This Man Has The Answer To America's Retirement Crisis (And No One Will Listen)

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AAG

AAG founder and CEO Reza Jahangiri, who has 15 guitars in his collection and has played with Elvis Costello and Jeff Tweedy, believes reverse mortgages can play a vital role in retirement planning.

Sporting light stubble and an open-neck dress shirt, Reza Jahangiri settles into his office and promptly apologizes for the strong smell of Windex. The 39-year-old founder and CEO of American Advisors Group, the nation's largest originator of reverse mortgages, confides that he wipes down the surfaces in his office several times a day. He also has three organic meals delivered to his office daily and follows a workout regimen that includes boxing with a trainer twice a week.

If Jahangiri seems a tad obsessive, it's a quality that has served him well in the rocky 13 years since he first heard about, and became convinced of the big potential for, a congressionally blessed product known as a Home Equity Conversion Mortgage, insured by the Federal Housing Administration. Depending on their age and house's value, homeowners 62 and older can borrow up to $636,150 against their homes--taking it in a lump sum, monthly payments, a line of credit or a combination of all three. The borrower makes no monthly payments. Instead, the accruing interest and FHA insurance fees are added to the principal, and the whole amount becomes due when the borrower (and spouse, if there is one) dies or moves out. This is a non-recourse loan, and if more is owed on the mortgage than the house is worth, Uncle Sam eats the shortfall.

When he first heard about reverse mortgages, Jahangiri was attending night law school at Loyola Marymount and working on a medical screening startup with his brother and his dad, who had fled Iran in 1978 with his wife and two young sons. Reza formed AAG in 2004. In 2007, he went all in, plowing $750,000 he had raised from selling out of the medical business into his reverse-mortgage shop.

Then the housing bust and Great Recession hit. Since then, FHA-insured reverse-mortgage originations have dropped more than 50%, Wells Fargo and Bank of America have exited the business, and federal rules on who qualifies for the loans and how they may be marketed have been tightened. Adding to Jahangiri's challenges, AAG's first two celebrity pitchmen died unexpectedly--Mission: Impossible 's Peter Graves from a heart attack in 2010 and actor/ex-U.S. senator Fred Thompson from a recurrence of lymphoma in 2015.

Yet, bolstered by $5 million in equity he had raised in 2009, Jahangiri hung in there. AAG now has 1,200 employees, and last year, it originated 12,000 of the 49,000 new reverse mortgages the FHA insured. Its 2016 revenues of $219 million came mostly from reselling securitized loans on the secondary market. Jahangiri says the company has been profitable for seven years running--though he won't disclose how profitable.

Say this for Jahangiri: As the second-largest owner of AAG, with a stake that Forbes estimates is worth $100 million, he's sitting pretty should more Baby Boomers decide that tapping home equity is a necessary, or desirable, part of their retirement plan. Certainly the untapped potential is huge. Currently, there's $145 billion in FHA-insured reverse-mortgage borrowings outstanding. But Americans 62 and older have $6.2 trillion of home equity, while those in their 50s are sitting on another $3 trillion. "From the point of view of providing a sustainable retirement for people in the future, this is going to be a very important component," says Robert Merton, an MIT professor and Nobel laureate in economics.

Increasingly, retirement experts are discussing reverse mortgages as a planning tool for middle-class and affluent retirees. One strategy: Use several years of reverse-mortgage withdrawals to delay taking Social Security retirement benefits until 70, which results in a 76% bigger monthly check than if you'd claimed benefits at 62. Another idea: Keep an untapped reverse mortgage as a backup should stock prices tank--to limit "sequence of returns" risk. (If stocks crash early in your retirement and you don't cut back on withdrawals from your portfolio until they recover, you're in trouble.)

Retirement income expert Wade Pfau has discovered that young retirees can even turn a reverse mortgage into a cheap put against their home. Here's the play: The percentage of your home's value you're approved to borrow is determined by your age (younger folks can't borrow as much) and interest rates at the time you get the mortgage. When rates are low, as they are now, you're approved for a higher starting percentage.

Currently, a 62-year-old can get a mortgage line equal to about 50% of his home's value. That line, if left untapped, grows as you age. By the time you're 86, there's a 90% chance it will be greater than your house's current value, Pfau calculates. (Growth also depends on future rates.) If housing prices collapse, you can draw down the full line, knowing that when you sell the house or die all the lender can recover from you or your heirs is the lesser amount the home is worth. (Pfau predicts the FHA will eventually curb this gambit but says it can't change terms retroactively for lines that are already open.)

So will retirees embrace reverse mortgages? Too soon to say, but they haven't yet.

"We were early to market," Jahangiri says with a pained smile, taking a sip from a pink-lettered Drop Dead Diva coffee mug. (His wife, actress Kate Levering, was a regular on the hit Lifetime television show.) He adds later: "It's going to feel great years from now to say we saw this coming and we doubled down on it."

At AAG's glass-walled headquarters in Orange County, California,150 licensed loan officers listen patiently on their headsets to seniors who have responded to ads featuring the company's current pitchman, Tom Selleck. It's a tough sell. Of the half-million folks who called last year, only 9,000 took a reverse loan. (Another 3,000 borrowers were brought to AAG through a network of independent mortgage brokers and community bankers.)

It's hard to convert callers to customers, in part because many don't qualify. Plus, the fees are high (upfront costs on a loan can be as much as $12,000), and both the product and the process of securing a loan are complicated. Among other things, the FHA requires all would-be borrowers to talk to a certified mortgage counselor independent of AAG, a consult that typically costs $125.

"We're trying to give people financial stability through an underutilized asset," Jahangiri says. "But it's an uphill battle, and there's still a perception issue."

That perception issue stems from real problems with how--and to whom--reverse mortgages were sold in the past. Under the terms of the HECM program, a homeowner can lose his property if he fails to pay real estate taxes, lets property insurance lapse or allows his home to fall into disrepair.

In a 2012 report, the Consumer Financial Protection Bureau found strapped borrowers were taking out (and spending) too much of their equity at once and that nearly 10% were at risk of foreclosure because they wouldn't be able to pay tax or insurance bills later on. The consumer agency later cracked down on "deceptive advertising" by reverse-mortgage companies, including AAG, which last year settled for a $400,000 fine. (AAG admitted no liability and said it had already changed the disputed practices.)

More significantly, the FHA tightened the rules, requiring prospective borrowers to demonstrate they'll have the cash to keep up with taxes and insurance, and discouraging them from drawing the money down too fast. The sum of these changes: Reverse mortgages are no longer a last resort for desperate homeowners. Future growth depends on whether the middle class is ready to use their home equity to finance retirement.