Study on Comparative Law of Housing Reverse Mortgage Loan System

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Abstract: This article aims to conduct a comparative legal study of the reverse mortgage system for housing. Reverse mortgage is a financial service aimed at the elderly, which allows them to obtain liquidity by mortgaging their houses to financial institutions while retaining the right of use and ownership until the borrower's death or sale of the property. Firstly, this paper introduces the concept, characteristics and historical development of the reverse mortgage for housing, and then conducts a comparative analysis of the reverse mortgage systems in the United States, Canada, France, and Singapore. By comparing the systems in different countries, this paper finds that there are various differences in the legal status, contract terms, asset assessment standards, risk management and supervision, consultation and information disclosure, and dispute resolution mechanisms of reverse mortgage systems. Finally, this paper summarizes the relevant information of the reverse mortgage system for housing, and provides suggestions and prospects for its establishment and improvement, aiming to provide a reference for the development of the system.

Keywords: Comparative analysis, Reverse mortgage, Housing, Elderly, Financial service.

1. System Overview

Reverse mortgage, also known as "residential property reverse mortgage," mainly refers to the borrower using their own house as collateral to apply for a loan from a lending institution. After evaluating the value of the mortgaged property, the lending institution calculates the borrower's life expectancy, determines the loan standard based on the property value and related principles, and then pays the borrower cash on a monthly or yearly basis for their retirement expenses. After the borrower passes away or permanently moves out of the house, the ownership of the property is transferred to the lending institution. From a legal perspective, reverse mortgage refers to the debtor, i.e., the borrower, using their property that they own to secure a loan from the creditor, i.e., the lending institution. The lending institution pays the borrower according to the contract's agreed-upon standards, and the borrower continues to occupy and use the mortgaged property during the contract period. If the borrower cannot repay the debt when the contract expires, the lending institution acquires the right to dispose of the mortgaged property.

Reverse mortgage has complex legal relationships. From the analysis of the reverse mortgage process, the system involves many parties, including lending institutions, underwriters, appraisers, notaries, lawyers, and other intermediaries. Different parties form different legal relationships, and different legal relationships intertwine to form a complex legal relationship for reverse mortgage. First of all, the elderly who meet the conditions for applying for reverse mortgage, as borrowers, apply for reverse mortgage loans from lending institutions, forming a creditor-debtor relationship based on this loan relationship. To ensure that their creditor's rights can be realized, lending institutions require borrowers to use their property as collateral. As a result, a legal relationship of mortgage guarantee is formed between the borrower as the mortgagor and the lending institution. Secondly, reverse mortgage requires the participation of many intermediary institutions, such as property appraisal, relevant matters certification, and other matters. Thus, a commission agency relationship is formed between the lending institution and various intermediary institutions. Finally, the government regulatory authority exercises its supervisory power over reverse mortgage, forming an administrative management relationship between the regulatory authority and the various participating parties in reverse mortgage.

It is worth emphasizing that the lending institution has no right of recourse. Borrowers apply for loans from lending institutions using their property as collateral, but the repayment of the loan is limited to the residual value of the mortgaged property when the contract terminates. Even if the lending institution's loan principal and interest have not been fully repaid, the lending institution cannot claim the debt from the borrower's other property. If the borrower and the lending institution agree that the mortgaged property will belong to the lending institution directly after the borrower's death, the borrower does not need to pay back the principal and interest to the lending institution during their lifetime.

At the same time, it is necessary to note that the parties participating in this system are specific. Although different countries have different restrictions on the conditions for reverse mortgage borrowers, they mostly apply to the elderly. The elderly must meet certain age requirements, generally limited to those who are 60 years old or older, and they must own property with complete independent property rights. Lending institutions have stricter restrictions. They should be specialized in reverse mortgage business to acquire or accept the mortgaged property of the elderly and gradually provide loans for their retirement expenses. They must be authorized to become lending institutions for reverse mortgage, not only meeting the statutory conditions but also having special authorization.

However, there are limitations on the exercise of property ownership by the parties involved. During the loan period, the
borrower still enjoys the ownership of the mortgaged property, but the exercise of their ownership is subject to certain restrictions. For example, the borrower can continue to live in the mortgaged property until their death, sell it, or permanently move out, and after their death, the property can still be inherited by their heirs. Of course, this is based on the condition that the heirs repay the entire loan principal and interest. At the same time, the borrower also has corresponding obligations, such as daily maintenance and repairs of the mortgaged property, payment of property insurance fees and property management fees, and so on. In terms of loan disbursement and repayment methods, reverse mortgage loans are disbursed in installments, and repayment is made in a lump sum after the loan period expires. Lending institutions can obtain the ownership of the mortgaged property by auctioning it or directly acquiring it.

2. Historical Evolution

Reverse mortgage was initially designed to solve the retirement difficulties faced by the elderly who have a house but no money. There are two views on its origin. One view believes that it originated in the Netherlands more than 400 years ago. At that time, some elderly people owned houses but could not provide themselves with a relatively affluent elderly life. Therefore, these elderly people sold their houses to young people who could choose to pay the house price in a lump sum or in installments. After the transaction was completed, the young people did not immediately take back the house but allowed the elderly people to live in the house until they died, but the elderly people had to pay rent. The second view believes that it originated in England and was introduced in the 1920s as Home-Equity Reversion.

Reverse mortgage has flourished in the United States. After successfully launching various types of reverse mortgage products in the United States, many European countries have also gradually launched this business. Countries such as Canada, Japan, Singapore, and Australia have also introduced this new type of financial product. Nowadays, reverse mortgage is not only used by countries around the world to solve their retirement problems but also proves to be an effective financing method.

3. Comparative Study on the Implementation and Experience of Reverse Mortgage in Various Countries

The mortgage system is the preferred solution for addressing retirement issues in major countries or regions around the world, but the United States has the most mature system for its operation.

3.1 United States

In 1961, the United States introduced its first reverse mortgage for housing, which was only processed as a single case. However, this mortgage drew people's attention to the role of reverse mortgages in addressing retirement issues. Various reverse mortgage products have been designed and developed, including periodic annuities, housing use annuities, credit limits, etc. However, due to the lack of legal regulation and control measures for reverse mortgage products, the market was relatively chaotic at that time. Additionally, the housing mortgage securitization market in the United States was not well developed, and assets lacked liquidity. The loan funds of financial institutions were locked in for decades, and the longer the term, the greater the risk. Therefore, financial institutions lacked enthusiasm for this business, and the market response was not strong in the early stage of the implementation of reverse mortgages.

As the United States rapidly enters an aging society, the government realizes the importance of opening up new retirement models, and reverse mortgages once again enter people's vision. The United States government timely launched various reverse mortgage products as its housing self-ownership rate increased, learning from the problems encountered in the early implementation of this system. The National Reverse Mortgage Lenders Association (NRMLA), established in 1981, is a professional non-profit organization that provides advice on reverse mortgages to the public and promotes the system. Additionally, a series of laws and regulations were introduced to regulate the operation of the reverse mortgage system, such as the National Housing Act of 1987. According to this act, the Home Equity Conversion Mortgage (HECM), which affects the operation of the reverse mortgage system in the United States, was designed. The Federal Housing Administration (FHA) expanded its role in guaranteeing reverse mortgages through the Home Equity Conversion Mortgage Insurance Demonstration Program. In 1989, Fannie Mae attempted to securitize reverse mortgages and sell them on the secondary market. Financial Freedom successfully securitized the repurchased housing through reverse mortgages in 1999, which changed the disadvantages of long cycles and large amounts of occupied funds, improved the liquidity of reverse mortgage products, and greatly increased the enthusiasm of financial institutions. Thus, this system developed rapidly.

After 2000, with the good operation of the macroeconomy and the steady development of the real estate market in the United States, the government increased its investment in reverse mortgage products, such as providing insurance for this product by the public insurance department, and further promoting reverse mortgage securitization measures. From then on, the reverse mortgage market in the United States has achieved unprecedented high-speed development.

In terms of the legal system, the United States government has done an outstanding job. The implementation of reverse mortgages faces many market operating risks, such as interest rate risk, moral hazard, and fluctuations in housing prices. As there are many participating parties involved in the system, it is difficult to coordinate the interests of all parties. Additionally, elderly borrowers have weak risk resistance and rights protection awareness. Therefore, effective control of the risks in the operation process of this system is particularly important. The US government attaches great importance to risk control in the implementation of reverse mortgages. Not only have laws and regulations been formulated to provide a legal basis for the implementation of the reverse mortgage system, such as the enactment of many housing laws, but also special regulations have been formulated to regulate the
supervision of the reverse mortgage system. In addition to formulating relevant laws and regulations, the US government also attaches great importance to updating the legal system. Relevant legislative bodies will revise or introduce new laws and regulations based on the continuous changes in the market and demand, allowing the reverse mortgage system to operate within its established legal framework, and thus allowing the law to protect the implementation of reverse mortgages.

3.2 France

The implementation of reverse mortgages in France followed a path from the private sector to the official sector. First, a quasi-financial product called “Viager” appeared in the private sector. The restrictions on collateral were relatively small. Not only could houses and small farms be used as collateral, but also yachts. The most significant feature of this product was that both parties to the loan contract were natural persons, with no participation of financial institutions or governments. The two parties to the contract were only bound by the contract they signed. This product was recognized and supported by the French government due to its characteristics of using houses for retirement and its good development status. In 2006, France introduced a reverse mortgage system with French characteristics called “Attached Collateral Lifetime Annuity Loan.” To better implement this system, France not only modified the Civil Code to avoid legal risks faced by reverse mortgages but also specifically stipulated the “Attached Collateral Lifetime Annuity Loan” system in the Consumer Code.

3.3 Singapore

Singapore introduced reverse mortgages in 1997, and the insurance cooperative that introduced this system is the only financial institution in Singapore that provides reverse mortgage products to the public. At the beginning of the product launch, the market response was not strong due to the excessively strict application conditions. Later, the product was adjusted appropriately, such as expanding the scope of applicants, no longer requiring applicants to be policyholders, and expanding the scope of applicants from elderly homeowners of private houses to homeowners of public housing. At the same time, there is no guarantee during the implementation of reverse mortgage contracts, and there are no guarantee clauses that the lending institution has no recourse in the contract. This has deterred many applicants. Later, the Housing Development Board of Singapore proposed to add the clause “the lending institution has no recourse against the borrower” to the contract and established a reverse mortgage insurance system.

4. Enlightenment

4.1 Government Support

Through a comparison of the implementation of the reverse mortgage system in several countries and regions, it can be seen that, except for Canada, all other countries and regions rely on government support. The government not only provides policy and institutional support but also supervises the participating entities and operations of reverse mortgages. The U.S. government particularly emphasizes its support and regulation of the operation of reverse mortgages. Firstly, the government can directly participate in the operation of reverse mortgages as a market entity. Secondly, to ensure the benign operation of the reverse mortgage system, the U.S. government attaches great importance to the establishment of a supporting legal system, which makes the operation of the reverse mortgage system more stable. Finally, to avoid harm to the interests of elderly borrowers caused by asymmetry of information and expertise on both sides, official or semi-official institutions provide free consultation services to applicants to ensure the impartiality of information. France provides support for reverse mortgages through macro and micro aspects, mainly in regulation and guidance, respectively. By regulating and guiding, the reverse mortgage market can operate benignly. Additionally, the government also provides insurance for both borrowers and lenders, which helps to mitigate risks.

4.2 Applicant Conditions

Reverse mortgages are mainly used to solve the problem of retirement, so the borrowers are limited to the elderly. From a comparison of the above-mentioned countries and regions, although the minimum age limit for applicants varies, the product is limited to the elderly. The United States limits HECM applicants to those aged 62 and above, Canada to those aged 62 and above, Singapore to those aged 60 and above, Japan to those aged 65 and above, and Hong Kong to those aged 55 and above. In addition to age restrictions, there are restrictions on the mortgaged property and other conditions. For example, different reverse mortgage products in the United States have different requirements for mortgaged properties, and in Hong Kong, not only is there an age restriction, but the applicant must also be a Hong Kong citizen, and there are restrictions on the value and acquisition of the mortgaged property. Japan has the strictest restrictions, requiring the applicant to reside in the mortgaged property alone without children, and there are also restrictions on the applicant's income, such as welfare recipients being ineligible for reverse mortgages. Canada requires that the mortgaged property have independent ownership, and jointly owned property is not allowed to be used for reverse mortgages.

4.3 Choice of Lending Institutions

Lending institutions for reverse mortgages include banks, insurance companies, and trust companies. The United States has the widest range of lending institution choices, including any entity, including the government, that can become a lender for U.S. reverse mortgage products. Canada has private professional companies, Singapore has insurance companies, Japan has the government or banks, and Hong Kong has banks as lending institutions, but mortgage securities companies in Hong Kong must provide guarantees for the product. Therefore, banks or insurance companies, or a combination of both, are the most commonly used lending institutions for reverse mortgages.

4.4 Mandatory Insurance or Guarantees

Reverse mortgage products face the problem of long cycles and large amounts. Therefore, for lending institutions, the risks they face are relatively large, and the borrowers of this
product are all elderly, who have poor risk resistance. Therefore, most countries and regions require borrowers who purchase reverse mortgage products to purchase insurance for the reverse mortgage product in addition to insuring the mortgaged property. For example, the United States has established a reverse mortgage reinsurance mechanism to reduce the risk of financial institutions through insurance or guarantees. Hong Kong bundles reverse mortgages and insurance for sale, with banks as lending institutions responsible for loan disbursement and mortgage securities companies as insurers providing guarantees for reverse mortgages. After signing the reverse mortgage contract, borrowers not only need to repay the principal and interest to the bank but also need to pay insurance premiums to the mortgage securities company. If the mortgaged property cannot fully repay the principal and interest of the bank loan when the loan term expires, the securities company will directly compensate the loan difference to the bank.

5. Suggestions

During the establishment and improvement of the reverse mortgage system, it is advisable to learn from the successful experiences of other countries that have implemented this system.

A sound legal and regulatory system should be established, including relevant laws, regulations, rules, and normative documents, to clarify the legal status and related provisions of reverse mortgages and standardize the various systems involved. For example, the United States has established the Housing and Urban Development Act and other laws and regulations that define, regulate, and outline the relevant procedures for reverse mortgages, safeguarding the rights and interests of borrowers and lenders. Secondly, clear contract terms should be formulated for reverse mortgages, including the rights and obligations of borrowers and lenders, loan interest rates, collateral assessment standards, and other content, to ensure that the interests of both parties are fully protected. For example, the United Kingdom has established the Reverse Mortgage Agreement and other contract terms, which clarify the content and procedures of reverse mortgages, safeguarding the legitimate rights and interests of borrowers and lenders.

What’s more, a reliable asset appraisal agencies and standards should be established to ensure accurate and reliable collateral valuation and to avoid risks caused by inaccurate asset valuation. For example, Australia has established the Reverse Mortgage Assessment Standards and other assessment standards, which define the assessment procedures and standards, safeguarding the rights and interests of borrowers and lenders. Of course, a risk management and supervision should be strengthened, including strengthening risk management and supervision of borrowers, establishing sound risk assessment, control, and prevention mechanisms, safeguarding the rights and interests of borrowers, and avoiding risks caused by borrower defaults and other reasons. For example, Canada has established the Reverse Mortgage Regulatory Standards and other regulatory standards, which clarify the regulatory requirements and procedures for reverse mortgages, safeguarding the legitimate rights and interests of borrowers and lenders. And a comprehensive consultation and information disclosure services should be provided, providing borrowers with relevant information and risk warnings about reverse mortgages, enhancing borrowers' risk awareness and self-protection capabilities. For example, Japan has established the Reverse Mortgage Consultation Service Standards and other standards, which clarify the requirements and procedures for reverse mortgage consultation services, safeguarding the rights and interests of borrowers and lenders.

Finally, a sound dispute resolution mechanism should be established, including arbitration, litigation, and other means, to ensure that disputes between borrowers and lenders can be resolved promptly, fairly, and effectively. For example, the Netherlands has established the Reverse Mortgage Dispute Resolution Standards and other standards, which clarify the procedures and requirements for resolving disputes related to reverse mortgages, safeguarding the legitimate rights and interests of borrowers and lenders.

Overall, it is significant to note that the reverse mortgage systems in different countries may vary. Therefore, appropriate adjustments and improvements should be made based on the actual situation of each country. At the same time, potential risks and problems of reverse mortgages should be taken into account, such as inaccurate asset appraisal and inadequate protection of borrower rights, and supervision and risk management should be strengthened to ensure the sustainable development and stable operation of the system.

Author Profile

Kanfan Shi obtained a Bachelor's degree in Economics from Zhejiang Business University in 2022 and is currently studying a Master's degree in Law at Hunan University. He has also participated in a law study visit to the National University of Singapore. With internship experience in court, he infuses theoretical knowledge into judicial practice.