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Financial Assessment

What is a financial assessment?

Effective in April 2015, the FHA began requiring borrowers to pass a “financial assessment” prior to obtaining the reverse mortgage. The goal of the financial assessment is to ensure the borrower is able to pay their homeowner’s insurance and real estate taxes, and can maintain a reasonable standard of living after obtaining the reverse mortgage.

What is the financial assessment process?

In the financial assessment lenders will review potential borrowers’ credit history and income to compare to their expenses. Borrowers with a satisfactory credit history will meet the following requirements:

- **No late property tax payments in the last 24 months before the date of the application. At the time of the application, all property charges must be current.**
- **All housing and installment debt payments have been made on time for the previous 12 months with no more than two 30-day lates in the past 24 months.**
- **No major derogatory credits appear on revolving accounts for the past 12 months.**

What if I have credit trouble?

If the borrower has a history of late payments, an explanation must be provided to the lender. The lender will then determine whether this explanation is considered an “extenuating circumstance.”

Extenuating circumstances may include, but are not limited to:

- Loss of income due to the death of a spouse or family member.
- Unemployment, reduced work hours or a granted leave of absence.
- Emergency medical treatments or hospitalization.

The financial assessment is designed to ascertain whether the lender must set aside a certain amount of money to pay for the borrower's homeowner's insurance and real estate taxes for the life of the loan. This "set aside" amount will reduce the loan proceeds available directly to the borrower.

Will a set aside be required?

Two components are used to evaluate whether a set aside is needed: willingness and capacity. Willingness is determined by examining a borrower's credit history. Capacity is determined by measuring a borrower's income against their expenses.

What is a LESA?

If the results of the financial assessment show that the borrower fails either the willingness or capacity requirement, a Life Expectancy Set Aside (LESA) may be required. A LESA allows some funds from the reverse mortgage to be set aside to ensure payment of taxes and insurance on the home.

The LESA is calculated based on the borrower's real estate taxes and homeowner's insurance and is adjusted to the anticipated increase over the term of the HECM. Its purpose is to pay taxes and insurance on the home in which the borrower lives.

If the borrower passes financial assessment, no LESA is required. If the borrower fails any part of the financial assessment, they either must overcome the failure with an explanation of extenuating circumstances or compensating factors, or be subject to a LESA.

Financial assessment guide: Glossary of terms

Compensating factors: characteristics of a borrower that show how their residual income is acceptable despite being below the standards for loan approval. Examples of compensating factors include income from a non-borrowing spouse; overtime, bonuses, and commissions; retirement and savings accounts; and a reverse mortgage line of credit.

Derogatory credits: negative marks on a credit report that show late payments, collections, foreclosure or bankruptcy.

Extenuating circumstance: a nonrecurring event that is outside the borrower's control and causes a serious and prolonged reduction in the borrower's income and an inability to pay bills.

Financial assessment: a process lenders use to make sure borrowers will be able to pay their homeowner's insurance and real estate taxes and maintain a reasonable standard of living.

Life Expectancy Set Aside (LESA): funds that are set aside to pay a borrower's homeowner's insurance and property taxes for the life of the loan. (See "set aside".)

Property charges: taxes, insurance and other fees on a home, such as property taxes, homeowner's insurance, flood insurance if applicable, as well as fees from homeowner associations (HOAs), planned unit developments (PUDs) and condominiums.

Set aside: funds from the reverse mortgage that are placed in reserve ("set aside") to pay a borrower's homeowner's insurance and real estate taxes. The set aside can affect the loan amount available to the borrower.

ReverseMortgages.com

3401 W. Broadway Business Park Ct. | Suite 213
Columbia, MO 65203 | 877.611.1329 | NMLS# 1313859
www.reversemortgages.com

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