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Mortgage defaults rise but homeowners stay put

More Californians are missing their mortgage payments -- some deliberately -- but fewer are having their homes repossessed.

By William Heisel

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More Californians are failing to make their mortgage payments than at any time in the last 20 years, but fewer of them are losing their homes, according to new figures.

The dip in foreclosures follows moratoriums adopted by major banks and mortgage giants Fannie Mae and Freddie Mac. The increase in loan defaults, meanwhile, suggests that rising unemployment and the continuing recession are still claiming fresh victims.

But another factor in the soaring default rate could be that some struggling homeowners are purposely skipping their payments so that they can get their loans refinanced, industry experts say.

Lenders are so backlogged with requests to adjust loan terms that "they focus on the borrowers who already are circling the drain and ignore the people who are keeping up with their payments," said Jeff Lazerson, president of Mortgage Grader, a Laguna Niguel loan broker.

Lynne Neagle, 73, of Westminster may be a case in point.

Neagle said she and her husband had trouble paying their mortgage, but their loan servicer ignored their pleas to renegotiate terms -- until they quit paying, that is.

Suddenly, she said, they were presented with new ways to lower their payments and are currently negotiating new terms through the Hope Now program set up by the federal government and some of the country's largest mortgage lenders.

"Before we stopped making our payments, nobody wanted to deal with us," Neagle said. "We stopped paying, and that really got their attention."

A default notice is the first step in the foreclosure process, and California homeowners received 135,431 of them in the three months ended March 31, MDA DataQuick of San Diego said Wednesday.

That's an 80% increase over the previous three-month period and a 19% jump over the same period last year.

Meanwhile, the number of actual foreclosures, in which the home was repossessed by the lender, fell to 43,620 in the first quarter, a 6% drop from the last three months of 2008 and a 7.6% decline from the year-earlier quarter. Foreclosures peaked in the third quarter of 2008 at 79,511.

Much of the drop stems from a change in state law that made it more cumbersome for lenders to foreclose, DataQuick analysts said. That also led to procedural delays for banks and other lenders, which in many cases were not prepared to handle the additional paperwork.

"Some of these outlets weren't staffed enough to process all these loans, and so they had this huge backlog that we're starting to see work its way through," said Andrew LePage, a DataQuick analyst. "There's also a chunk of it that could be the lender pushing the borrowers into default to get the modification rolling or the borrowers doing it themselves to qualify."

Nationally, foreclosure numbers also have fallen.

Data firm RealtyTrac of Irvine said Wednesday that the number of homes taken over by banks dropped to 190,543 in the first three months of the year, a 13% decrease from the last three months of 2008. Defaults jumped 10% over the same period, to 306,785.

Late last year, the country's two biggest buyers of home loans -- Fannie Mae and Freddie Mac -- stopped foreclosures on many of the loans under their control. Citigroup Inc., JPMorgan Chase & Co., Bank of America Corp., Morgan Stanley and Wells Fargo & Co. all followed suit, saying they wanted to give President Obama time to work out the details of his housing plan.

Those moratoriums have tapered off. Fannie and Freddie announced at the beginning of April that they would begin foreclosing on homes again.

The various federal efforts now underway do offer some incentives for banks to help homeowners in default -- including a $1,000 payment to loan servicers for every successful loan modification.

But the incentives are even better for loans that are current -- $1,500 in those cases. And the centerpiece of Obama's plan, the Homeowner Affordability and Stability Program, is aimed at people who are current on their loans.

But many troubled borrowers in California are not eligible for help under Obama's plan because they owe much more on their loans than their homes are worth. To qualify for one of Obama's programs, a mortgage's balance must be no more than 105% of the value of the home.

"California loans are so far underwater that people won't fit into that narrow window," said David Leibowitz, a bankruptcy and foreclosure attorney at Lakelaw in Chicago.

With the unemployment rate -- now 8.5% nationally and 11.2% in California -- expected to continue rising, economists believe more people will be struggling to make their mortgage payments, leading to a continued uptick in defaults. But foreclosures won't necessarily follow the same trend, experts say, because banks don't want to overtax a housing market already flooded with cut-rate properties repossessed by lenders.

"If they can work something out with a borrower, they are going to try to work it out because they don't want to recognize these losses," said Steve Hable, a loan modification administrator who works for San Diego attorney and AM radio show host Jeff Isaac.Isaac has been holding seminars encouraging people to hire attorneys like himself to help them through the loan modification process. He said that when he meets with struggling borrowers, he finds that getting the bank's attention has been one of their biggest problems.

"There is so much confusion out there," Isaac said. "And people end up making really bad decisions, like borrowing against their 401(k) to make their house payments. You do that and you are destined for real misery down the road."

The demand for modifications has become so pressing that Bank of America, which services more home loans than any other company, said last week that it had 6,400 employees working on mortgage restructurings.

Neagle and her husband were close to paying off their home loan in the early 1990s when they decided to refinance and take out some equity to help pay for their son to study aerospace engineering at Cal Poly Pomona.

He earned his bachelor's degree in 1999, but the Neagles ended up with about $600,000 in debt and, as the housing market started to crash, a home that was worth only a little over $400,000.

They tried to talk with their loan servicer, American Servicing Co., which is part of Wells Fargo, about a modification but were rebuffed, said Neagle, who works for Wells Fargo as a collateral specialist in Irvine.

"I guess it's good that it didn't matter where I worked," she said. "It means they treat everyone the same."

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