NEWS ON FINANCING REALTY PROPERTY MANAGEMENT

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SPECIAL POINTS OF INTEREST:

- Shrink principal by 30%
- Borrower to have balloon payment
- Servicers encouraged to participate
- Balloon due at Sale or ReFi

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Loan Modification, a Sham?

The Obama Administration's endeavors towards Real Estate Recovery has taken many turns over the brief life of this administration. However, several of the attempts to remedy the problem seems to address symptoms rather than the root of the problem. The plan announced this month shows the desperation of these moves. After the Senate failed to pass the "Cramp Down" option, see our May 2009 issue ***"The Great Real Estate Swap Meet"*** here *http://www.washingtonreal.com/Newsletter*, the administration seems to be using a shovel to pick the debris, instead of an excavator.

Who really thought about this new one? In this iteration, the FHA seeks to reduce mortgage-related payments to 31% of monthly income. So far so good. The mortgage servicers or lenders can reduce the amount of principal on which the borrower must make loan payments by as much as 30% in order to get monthly payments to affordable levels. That sounds good, but here is the messier part, the borrower will keep making the reduced payments for the life of the loan, but is responsible for paying off the full loan amount when the home is re-financed or sold.

So let us put some numbers behind this scenario to "bring it to life" shall we say. If you bought the house in 2006 at $500,000 with a 6%, 30 years fully amortized interest rate, your payment will be $2997. If the house is now worth $250,000, within the purview of the program and based on FHA parameters, you could qualify for a modified loan based on this $250,000 as the new principal at a payment of $1,380 based on a 5.25%, 30 years fully amortized interest rate. But while your new neighbors who bought their home at $250,000, will owe nothing at the end of 30 years, supposing you keep the house for the duration of the loan, you will have a $250,000 balloon payment due. Interesting scenario, right? Which will be a better scenario, to let the lenders take immediate possession of the house, and jump back into the fray in twenty-four to thirty-six months, or hold on to thirty years? I can only imagine what you are thinking.

But while you were waiting on the sidelines, you missed the tax-related advantages of homeownership, especially if you lack avenues to reduce your tax obligations such as having children, but this is where your tax consultant comes in handy to look at your situation very closely and gives hopefully a sound advice on what next steps should be.

The proposal seems to me as similar to what is attainable at car dealerships, "what payment can you afford?". The main difference being that the government has already predetermined the answer for the borrower. Some in the industry are very reluctant advising their clients to take this new initiative seriously. As most borrowers who have faced the long wait times on loan modification phone calls will tell you, it is incredibly frustrating to deal with the inability of the loan servicers to be forthright in dealing with them. Why the government has failed in initiating a worthwhile process to address this problem is unfortunate, because until this issue is addressed head-on, the housing market will have several more summers to go in order to fully obliterate the problem, as many ARMs come due, their problems become due.

-Al Som-Anya, MBA, President