Testimony of the
National Council on Aging

Before the
Subcommittee on Health
Committee on Energy and Commerce
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Regarding
Planning for Long-Term Care

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Barbara R. Stucki, Ph.D.
Project Manager, Use Your Home to Stay at Home Initiative
National Council on Aging

Good afternoon, Mr. Chairman and Members of the Subcommittee. My name is Barbara Stucki. Over the past 13 years, I have been conducting research on private sector financing for long-term care. I currently manage the Use Your Home to Stay at Home Initiative for the National Council on Aging (NCOA). I would like to thank you for providing the NCOA the opportunity to testify about the need to include home equity as an essential element of long-term care planning.

Americans want to continue to live at home as they grow older, even if they need help with everyday tasks (termed "age in place"). Many impaired older homeowners, however, are unprepared for the financial challenges that can come with a chronic health condition. This is true not only for cash-poor seniors, but also for middle-income families who often struggle to pay the extra cost of help at home. When family budgets become strained due to unexpected long-term care expenses, impaired elders often turn to Medicaid for support. Due to the high cost of nursing homes, elders who get help in institutional settings are especially vulnerable to spending-down to Medicaid.

We believe that reverse mortgages offer important opportunities to rapidly reduce the need for government assistance by strengthening an elder's ability to age in place. Over 80 percent of people age 65 and older are homeowners.[1] For many older Americans, home equity is the most important financial resource to increase their resilience to the financial shocks that can come with declining health and ability. These added resources can help impaired elders to both avoid a costly crisis, and to plan ahead for these needs. Greater use of home equity among older homeowners has the potential to reduce their risk of needing Medicaid by:

- Providing resources sooner to keep small problems from becoming major catastrophes.

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[1] Callis, Robert R. and Cavanaugh, Linda B. (2004). Census Bureau Reports on Residential Vacancies and Homeownership. Washington, DC: United States Department of Commerce News, CB04-179.

- Increasing flexibility in the household budget to help seniors to pay a wide array of expenses associated with aging in place, and to reduce the financial shocks that often come with declining health and ability.
- Strengthening ties of reciprocity that underlie the networks of informal support for elders.

Encouraging older Americans to use reverse mortgages to "age in place" also can offer a more effective and equitable approach to reducing taxpayer burdens for long-term care than limiting Medicaid eligibility or benefits. With over **$2 trillion** tied up in their homes, home equity has the potential to help to rebalance our nation's long-term care delivery system, integrate financing for housing and supportive services for seniors, and create new opportunities for public-private partnerships.

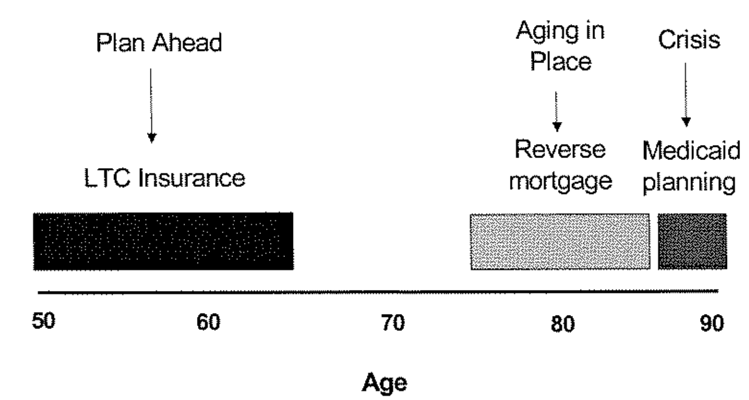
Home Equity – A New Resource for Long-Term Care Planning

Americans of all ages value their ability to live independently. But without careful planning, living at home with an impairment may be difficult. A serious fall or chronic illness can quickly drain hard-earned retirement dollars. Maintaining adequate cash flow can also become problematic when the need for supportive services fluctuates from month to month. Families who are assisting elders with a progressive chronic condition, such as Alzheimer's disease, face considerable uncertainty in trying to budget funds to provide help for many years.

Currently, there are two main financial strategies to deal with these challenges. One option is to purchase long-term care insurance before retirement, when a person is healthy and premiums are affordable. The more common approach is to rely on income and savings, and hope for the best. Most seniors today rely on this "pay as you go" approach, and often to turn to Medicaid and other public programs for assistance when they come up short.

Tapping home equity offers a third alternative for homeowners who could not prepare for this need with private long-term care insurance or savings (Figure 1). By taking out a reverse mortgage, older homeowners can convert a portion of their home equity into cash while they continue to live at home for as long as they want. To qualify, all owners of the property must age 62 or older. Borrowers do not need to make any loan payments for as long as they (or in the case of spouses, the last remaining borrower) continue to live in the home as their main residence. When the last borrower moves out of the home or dies, the loan becomes due.

Figure 1. Reverse Mortgages – A New Planning Tool for Aging in Place



If used wisely, reverse mortgages can pay for preventive measures and day-to-day support so that impaired elders can continue to live at home safely and comfortably for many years. As an immediate long-term care financing tool, these loans also have the potential to reduce the risk that impaired elders and their families will to turn to Medicaid in times of crisis. The following example highlights the potential benefits if a homeowner with $150,000 in home equity took out this loan:

> Scenario #1: Janet Zibley (age 85) has arthritis, which makes it difficult for her to manage on her own. She pays a neighbor $1,000 per month to help around the house. But when she needs more assistance from a home health aide, her monthly bill for services can be over $3,000. At her age, Janet could receive $102,378 from a reverse mortgage. Her line of credit could cover monthly expenses of $1,000 for over 13 years, or $3,000 each month for over 3 years, at the current interest rate.

When an unstable health condition disrupts the family budget, it can be easy to come up short when it is time to pay the bills. A reverse mortgage credit line can help manage cash flow since the money is available when needed. Borrowers only pay interest on the amount that they use.

Strengthening the Safety Net

Shifting the focus of long-term care from the facility to the home has profound implications for the amount, timing, and sources of funding that will be needed. When a person develops a chronic health condition such as diabetes, arthritis, or Alzheimer's disease, aging in place means more that just staying put. They will need a place to live that is safe and fits with their abilities. As driving becomes difficult, it is important to have reliable and affordable transportation. Extra funds for family caregivers or for home modifications (such as a ramp or lift) can extend the time that an impaired elder can live at home.

One of the challenges of our current long-term care financing system is that it is based primarily on insurance approaches. Insurance works best to protect against catastrophic costs, such as nursing home care. However, this financing mechanism is not appropriate to deal with everyday expenses, such as weekly transportation to the doctor or help with household chores. These expenses can still be a big burden on the family budget, and can increase the risk for spend-down among impaired elders on a fixed income.

Reverse mortgages can supplement and strengthen insurance-based long-term care financing strategies by offering older homeowners more flexibility to fill unmet needs and critical gaps in services. Proceeds from a reverse mortgage are tax-free, and borrowers can use these funds for any purpose. Borrowers can select to receive payments as a lump sum, line of credit, fixed monthly payments (for up to life in the home) or in a combination of payment options.

Home equity can be the "glue" that holds an elder's financial plans together when they have a chronic health condition. Consider the potential value of a reverse mortgage if a family that lives in a house that is in good repair and worth $150,000 took out this loan. They own their home free and clear of any debt:

> Scenario #2: Tom and Jill Smith (ages 69 and 65) bought long-term care insurance that will pay for services when they need help with personal care (such as bathing, dressing, or eating) or supervision due to Alzheimer's disease. For now they can still manage on their own, but want to add a bathroom downstairs to reduce the strain of climbing the stairs. Based on Jill's age, the Andersons would receive $66,104 from their reverse mortgage. They could take $20,000 of the loan to install a new bathroom. They could keep the rest ($46,104) in a line of credit. These funds could be used to meet any additional expenses before they become eligible for services under their long-term care insurance policies.

This story highlights how people with a chronic condition can have a variety of unmet needs, even with good financial planning.

Another limitation of Medicaid and private long-term care insurance is that they are designed to help seniors cope with a severe mental or physical impairment after it has occurred. In contrast, reverse mortgages can reduce long-term care risks by paying for a wide array of early interventions that help impaired elders avoid a crisis. A high proportion (46 percent) of older homeowners have a functional limitation, such as difficulty with climbing stairs or carrying groceries, that may make it hard for them to continue to live at home safely.[2] While these impairments are modest, they can have serious consequences if they lead to bigger problems such as malnutrition or debilitating injuries.

Potential of Reverse Mortgages

In the past few years, there has been a dramatic increase in the volume of reverse mortgages made nationwide, reaching over 195,000 loans originated in total.[3] Low mortgage rates, combined with growing awareness of this loan, have significantly increased the popularity of reverse mortgages.

Older homeowners can select from several different types of reverse mortgages. These include:

- Home Equity Conversion Mortgage (HECM) – This program is offered by the Department of Housing and Urban Development (HUD) and is insured by the FHA. HECMs are the most popular reverse mortgages, representing about 90% of the market.

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[2] Stucki, B. (2005). Use Your Home to Stay at Home. Washington, DC: National Council on Aging.
[3] National Reverse Mortgage Lenders Association Year-By-Year HECM Production (1990-Present). From www.nrmalonline.org, retrieved 5/15/06.

- Fannie Mae Home Keeper loan - Borrowers can receive more cash from these loans than with a HECM since the loan limit for this product is higher.
- Financial Freedom Cash Account loans – This product is beneficial for seniors who own homes that are worth more than $400,000 since there is almost no maximum loan limit.

As private residences continue to appreciate in value, their equity grows as a financial resource. The median home value among people age 65 and older in 2003 was $122,789. The amount that reverse mortgage borrowers can receive is based primarily on the value of the home, the type of loan, and the current interest rate. A HECM loan at today's interest rate for a house worth $122,789 could range from $52,950 for a borrower age 65, to $67,261 for a borrower age 75, to $82,884 for a borrower age 85.

When the last borrower dies or moves out of the home, the reverse mortgage becomes due and needs to be paid. How much equity will be left at this point depends on the amount of money used from the loan, how long the loan was kept, interest rates, and any home appreciation.
If, at the end of the loan, the loan balance is less than the value of the home, then the borrower or heirs get to keep the difference. An important protection offered by reverse mortgages is that the borrower (or heirs) will never owe more than value of the home at the time they sell the home or repay the loan. This is true even if the value of the home declines.

Figure 2. Candidate households to use a reverse mortgage for aging in place

27.5 million households age 62+ in 2000

↓

21.5 million own a home

↓

15 million would likely qualify for a reverse mortgage

↓

13.2 million could receive at least $20,000 from a reverse mortgage (48%)

Source: NCOA (2005). *Use Your Home to Stay at Home*. Analysis based on data from the 2000 Health and Retirement Study.

Based on our analysis of data from the 2000 Health and Retirement Study, we estimate that a total of **13.2 million** (48 percent of the 27.5 million elder households) are candidates for using a reverse mortgage to pay for long-term care (Figure 2). These households would likely meet the requirements to qualify for this type of loan. In addition, they would likely receive a loan worth at least $20,000 based on their age and the value of their home.

Medicaid and Reverse Mortgages

Until recently, policymakers have largely favored preserving the home of impaired elders. The passage of the Deficit Reduction Act of 2006, which includes limits on home equity for Medicaid eligibility ($500,000 or less, up to $750,000 at state discretion), now sends a strong message to Americans that housing wealth will be part of the long-term care financing mix. As a result, impaired elders who have a large amount of equity in their home will be more likely to consider using a reverse mortgage. The law explicitly allows elders to use this financing tool to reduce home equity to meet Medicaid eligibility levels.

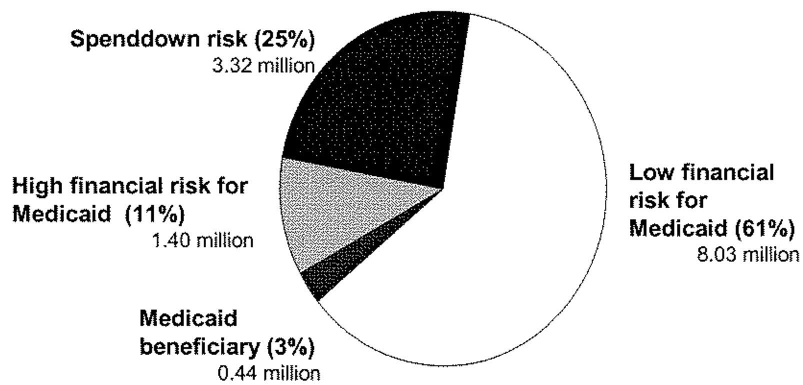
We believe that Medicaid could also benefit from voluntary initiatives to encourage impaired elders with modest housing assets to tap their home equity. An important target for these efforts are older homeowners who are most likely to turn to public programs for assistance. We estimate that among the 13.2 million households that are likely candidates for a reverse mortgage, about 5.2 million (39 percent) either receive Medicaid benefits or are at financial risk for needing government assistance (Figure 3). This vulnerable population includes distinct subgroups, each of which will likely respond differently to incentives for reverse mortgages.

Pre-Medicaid population – These elder households are important from a policy standpoint because their limited financial resources place them at greatest risk for turning to public programs should they need long-term care. The group that may benefit most from incentives for reverse mortgages may be spend-down risk households. These households are primarily composed of "tweeners," elders whose financial resources are sufficient to pay for everyday expenses but not to handle substantial out-of-pocket payments for services and supports at home. These elders may be able to qualify for Medicaid by depleting their income and assets to pay for long-term care (termed "spend-down") in the community.

For many tweeners, home equity is their main financial buffer against substantial medical and long-term care expenses. For these elders, uncertainty about future health expenses can make getting a reverse mortgage seem like a risky proposition. Borrowers who spend their equity at an earlier stage will have fewer financial resources when they become more severely impaired. Tweeners might be encouraged to tap home equity by a public-private partnership program that would provide additional protections and help them to leverage their limited assets so they can stay home longer.

Figure 3. Candidate households are on or at financial risk for Medicaid

N=13.2 million older households who are candidates for a reverse mortgage for aging in place



Source: NCOA (2005). *Use Your Home to Stay at Home*. Analysis based on data from the 2000 Health and Retirement Study.

Medicaid long-term care beneficiaries – Though Medicaid beneficiaries may be receiving home and community services, additional cash from reverse mortgages can help cover unmet needs while providing greater choice and control over services. A significant challenge for these elders who live at home is the strict financial eligibility requirements for Medicaid Home and Community Based Services (HCBS). States that restrict the income available to HCBS beneficiaries, and limit spousal protections, often place these older homeowners at risk for moving to the nursing home since they are left with few resources to pay everyday expenses or to deal with financial emergencies such as a leaky roof.

To increase the financial resilience of these elders, Medicaid could allow HCBS beneficiaries to supplement their benefits with the proceeds of a reverse mortgage. These additional funds could make a critical difference in their ability to pay for the expenses associated with living in the community. This approach could also provide additional support to family caregivers.

Implementing this strategy will require changes to limitations on supplementation under Medicaid. Currently, beneficiaries are not allowed to receive additional financial assistance from other sources, since Medicaid is seen as a payer of last resort. One option would be to develop a plan of care for beneficiaries that would include everyday expenses that could be covered by the loan. This approach to using home equity would need to be evaluated carefully, to take into consideration such factors as the presence of a spouse.

Our research indicates that only about 3 percent of older homeowners are Medicaid beneficiaries. This may reflect the fact that these elders have few financial resources, including housing wealth. However, recent research suggests that other factors may also be at work. In particular, older homeowners who face nursing home stays of 100 days or longer are more likely to sell the home than those who do not need such lengthy care in a facility.

Reverse mortgages could make it easier for Medicaid nursing home beneficiaries who still own a home to transition from the facility to the community, if this is their wish. Loan funds could pay transition expenses and cover care management costs that facilitate a move from the institution to community living. These funds could also help impaired elders to pay for substantial home modifications and other assistance not covered by Medicaid, that can help them to stay at home.

Expanding the Use of Home Equity Through Public-Private Partnerships

Despite the potential of reverse mortgages, older Americans have not been encouraged to tap into their substantial housing assets to pay for home and community long-term care services. Instead, home equity is usually liquidated by selling the house, often in emergency situations, to pay for nursing home expenses.

Getting people to adopt new behaviors is never easy. This is especially true for reverse mortgages, since the idea of tapping home equity for aging in place is a relatively new concept. A new public-private partnership demonstration program for reverse mortgages would play an important role to identify the right kind of incentives and messages that will get older homeowners to take action. Such a program could expand the options for impaired older homeowners, and encourage them to tap the equity in their homes sooner to avoid a crisis.

Elements of a partnership program for reverse mortgages. The model for this new public-private partnership program for reverse mortgages could be the existing Long-Term Care Partnership Program (LTC Partnership). The goal of the LTC Partnership is reduce Medicaid expenditures by encouraging the purchase of private long-term care insurance as a way to delay or eliminate the need for policyholders to rely on Medicaid. Individuals who buy designated partnership policies are allowed to protect some or all of their assets from Medicaid spend-down requirements, should they exhaust their insurance benefits and need public assistance for long-term care. Under this program, policyholders must still meet Medicaid income requirements.

A similar approach could be used to encourage older homeowners with moderate incomes to take out a reverse mortgage to fund their long-term care needs rather than relying on Medicaid. Under this type of partnership, borrowers who use a certain portion of the equity in their homes to pay for home and community services could receive more favorable treatment under Medicaid's asset rules. One issue would be whether borrowers would still need to meet Medicaid income requirement. Impaired older homeowners who participate in a reverse mortgage partnership program would likely need these funds to help them to continue to live at home once they qualified for Medicaid.

In developing this type of public-private initiative for reverse mortgages, there will be many issues that go beyond the framework of the LTC Partnership. These include:

- Determining which types of expenditures, including paying for such items as a new furnace or support for family caregivers, qualify as "long-term care services" to meet Medicaid requirements under the partnership program.
- Monitoring the use of reverse mortgage funds, to ensure that they are being used appropriately.
- Determining the amount of home equity that would meet the program criteria to receive more favorable treatment of assets under Medicaid.
- Identifying the loan payment options (lump sum, line of credit, monthly payment) that will be allowed under the reverse mortgage partnership program.
- Prioritizing access to services and supports under a state HCBS program for participants in the reverse mortgage partnership program who want to continue to live at home.

One of the benefits of a reverse mortgage is that they can currently be used for any purpose, including to pay for a wide array of services and supports, as needed. This flexibility will also create additional challenges to ensure that the loan funds are being used as intended under the partnership program.

Example from Minnesota. Many of these issues were recently tackled by policymakers, along with aging and housing experts, in the State of Minnesota, who developed a model reverse mortgage incentive program targeting older homeowners at risk of needing nursing home care. This effort was conducted as part of an ongoing study that is being funded by the Assistant

Secretary for Planning and Evaluation (ASPE) and the Administration on Aging (AoA), and directed by NCOA and the Lewin Group.

The proposed program, which is being considered by the Minnesota Legislature, would combine education and counseling, with reduced reverse mortgage closing costs and assistance in the home through the state's Alternate Care program. Older people with modest value homes (worth up to $150,000) who need supportive services that are not paid by government programs would qualify for reverse mortgage incentives. These would include up to $1,500 to pay the upfront mortgage insurance premium for a HECM loan, and reduced servicing fees. To qualify for help at home under the Alternate Care program, program participants would need to use up the proceeds of their reverse mortgage loan, or spend substantially all of the payments from a reverse mortgage to pay for services for a period of at least 24 months or in an amount of at least $15,000. Besides help at home, these services and supports could include basic shelter needs, home maintenance, and modifications or adaptations, necessary to allow the person to remain in the home as an alternative to a nursing facility placement. Participants would be required to spend the proceeds of their loan according to their individual spending plan. Those who used home equity to qualify for Alternate Care program would not be required to pay a monthly participation fee for the program, nor would they be subject to an estate claim by the state for the services they received.

Minnesota believes that the program would add another layer of access to services and supports for this vulnerable population. In addition, the program could free up some public resources and may influence when and where these elders access public assistance in the future.

Reducing Loan Costs

Many seniors are deterred by the substantial upfront costs of reverse mortgages. Today, a 75-year-old HECM borrower with a home valued at $150,000 would have to pay $6,000 in closing costs on a loan worth $83,490. These closing costs (the origination fee paid to the lender and the upfront mortgage insurance premium required by HUD) represent a significant amount of the money that could be available to pay for long-term care. Additional costs include other loan-related fees (such as title search and inspections) and any repairs that the house may need to meet minimum HUD requirements.

To help reduce their long-term care expenditures, state Medicaid programs could be allowed to subsidize mortgage insurance, origination fees, and other closing costs for long-term care beneficiaries. Such incentives could make this financing option more attractive to elders with limited liquid resources, including Medicaid beneficiaries who live in the community, and increase the amount of funds available to them.

The costs associated with taking out a reverse mortgage become even more critical for impaired elders. These seniors are likely to be older and poorer than typical reverse mortgage borrowers. It will be important for the Department of Health and Human Services to work with HUD and the mortgage industry to identify ways to reduce the cost of HECM loans for this vulnerable population.

Strengthening Consumer Protections

The market for reverse mortgages will continue evolve rapidly over the next few years in response to growing consumer interest in these loans. How these changes unfold will hold significant policy implications for our aging society. With so much wealth tied up in the home, the decisions that older homeowners make about this financial asset can significantly impact our nation's ability to balance public and private funding for long-term care and to respond to consumer preferences for aging in place. The public sector will need to play an active role to ensure that these developments include strong consumer protections and appropriately serve the needs of older Americans.

Despite the promise of reverse mortgages, few older homeowners are interested in tapping home equity for long-term care, often due to a lack of understanding about how these loans work. An important new resource to help address this barrier is the establishment of the National Clearinghouse for Long-Term Care Information, as part of the Deficit Reduction Act of 2006. NCOA would like to thank the Committee for creating this resource to educate Americans about long-term care. It will be important that the Clearinghouse include information and decision-support tools to help elders and their families make wise decisions on the use of home equity and reverse mortgages as a planning tool for aging in place.

A unique feature of reverse mortgages is that all borrowers must first meet with a HUD-approved reverse mortgage counselor before their loan application can be processed or they incur any costs. The main objective of this counseling is to educate potential borrowers about the appropriateness of these loans to address their financial needs and situation. We commend HUD for its recent efforts to expand counseling to address the unique needs of older homeowners who are considering a reverse mortgage so they can continue to live at home. The AoA is also playing a key role in providing the infrastructure for more in-depth counseling on reverse mortgages for aging in place through its Aging and Disability Resource Centers.

Ongoing discussions and joint actions by government, industry, and the private nonprofit sectors will be critical to overcome a wide array of barriers to the use of reverse mortgages, and to create a substantial "win-win" for government and consumers in the near future. Close collaboration between CMS, AoA and HUD should be encouraged as part of Federal policy, to achieve this goal.

Conclusions

As the population ages and the pressure on state Medicaid budgets rises, it becomes increasingly important to find effective ways to improve our long-term care financing system. Funding the growing demand for long-term care is a major national challenge that will require increased spending by both the public and private sectors.

Reverse mortgages have the potential to be a powerful force for system change, and to expand the boundaries of what is possible in using private funds to finance home and community services. Using this asset as a planning tool for aging in place could significantly enhance the resilience of older Americans to the financial risks of long-term care. If used wisely, a reverse mortgage can help borrowers to live with independence and dignity for many years. With supportive public policies, appropriate incentives, careful protections, and innovative products, the voluntary use of reverse mortgages may offer additional options for impaired older Americans to take action today, and use their existing resources more effectively.