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Mortgage Holders Find It Hard to Walk Away From Their Homes

By VIKAS BAJAJ

As American homeowners fall behind on their mortgages in growing numbers, bankers and policy makers worry that while many of these people cannot pay, some simply will not.

Millions of Americans are “upside down” on their mortgages — they owe more on their homes than their homes are worth. So far, however, there is little evidence that people who have the means to pay are walking away from their homes as values sink.

The blogosphere is full of tales of homeowners who supposedly are choosing to mail the house keys to their lenders rather than keep their depreciating homes. And yet “jingle mail,” the term for those tinkling packages of keys, appears to be far rarer than many seem to think.

Freddie Mac, the big government-sponsored mortgage company, estimates that just 0.14 percent of the defaulted mortgages in its portfolio involved properties that were abandoned by borrowers. Fannie Mae, another mortgage company, puts the figure in the single digits. Both companies deal in relatively conservative loans, so the total rate may be somewhat higher. Industry officials say they have no way of knowing for sure.

Even so, the idea that some people are simply refusing to pay their mortgages has gripped the popular imagination. The notion picked up momentum in the last few weeks after “Inside Edition,” the celebrity-focused TV news program, reported that Jose Canseco, the former American League most valuable player who made millions during his baseball career, abandoned his $2.5 million mansion outside Los Angeles to move into a smaller property.

“You look at the Jose Canseco issue and say that it’s a walkaway, but he is probably the only person on his block that did that,” said Robert Padgett, director of loss mitigation for Freddie Mac. “Those types of stories garner a lot of attention,” he added, but they are “isolated occurrences.”

Many economists agree. The low numbers from Freddie Mac and Fannie Mae are consistent with past housing busts, like the ones that occurred in Texas in the 1980s and in the Northeast and California in the early 1990s. Homeowners typically do not walk away from homes they live in unless they are unable to pay the mortgage, usually because of job loss, a death in the family, divorce or a big jump in their monthly payments. Real estate speculators, of course, do abandon properties when prices fall.

In fact, researchers say the rich are no more or less likely to walk away — “ruthlessly default” is the economic term for it — than those of more modest means. A person’s credit history is usually a better indication of how he will behave than his income. How much money a person put down on the house when he bought it also makes a difference.

Investors “are going to default right away because they have negative equity,” said Robert Van Order, an adjunct professor of finance at the University of Michigan. “But that’s different from people who moved into the house.”

Owners who live in their homes do tend to default more when home prices fall. That is because being under water leaves borrowers fewer options if they run into financial trouble. When prices are rising, borrowers can usually sell their houses for more than they paid or refinance their mortgages.

Most homeowners default when there is “an intersection of two events: they don’t have equity in their houses and they run into trouble,” said Mr. Van Order, a former chief economist at Freddie Mac.

An estimated 9 million American households, or 10.3 percent of all single-family homes, owe more than their home is worth, according to Moody’s Economy.com. By comparison, 4.8 percent of home loans were in foreclosure or delinquent by 60 days or more at the end of last year, according to the Mortgage Bankers Association.

For a variety of reasons, most homeowners find walking away difficult and expensive.

A foreclosure can make it hard for borrowers to get other loans and sometimes even an apartment. Economists refer to these as “transaction costs” that offset the benefit borrowers might get from defaulting on an underwater home loan.

Lenders can also pursue deficiency judgments against borrowers to recoup the difference between what is owed on the debt and what the property is sold for after foreclosure. Such claims are time-consuming and expensive to win, so most lenders do not pursue them. In the past, some lenders have sought judgments against a few borrowers to deter others from walking away, said Grant S. Nelson, an emeritus law professor at the University of California, Los Angeles.

In an attempt to reduce the incentive to default, Fannie Mae recently increased to five years, from four years, the time borrowers have to wait after a foreclosure to get another Fannie Mae loan. The company will make exceptions under extenuating circumstances.

The Bush administration has said that the only people who deserve housing relief are those who cannot pay, not those who will not pay.

“Let me also emphasize that any homeowner who can afford his mortgage payment but chooses to walk away from an underwater property is simply a speculator,” Treasury Secretary Henry M. Paulson Jr. said in late March. “Washington cannot create any new mortgage program to induce these speculators to continue to own these homes, unless someone else foots the bill.”

Nonetheless, some real estate professionals, particularly those in markets where home prices are falling fast, say borrowers who can pay may be tempted to walk away.

Brett Barry, a real estate agent in the Phoenix area, said some of his clients owe $100,000 more than their houses are worth. Single-family home prices have fallen 24 percent from their peak in the summer of 2006 in the region, according to the Standard & Poor’s Case-Shiller home price index, and the decline shows no sign of abating.

While some of Mr. Barry’s clients are having a hard time making payments, others who can afford to keep paying are also thinking about leaving because they worry their homes will be under water for many years to come.

“These markets are driven by psychology,” Mr. Barry said. “If people see that the market will continue to decline and they are already in the hole by 50 to 100 grand” they will leave.

One of his clients, a woman named Vivian, recently mailed the keys to her second home to the bank and walked away.

She and her husband bought the house outside Phoenix in 2004 in hopes of retiring there near one of their daughters. They put 20 percent down on the $240,000 house and at first made their payments without struggle.

But her husband, who was the primary income earner in the family, died suddenly last year from a staph infection. Vivian said she could no longer afford to keep paying the mortgage on two homes, because her only source of income now was a monthly Social Security check.

“I can’t sell it, I can’t pay for it,” said Vivian, 64, who spoke on the condition her surname not be used.

Though no two stories are exactly the same, such cases are not uncommon, housing specialists say.

The boom of recent years left many Americans financially vulnerable because they had borrowed too much against their homes, thinking prices would not go down. Others speculated by buying multiple homes. The housing and mortgage industries championed the notion that home prices had never declined nationally and that buying a home, even in a frenzied market, was always a good investment.

Jon Madux, a founder of the site YouWalkAway.com, which helps borrowers leave their homes, said a majority of the site’s clients default because of financial hardships. But in the Southwest and Florida, more of its customers are investors who bought multiple condos or houses and are now not able to find renters or sell for more than they owe.

The Mortgage Bankers Association estimated that the owners of 18 percent of the homes in foreclosure as of September 2007 did not live in those properties. Many used riskier loans, which are defaulting faster than more conventional mortgages.

Peter Chinloy, a real estate and finance professor at American University in Washington who has studied how borrowers behave when home prices fall, said policy makers should recognize that the problems are most severe in a few states in the Southwest, the Midwest and in Florida, and should aim relief in those places. It is also most severe for loans made between 2005 to 2007, when credit was at its easiest.

“One of the thing that has not gotten much attention,” he said, “is how localized the problem is.”

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