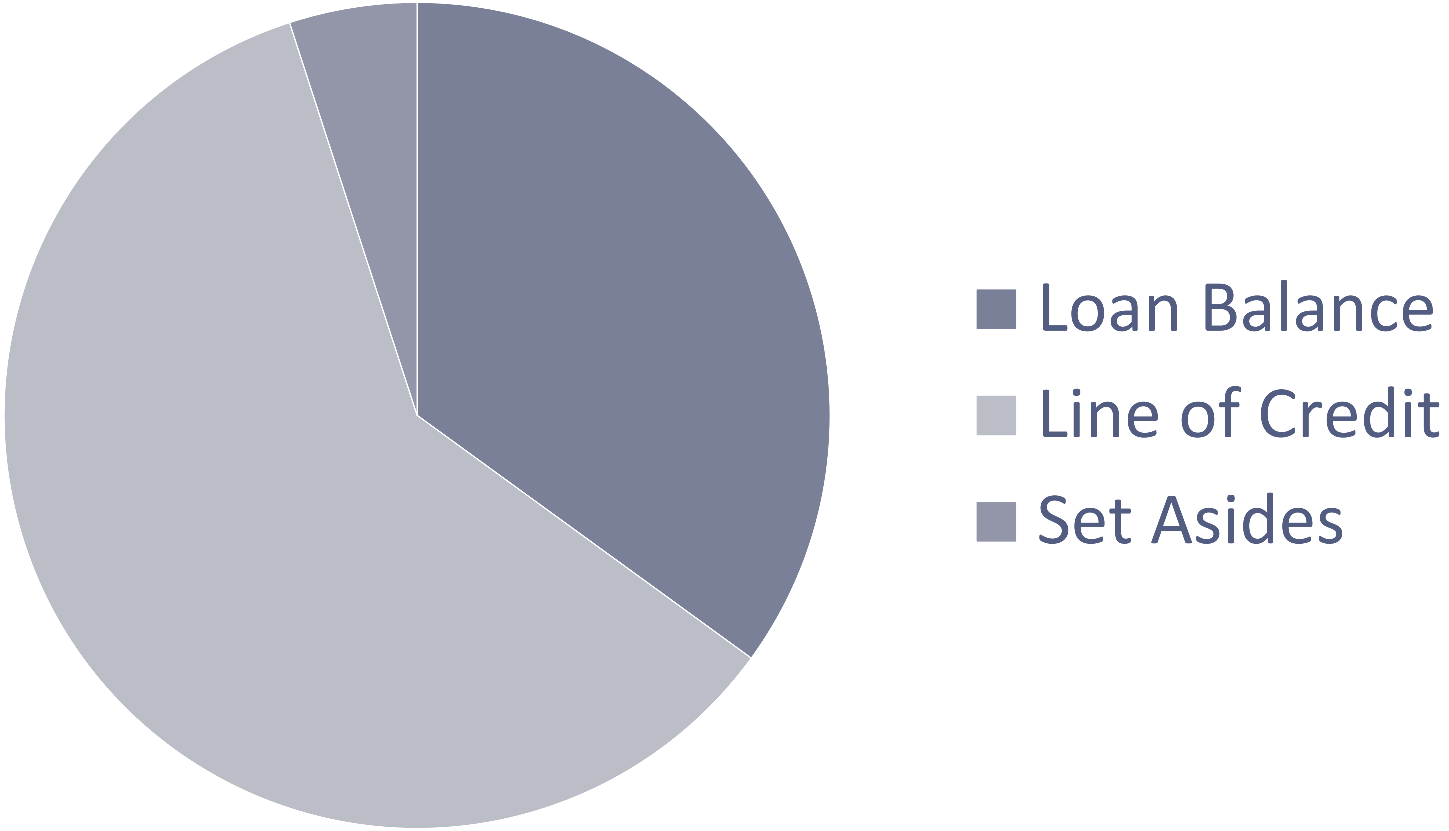
Understanding Line of Credit Growth

Principal Limit = Loan Balance + Available Line of Credit + Set-Asides



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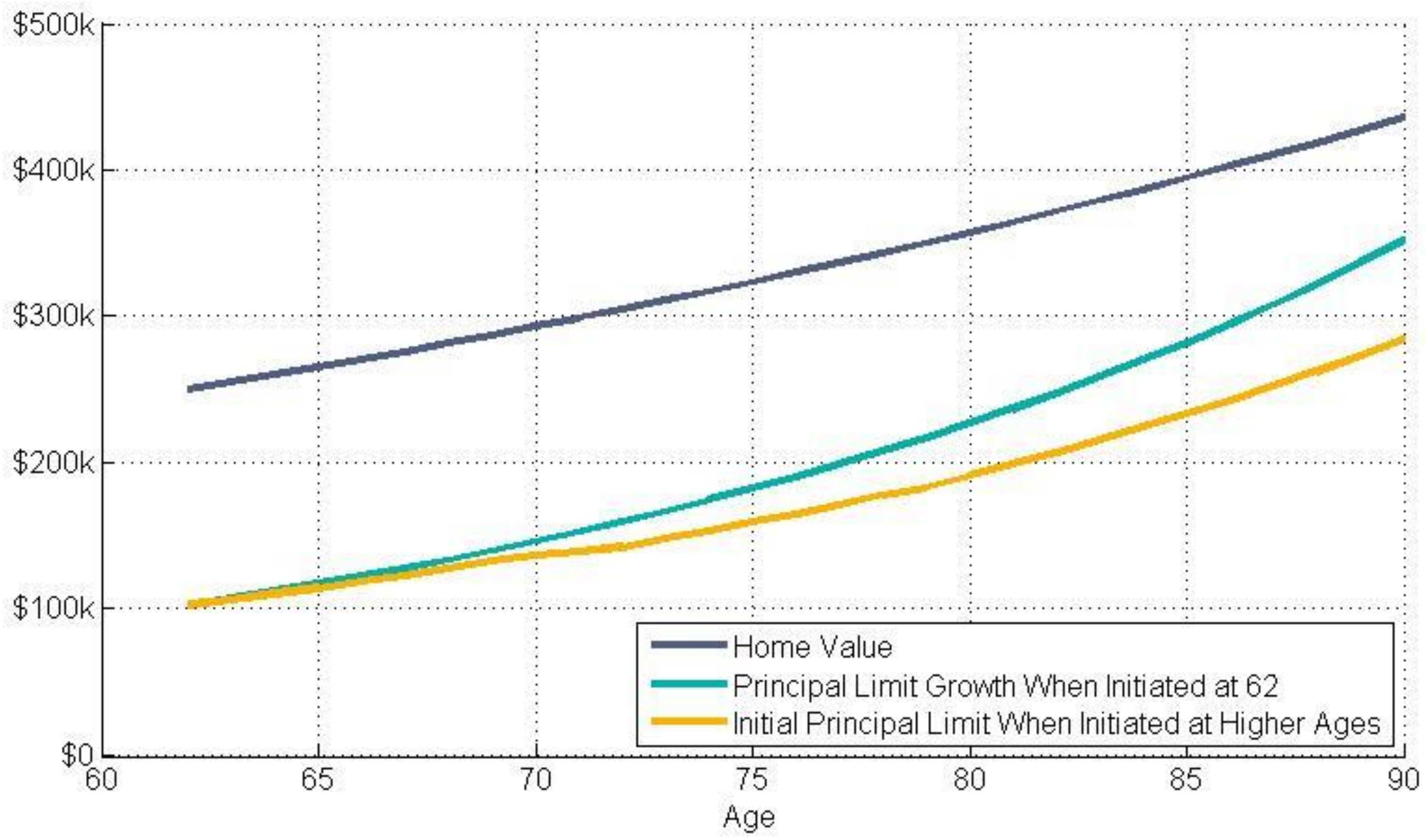
Understanding Line of Credit Growth

Comparing Principal Limits Based on When the Reverse Mortgage Opens



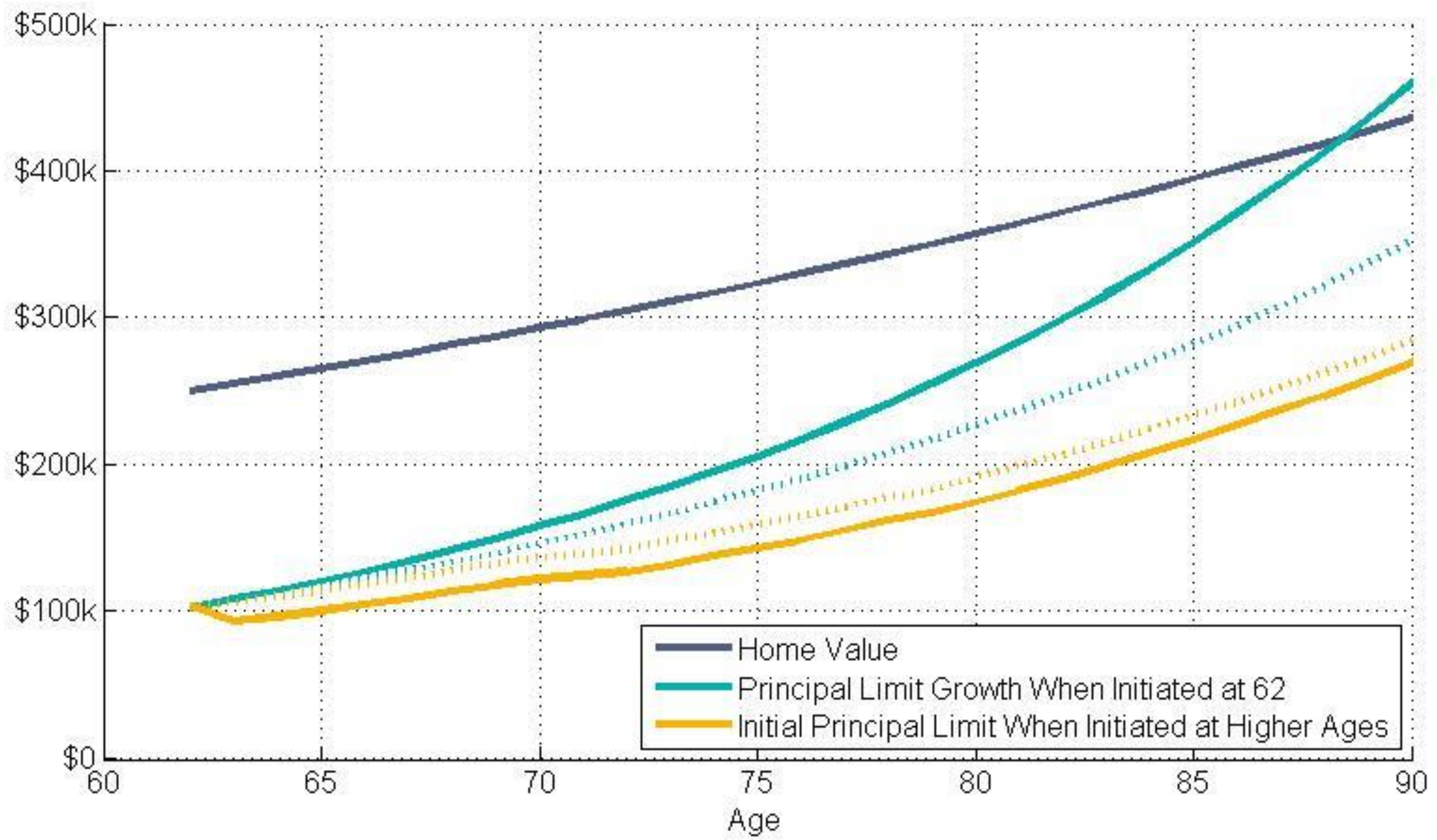
10-Year LIBOR Swap Rate: 2.25%

Lender's Margin: 2.75%

One-month LIBOR rate: 1.25%

Understanding Line of Credit Growth

Comparing Principal Limits Based on When the Reverse Mortgage Opens



Impact of 1% interest rate increase later in the first year

HECMs and the Interest Rate Environment

Low interest rates *favor* HECMs:

- Lower expected rate = larger initial principal limit
- Subsequent principal limit growth is lower, unless interest rates subsequently rise and accelerate growth

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HECM Spending Options

1. Lump-sum payment
2. Tenure payment
3. Term payment
4. Line of Credit

5. Modified tenure or modified term payment

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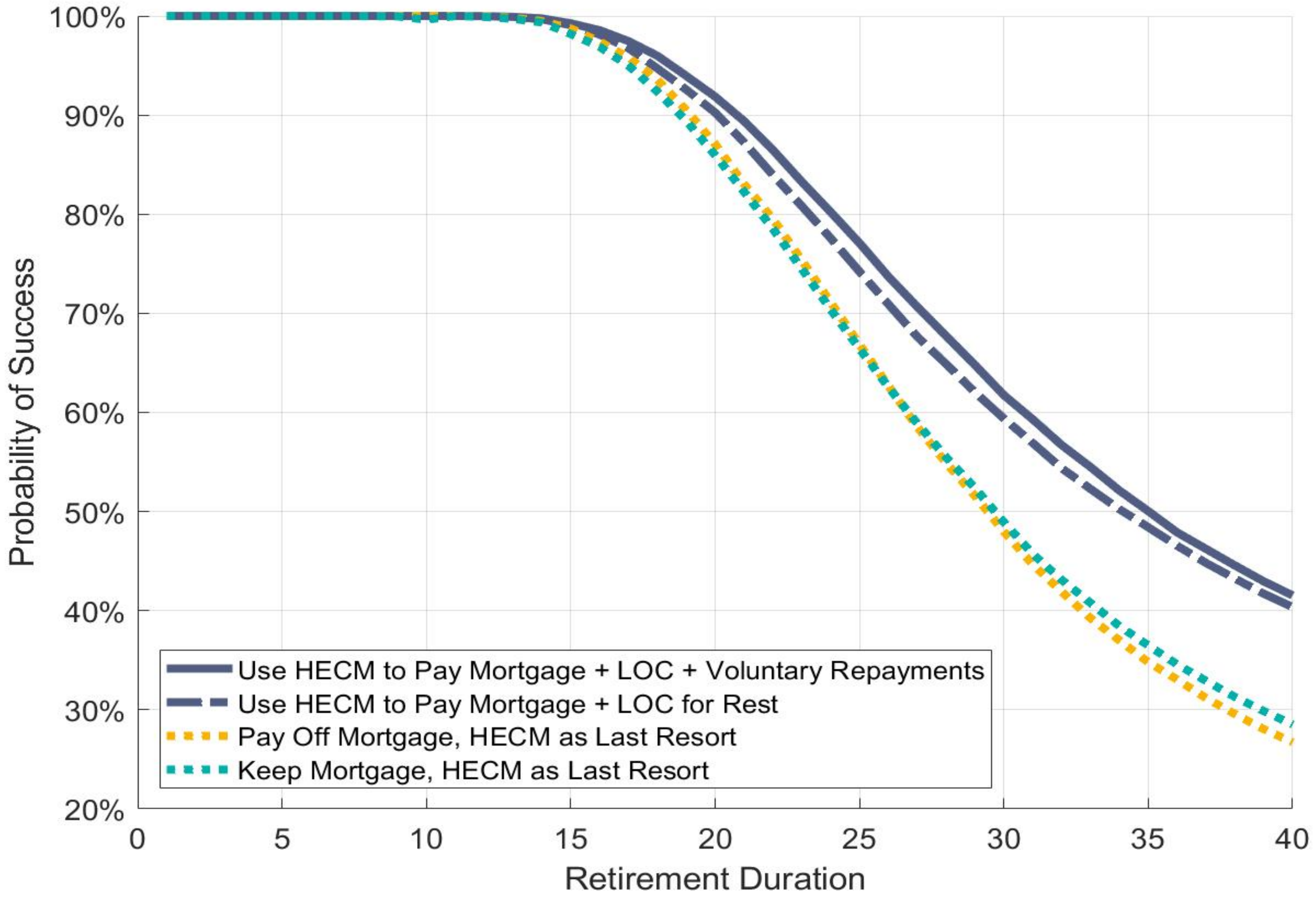
Traditional Mortgage

Reverse Mortgage

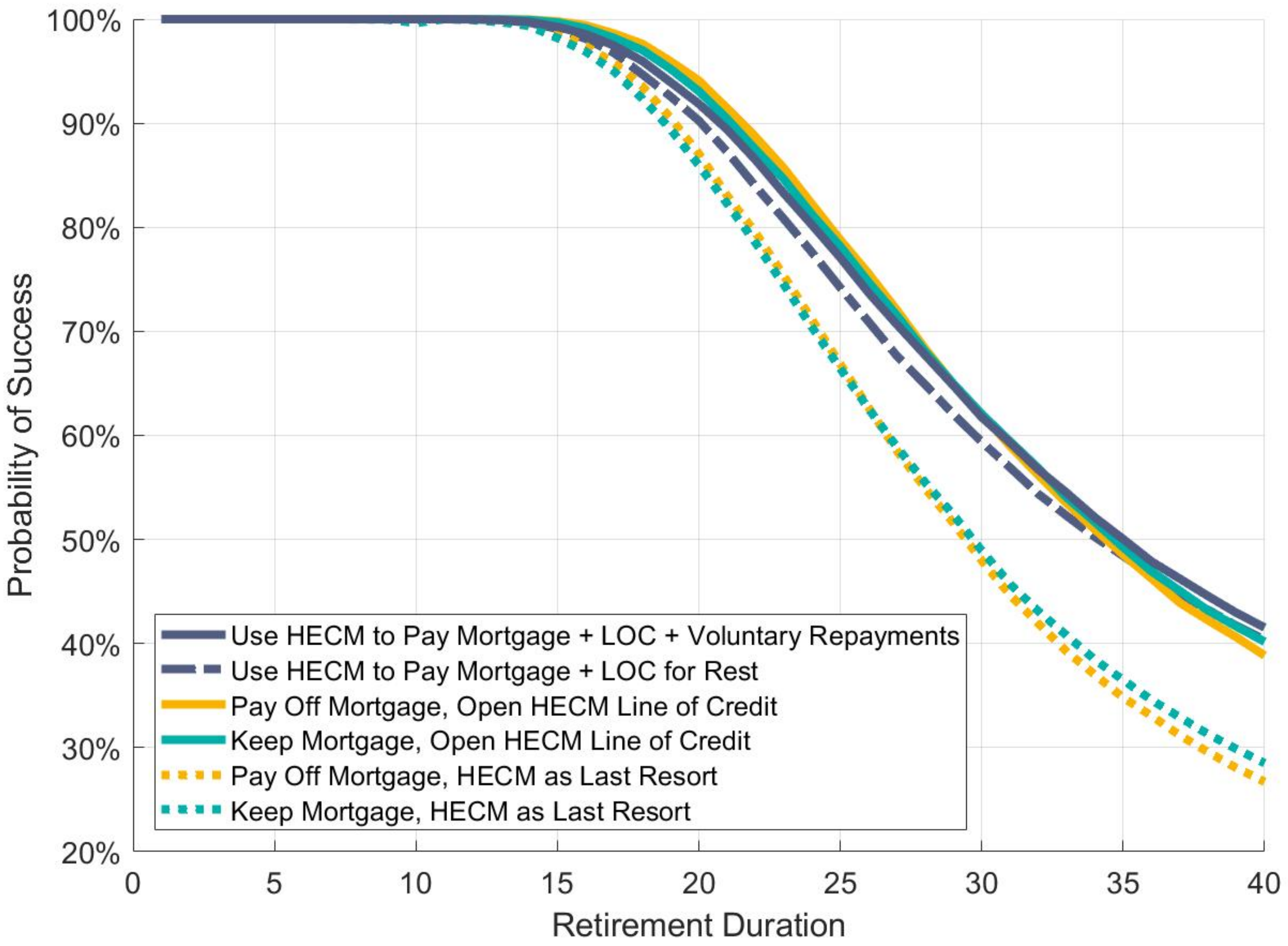
Example for Carrying Mortgage into Retirement

- 65-year old couple enters retirement
- Twenty years ago, purchased a $300,000 home with a 20% down payment, using a 7.5% fixed 30-year mortgage for the rest
- Five years ago, refinanced into a 3.5% fixed 15-year mortgage
- Annual mortgage payments = $15,574
- 10 years left on mortgage; Remaining mortgage balance = $129,526.
- Home value grew at 3% for past 20 years. It is worth $541,833 today.
- The principal limit is 45.9% of $541,833, or $248,701
- Upfront costs: $6,000 + $10,837 + $2,500 = $19,337 financed in loan
- Remaining Line of Credit: $99,839

Probability of Success for a 4% Post-Tax & Mortgage Initial Withdrawal Rate, $1 million portfolio, $541,833 home value, 25% Marginal Tax Rate



Probability of Success for a 4% Post-Tax Initial Withdrawal Rate
$1 million portfolio, $541,833 home value, 25% Marginal Tax Rate



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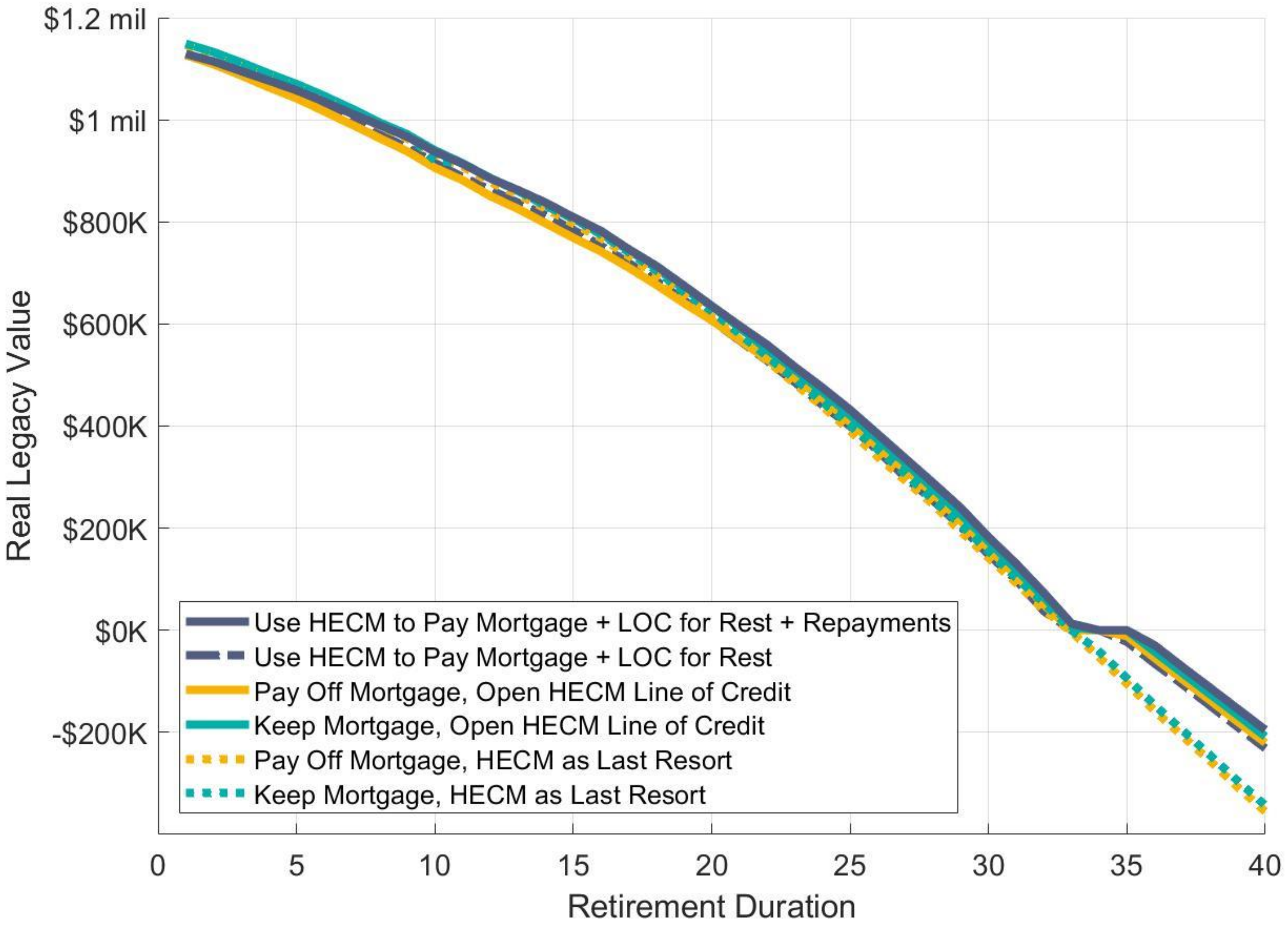
Median Legacy Wealth for a 4% Post-Tax Initial Withdrawal Rate
$1 million portfolio, $541,833 home value, 25% Marginal Tax Rate



Shifting from Traditional Mortgage to Reverse Mortgage:

- Reduced withdrawal rate -> reduced sequence risk -> increased probability of success

- Mortgage leverages the portfolio – legacy will be larger if portfolio growth rate exceeds loan growth rate

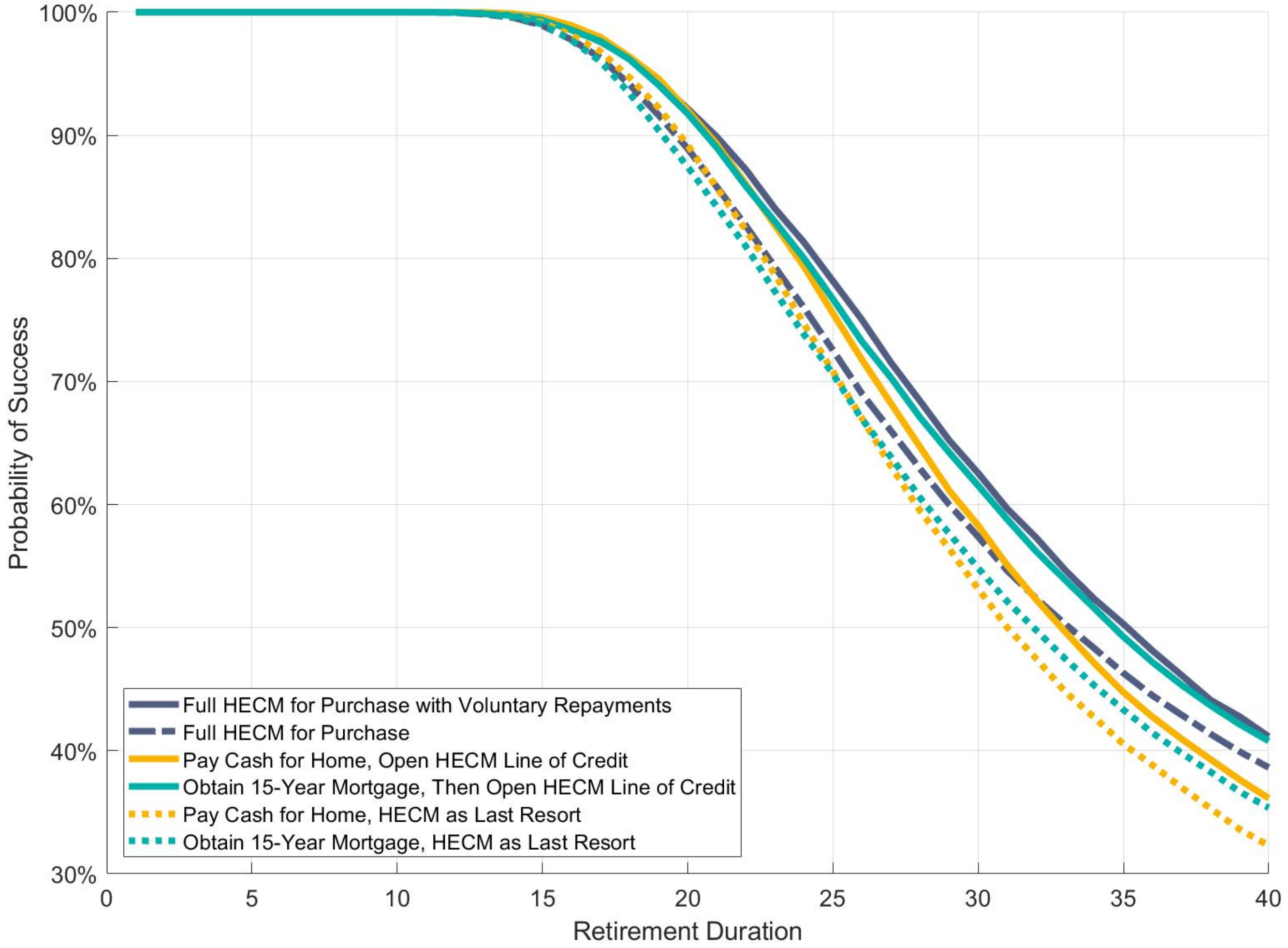
- High initial HECM borrowing reduces the overall percentage of the initial home value that can be accessed through reverse mortgage (voluntary repayment helps against this advantage for Line of Credit uses)

HECM for Purchase

Example for HECM for Purchase

- 65-year old couple enters retirement with $1.4 million in IRA
- Seeking to purchase a $300,000 home
- Traditional mortgage:
  - A 3.5% fixed 15-year mortgage with a 20% down payment
  - Annual mortgage payments = $20,838
- HECM for Purchase:
  - The principal limit is 45.9% of $300,00, or $137,700; Portfolio to finance the rest
  - Upfront costs: $5,000 + $6,000 + $2,500 = $13,500 paid from portfolio
  - No Remaining Line of Credit

Probability of Success for a 4% Post-Tax Initial Withdrawal Rate
$1 million portfolio, $541,833 home value, 25% Marginal Tax Rate



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HECM for Purchase:

- Reduced withdrawal rate -> reduced sequence risk -> increased probability of success
- HECM for Purchase leverages the portfolio – legacy will be larger if portfolio growth exceeds loan growth
- High initial HECM borrowing reduces the overall percentage of the initial home value that can be accessed through reverse mortgage (voluntary repayment helps)

Portfolio Coordination for Retirement Spending

An idea whose time had come?

"Reversing the Conventional Wisdom: Using Home Equity to Supplement Retirement Income"

Barry Sacks and Steven Sacks

Journal of Financial Planning, February 2012

"Standby Reverse Mortgages a Risk Management Tool for Retirement Distributions"

John Salter, Shaun Pfeiffer, and Harold Evensky

Journal of Financial Planning, August 2012

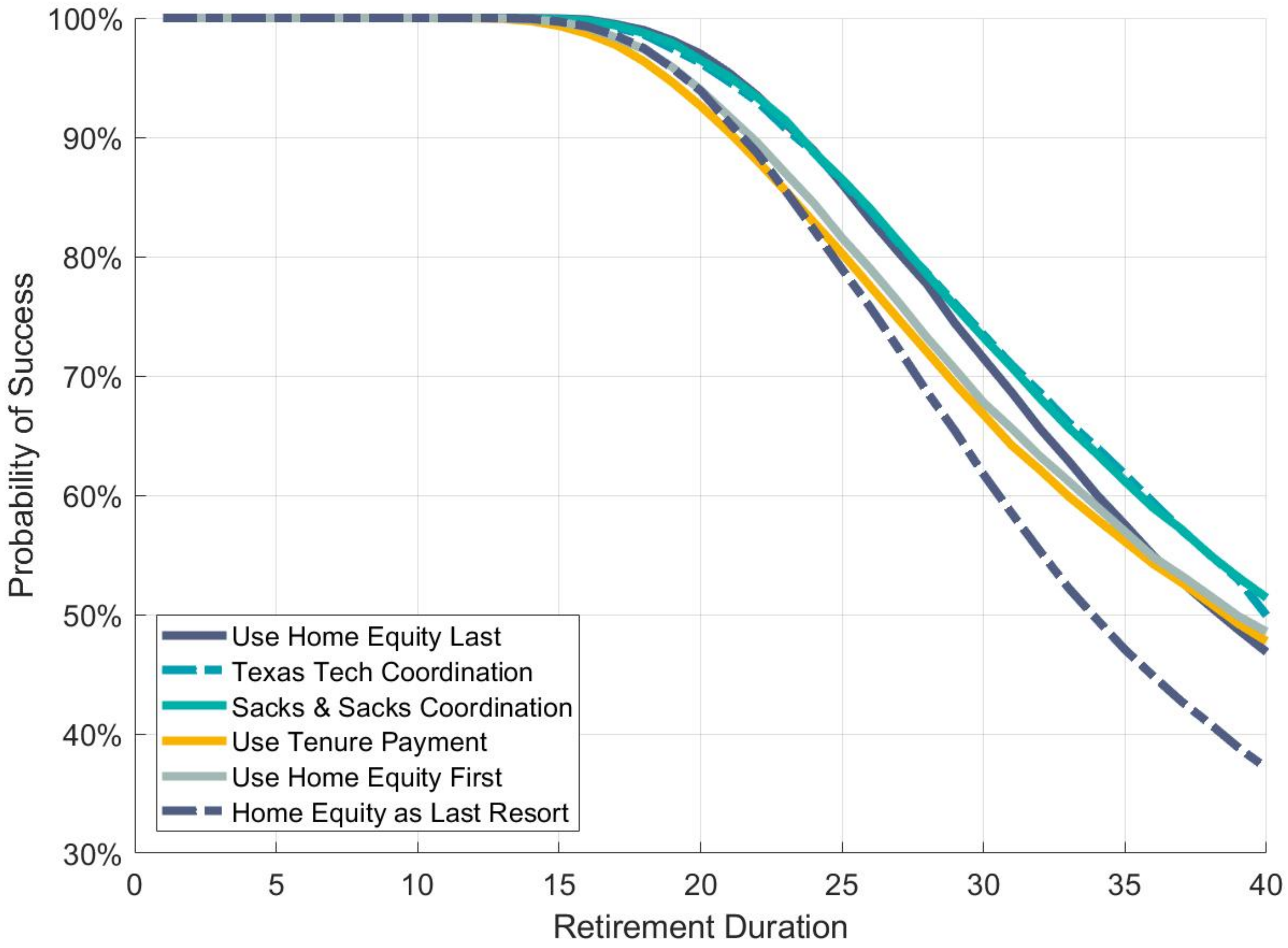
Thesis: Strategic use of a reverse mortgage standby line of credit can create retirement income efficiencies through its contribution to managing sequence of returns risk in retirement

HECM Strategies for Portfolio Coordination

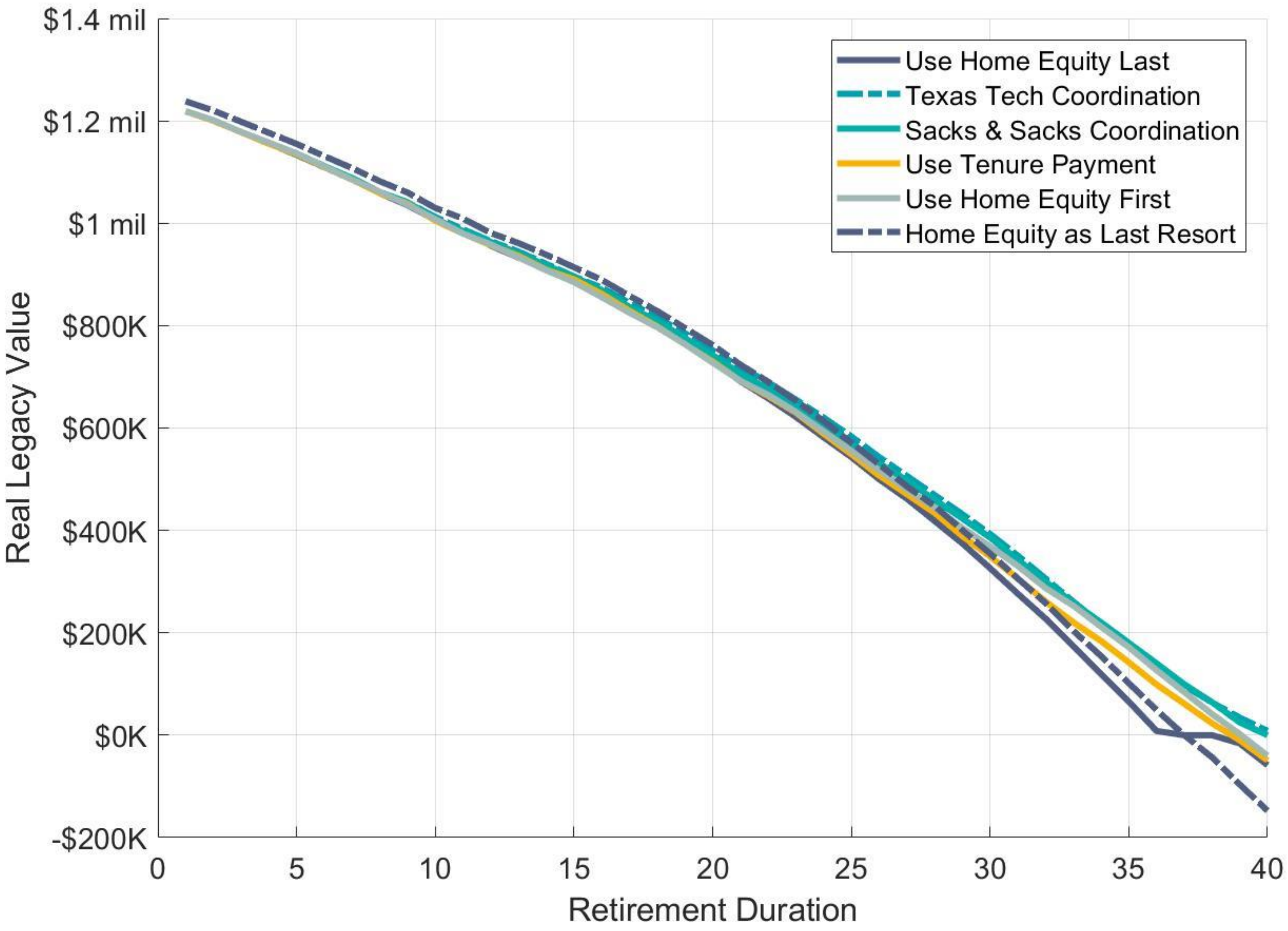
- Ignore Home Equity

- Home Equity as Last Resort ("Conventional Wisdom")
- Use Home Equity First
- Sacks and Sacks Coordination Strategy
- Texas Tech Coordination Strategy
- Use Home Equity Last
- Use Tenure Payment

Probability of Success for a 4% Post-Tax Initial Withdrawal Rate
$1 million portfolio, $500,000 home value, 25% Marginal Tax Rate



Median Real Legacy Value for a 4% Post-Tax Initial Withdrawal Rate
$1 million portfolio, $500,000 home value, 25% Marginal Tax Rate



Conclusions

- Conventional wisdom hurts retirement sustainability: HECM shouldn’t be last resort
- Strategic HECM use: improved retirement sustainability, larger legacy
- WHY IT WORKS: Buffer to Mitigate Sequence Risk; Growing Line of Credit
- Low interest rates favor HECM (unlike everything else)
- HECM helps middle class: more benefits when home value is large relative to portfolio size (and when home value is under $765,600)
- Responsible use of HECM can improve retirement income efficiency

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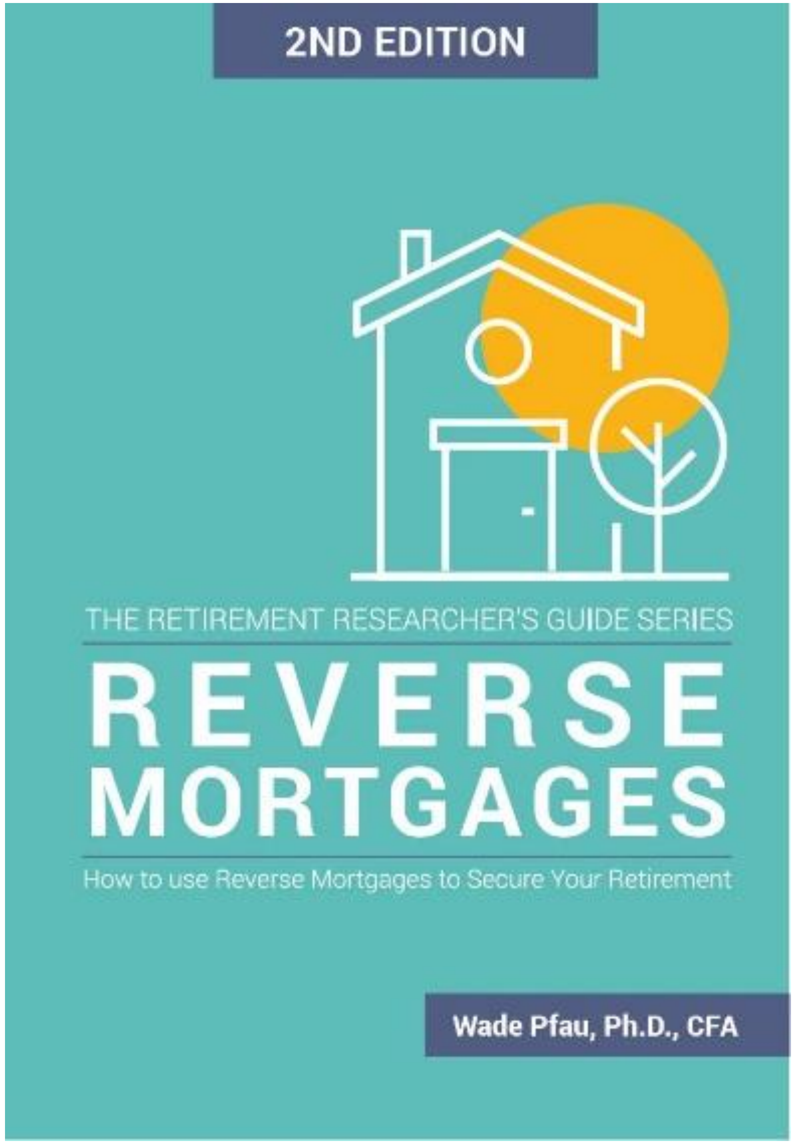
THANK YOU!
ANY QUESTIONS?



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