

Mortgage Matters

It's a cliché, but, yes, owning a home is the American Dream. According to the Department of Commerce's Census Bureau, the U.S. homeownership rate has been close to 70 percent for the last several years. For many, their home is their greatest asset. It is at once an emotional and financial investment. Because of this, its value should be carefully guarded.

A mortgage, however, is not an asset. It's a liability and must be taken seriously. Every day, homeowners unnecessarily risk losing their homes by not making their mortgage payments. Foreclosure has an immediate personal impact and can affect a borrower's ability to buy a home in the future.

Happily, there are strategies to avoid defaulting on a mortgage and facing foreclosure. It's critical to understand these options in order to save your home. It's even more important to learn how to avoid foreclosure in the first place.

Flying Low, Flying High

Kyle was in big trouble, and he knew it. A pilot for a private airline that catered to corporate business travelers, he had been able to buy a large home in an upscale neighborhood a decade ago, and he mortgaged it to

the maximum amount possible. Over the years, he had maintained his property in a meticulous fashion and paid his mortgage like clockwork. But 9 months ago, the owner of the airline had some financial difficulties, putting Kyle out of work. Kyle could have found another job while the company was reorganizing, but he felt an allegiance to the company and especially its executive clientele, so he preferred to wait it out.

During this period, Kyle had only two sources of income: unemployment benefits and rental income from tenants who lived in the basement apartment of his house. This was just enough to pay for his utilities, food, and incidental expenses, but not much more. He was not able to afford his largest obligation, his mortgage, on this reduced income. Kyle reasoned that he could get away with skipping a few payments and as soon as he got back to work he would catch up.

Unfortunately, reorganizing the company took longer than he anticipated, and Kyle's creditors, including several credit card companies, started closing in on him. He consulted a friend, an attorney, who recommended filing for bankruptcy to discharge his credit card debt. Because bankruptcy does not discharge mortgage loans, **AU: REVISION OK?** Kyle's mortgage payments continued to fall further and further behind. He received notice that the bank had started default management procedures, a precursor to initiating foreclosure proceedings.

Although the bankruptcy severely downgraded his credit score, it allowed Kyle to put more of his income toward his mortgage loan. And it turned out that his previously regular payment history worked in his favor. His bank's default management department agreed to work with him to see what could be done to help him avoid losing his home.

It was clear that it was going to take a great deal of work to assist Kyle. The loan was now more than 9 months in arrears. Although the typical time frame for referring a loan to foreclosure is 4 months after the initiation of default management procedures, the bankruptcy had stalled the collection and foreclosure process, allowing the mortgage to run 9 months past due. Kyle asked his family to advance him a personal loan, which they agreed to do, with the stipulation that it would be repaid once he was working steadily again. Because of this loan he was able to offer the bank a substantial payment of \$15,000 toward the default on the property.

Kyle's bank officer then suggested he consider a loan modification, a revision of the defaulted loan that could help pay down past-due amounts by adding a portion of the delinquency to the current unpaid principal balance. But there were complications. Kyle's loan had been sold to another lender. His original bank no longer "owned" the loan. It was just acting as the servicing agency, or the entity that collects the payments owed on a mortgage on behalf of the lender or investor holding and owning the loan.

The modification plan that Kyle's bank suggested was well beyond the new lender's guidelines. The new lender indicated that because of the magnitude of the default, Kyle's best course would be to sell the property. His bank officer then went to bat for him, pointing out that Kyle had \$15,000 to put toward the default and that the property was well maintained. Fortunately, the investor agreed to give Kyle a second chance to save his home.

Kyle's bank then argued that it would be best for all parties if Kyle was put on a repayment plan through modification of his loan. Kyle would pay the \$15,000 as a down payment and would be responsible for 12 payments of his previous monthly amount plus an additional \$1,000. This would result in the delinquent amount being paid off after one year.

Kyle knew this additional amount would be hard to swing. The house was so important to him that he decided he could make some temporary lifestyle adjustments to afford it. He gave up his car, which was leased, and started taking public transportation. This immediately freed up \$450 a month. When his tenants in the downstairs apartment moved out, he took the opportunity to charge a higher rent to the subsequent renters. And he tightened his belt on other living expenses.

Kyle was relieved when he got the call to return to work. He called his bank officer to report that things were "looking up" and thank him for stepping in when he needed the help.

Commonsense Considerations

Throughout negotiations, Kyle's bank representative was able to point out to the new holder of his mortgage that prior to his financial crisis,

Kyle had been making consistent payments for several years, and it was likely that this pattern would continue.

If you are experiencing difficulties and find it hard to make your monthly mortgage payments, you should communicate the facts to your lender or the firm servicing your mortgage—the sooner the better. Extenuating circumstances might include unemployment or a job change that caused a decrease in your income, illness, divorce, or a recent death in your immediate family. Many lenders will appreciate that you contacted them and assist you based on their investor or insurer guidelines on your loan.

Here are some of the options that may allow you to keep your home:

- **FORBEARANCE**, which is a temporary suspension of payments to allow you to bring your account current, can be offered if your financial situation is temporary and you will be able to afford your mortgage payments in the near future.
- **REPAYMENT PLANS** suggested by the lender where you make more than one payment per month until the loan is brought current. For example, a payment plus $\frac{1}{4}$ more.
- **MODIFICATION**, or the elimination of past-due amounts by adding all or a portion of the delinquency to the current unpaid principal balance. Term extensions and interest rate adjustments may also be considered, when necessary, in order to create an affordable payment.
- **CLAIM ADVANCE**, if your loan includes mortgage insurance. The lender can determine if you qualify for a loan from your mortgage insurance company to bring the account current.

Letting Go to Stay Ahead

Annie and Carl had inherited Annie's grandmother's large, colonial-style house in the 1960s and raised six children in it. Along the way they had taken out a mortgage to provide the cash flow to finance upgrades, pay college tuitions, and provide tax relief. Carl retired from his job as a freelance sound recording engineer when he turned 65, and Annie took an early-retirement package 2 years later when the nonprofit company she

was working for underwent an internal reorganization. Both were quite involved in community and charitable endeavors and weren't really paying attention when interest rates started to creep up after several years of being relatively flat. Because interest rates were falling when they financed the house, they had signed up for an adjustable rate mortgage, which had been a smart financial move at the time.

One day when they were in the dining room paying bills, they noticed that their payments had jumped up by more than \$300 over the same month the year before. At the same time, the price of heating the house was going through the roof. Although they were quite conservative about keeping the thermostat low, the house was old and drafty and the heating system inefficient. They were genuinely shocked to open a bill for \$1,400 for a single month of natural gas.

Annie and Carl might have considered selling the house, even though it had been in the family for more than a century, but there was an added wrinkle. Their youngest son, Rickie, was a "boomerang baby" who had returned home after college and never left. He lived in a room they'd fixed up for him in the basement, working at a series of low-paying jobs that never seemed to last for more than a few months. If they sold the house and downsized, what would become of Rickie?

Everyone in the family, of course, had an opinion. Their eldest daughter was married to a commercial real estate developer who was convinced that the house could readily be broken up into condominiums and sold for a huge profit. Their next daughter, Amy, was deeply emotionally attached to the house and burst into tears any time the suggestion of selling arose. One son urged them to look into taking a second mortgage or line of credit, and another thought it might make sense to rent the property and move to Florida until interest rates settled down again. Rickie's twin brother, who was a paralegal, brought up the possibility of a reverse mortgage that sounded intriguing. He didn't know much about reverse mortgages other than you have to be at least age 62 to apply for one, but he thought the topic might be worth investigating.

Annie and Carl decided to educate themselves about reverse mortgages. They went to the library, where a research librarian helped them do an Internet search and showed them the section where personal finance books were shelved. Reverse mortgages, they found, come in

assorted shapes and sizes. But basically, a reverse mortgage is just what it sounds like—an inside-out mortgage.

With a regular mortgage, the bank advances you the money to purchase the house and you pay it back gradually over time. With a reverse mortgage, the bank pays you the value of the house, either in a lump sum or over time. Then you (or your estate) pays this back with interest at the end of the loan period. A reverse mortgage doesn't get you off the hook for paying for utility costs, such as heating and electricity, or property taxes, since you are still the owner of the house. As for the amount that can be advanced through a reverse mortgage, this depends on the value of the house and your age. Believe it or not, the amount you can get is greater the older you are. If you have a current mortgage, you can use the reverse mortgage money to pay it off or do this with other resources you may have, but you can't have both a conventional and a reverse mortgage.

Initially, this seemed like an attractive proposition to Annie and Carl. They liked the idea of the debt limit—that the amount of the loan could never exceed the value of the house. If real estate values crashed, it wouldn't be their problem—it was the bank's loss. And Rickie could stay put.

Then, a few clouds appeared that shed some rain on their plans. First, their son-in-law pointed out that it was his understanding that Annie and Carl could never add the name of one or any of their children (or anyone, for that matter) to the title of the house. That meant if they decided to take an extended trip or move to warmer environs for the winter and wanted to rent the house out in their absence, they might be considered in default. Under the terms of some reverse mortgages, they would have to stay put.

Annie and Carl needed a third-party opinion to help balance their options, so they called their accountant, Georgina. She asked them to try to set aside the emotional issues while evaluating the facts. How much would it cost them just to stay put? Annie and Carl were pretty sure that just keeping up with the mortgage would be an increasing struggle. What could they get for their house now? They said they believed that the house was worth more than it ever had been, but they were unsure that this value would hold. Right now it was in a good school district,

and this made the neighborhood particularly attractive to couples with young children. It was rapidly becoming clear that perhaps the best option was to sell the house and purchase a comfortable but more modest home, or even rent and use some of the proceeds to resettle Rickie in his own apartment.

When they explained this analysis to their children, they allowed each one to voice an opinion but stayed firm on their decision. Just as they were about to put the house on the market, Amy, their younger daughter, came forward. She had convinced her husband to relocate his business to her hometown, and the two of them were interested in buying the house “to keep it in the family.” While this pleased Annie and Carl, they told Amy that they were going to move ahead with their real estate agent to see what kind of price they could get for the house. They did not want Amy’s brothers and sister to think they had cut her a deal, so once there were some offers on the house, Annie and Carl would negotiate a price. If Amy and her husband didn’t want to meet that price, the house would be sold to the highest bidder.

Annie and Carl felt like they had made some monumental decisions, but firmly believed they had chosen the best options for themselves and their entire family. The last thing in the world they wanted was to lose their house to the bank through defaulting on their mortgage, and now they realized that sometimes to hang on, you’ve got to let go.

Commonsense Considerations

Annie and Carl considered their mortgage payment an important obligation, well worth their attention. Recognizing that your home is at once an asset, a liability, and an investment will pay in the end. Even if you do go into default, there are still options that your lender may allow you to explore. For instance:

- **SHORT SALES** occur if you can no longer afford your home and the property sales value is not sufficient to pay your loan in full. In a short sale, the lender may be able to accept less than the full payoff as settlement in full for the account.
- **LOAN ASSUMPTIONS** are another option. If you can find a qualified buyer

who would like to assume your mortgage loan, the lender may allow this transfer of ownership.

- DEED-IN LIEU is when you have had the property listed for sale at fair market value for 90 days with no activity. The lender can review the account to accept a “deed in lieu” of fulfillment of your mortgage obligation. If you qualify, the lender would agree to accept the property as settlement.
- See also Chapter 12, “Home Sweet Home Loans.”