

[Print Page](#)

Hey, Neighbor, Did You Get Your Mortgage Reduced?

By [KELLY BENNETT](#)

Friday, Oct. 10, 2008 | Under a [settlement](#) struck this week to end deceptive lending lawsuits filed by 11 states, mortgage giant Countrywide Financial Corp. said it would modify 400,000 subprime and pay-option mortgages by lowering interest rates and payments. In some cases the bank plans to reduce the principal amount a borrower owes.

The idea is to stave off foreclosure by making a loan affordable for a borrower facing skyrocketing interest rates and payments. It could mean a borrower who paid \$500,000 two years ago now only owes \$300,000, based on a calculation of her income, indebtedness and a formula to make sure her housing-related expenses don't surpass 34 percent of her income.

When distressed homeowners sell for less than is owed on their mortgages or the bank forecloses on them for missing payments, those distressed sales drag prices down in neighborhoods. But unlike in a short sale or a foreclosure, the new "price" of a house with a loan modification might not be publicly recorded information. If it were, some housing experts say it could serve to depress property values even further. Others say the modified balances won't matter for figuring out a property's value.

Even if the loan modification terms were attached to a property's title, they wouldn't help an appraiser determine the value in a neighborhood. Real estate appraisers don't use loan information for neighboring homes to compile their appraisals of a property's value. They use transaction information from nearby comparable properties that have changed hands.

But if a prospective buyer could see to what level a handful of homeowners on a certain street had just negotiated their mortgages, that buyer's psychology could be altered and he might offer less for a nearby home than he would have otherwise.

The county recorder keeps public property records, including a house's transaction history and loan history. If a homebuyer has refinanced to take advantage of a rising housing market, the refinance amount is recorded. Real estate agents, housing websites and individual buyers use the information to track the performance of a particular neighborhood over time and to help them decide what a neighborhood's value is now. Some think it only makes sense for the modifications to show up in public record on the way down, too.

"You would think that should be a requirement because all the other ones are public record," said Fred Eckert, a local title representative with

Chicago Title. "If [a lender] records a modification, you have an accurate picture of what's happening with that property. If things weren't recorded, how would you know what's happening on the street?"

The concept of widespread loan modification amidst the foreclosure epidemic is new enough that the hows and whys of its implementation are not yet known. Unless a loan's balance is increasing, the lender isn't required to file a public change. Because the modification is between a lender and a private consumer on an existing loan, the lender is not legally required to attach news of the modification to the property record, experts said. In some cases, even when the balance is decreasing, lenders do attach a notice that the loan has been modified.

The question of whether or not the public should always know the details of a modification is contentious. Proponents hope loan modifications will keep people in their homes. Some hope they'll help stabilize property values for the neighborhood, too. Without the loan modification, that homeowner might succumb to foreclosure, adding another reduced-price repossessed house to a bulging stock of such properties. By keeping the details of those loan modifications private, the most recent transaction value of the property would be what the owner originally paid, not the new lower mortgage balance.

But that could leave consumers, homebuyers and housing professionals somewhat in the dark about the current value of a neighborhood.

Here's the underlying situation: A borrower might have paid \$600,000 for a house in 2005. Rather than foreclose on the home when the payments shoot up, that borrower might obtain a loan modification. But the borrower might never have been able to afford that house without the exotic loan to begin with. That happened thousands of times over, which contributed to the shocking rate of appreciation in home values this decade.

Now the bank is changing the terms of the loan, but not necessarily recording publicly the new loan balance. In many cases, that new loan balance will essentially be the price the borrower could've paid for the house to start with, if mortgage guidelines had stayed rooted in what a borrower could afford based on income. In many neighborhoods, the value of that house may have already fallen to \$400,000, even if the loan modification isn't recorded publicly.

During the boom, mortgages were made available with terms many borrowers would eventually not be able to afford as the loan matured. Those loans, with low introductory payments, helped to fuel the real estate frenzy here. House prices in the county shot up by 150 percent in five years. Even though prices are falling and foreclosures are piling up, the price of a house in the county is still 75 percent higher than it was in 2000, according to the Standard & Poor's Case-Shiller home price index.

In most neighborhoods where loan modifications will be applied under the Countrywide plan, foreclosures and short sales have already wreaked significant havoc on home values. But if loan modification is made available for borrowers in neighborhoods less affected by foreclosure, the neighborhood might better hide its distress from a potential homebuyer. That buyer could end up paying more for a house than he would otherwise, because his soon-to-be neighbors may appear in public records

to have a \$500,000 mortgage when really they've modified their balance to \$350,000.

A buyer looking for a house who is only privy to the most recent sales data would completely miss the modification that three homeowners on that street had been able to obtain. By obtaining such a modification, an owner is essentially achieving financing for a house at a level he can afford.

The loan modification program, at least the Countrywide settlement signed by state Attorney General Jerry Brown, aims to stabilize neighborhoods by not letting houses become abandoned magnets for vandalism. But this program doesn't exist to keep prices from falling further, said Deputy Attorney General Ben Diehl.

"The real estate market will set the fair market price," Diehl said. "It's not the attorney general's business to enter into a settlement either to inflate or deflate prices. It's the attorney general's business to step in and make a program and mitigate the foreclosures that came about because of the deceptive lending practices we alleged in our complaint."

Countrywide, now owned by Bank of America, isn't the only bank instituting a loan modification program. When the Federal Deposit Insurance Corp. took over IndyMac Bank after its failure this summer, it began a similar proactive loan modification plan for the troubled mortgages in IndyMac's portfolio. Advocates for loan modification hope that similar programs will be adopted on an even larger scale by the lenders that are left, either due to the fear of potential litigation like Countrywide or for a better bottom line like IndyMac.

Some real estate agents and appraisers said it doesn't matter if the loan modification is noted publicly or not. They argue that whatever forces are leaving borrowers upside down in their loans are already public -- general price declines, continuing foreclosures and distressed sales that are dragging prices down even more.

"Don't forget that prices are falling anyway," said Chris Thornberg, principal at Beacon Economics. "Stopping foreclosures only bails stupid people out. It doesn't stop prices from falling."

What matters, said real estate appraiser Todd Lackner, is that the program encourages people not to abandon their houses.

"I think that's the best news that the real estate market has had in a long time," he said. "Say you paid \$475,000 in 2006. You're saying right now, loan mod or let it go? It's worth 300 grand now. If they do that 300 grand loan modification they're more apt to stay."

Larry Buster, San Diego county manager for First American Title Company, said a sales price will be based on what someone's willing to pay for a house, regardless of whether loan modifications are public.

"The value is really based on what property is selling for, not how badly it's encumbered," Buster said. "If Countrywide is reducing the indebtedness, the test is still going to be what are people willing to pay for the property."

Please contact [Kelly Bennett](#) directly at

kelly.bennett@voiceofsandiego.org with your thoughts, ideas, personal stories or tips. Or set the tone of the debate with [a letter to the editor](#).

Close Window
