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From the Los Angeles Times

In mortgage market, 'walkaway' homeowners may be urban myth

Bankers and housing analysts say many homeowners, owing more than their homes are worth, are defaulting on their loans even when they can afford payments. But no hard numbers back up their claims.

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Bankers and housing market analysts are warning of a chilling new trend in the mortgage world: Homeowners voluntarily defaulting on their loans even though they can actually afford to make the payments.

It's known colloquially as "walking away," or more jocularly as "jingle mail," from the sound your house keys supposedly make when you mail them back to your bank.

It's a way of saying that Americans are beginning to apply a cold financial calculation to home ownership: When a home's value has fallen below what is owed on its mortgage, they feel it makes no sense to keep up the payments.

"That is going on, clearly, and there's lots of evidence of that in the market," Don Truslow, senior executive vice president of Wachovia Bank, said in a conference call with investors last month. A few weeks earlier, Treasury Secretary Henry M. Paulson had waggled a stern finger at homeowners contemplating walking away from affordable mortgages: Do that, and you're no better than a "speculator," he said.

Elsewhere, media reports and Internet postings are rife with stories about the trend and a supposed sea change in American attitudes toward debt. But there's a major problem with all this talk about the phenomenon of solvent homeowners "walking away": There doesn't appear to be any hard evidence that it's actually happening.

When pressed for the number of borrowers who could afford their mortgage payments, major banks and lender groups could not produce numbers figures.

Nor could the Mortgage Bankers Assn., the leading trade group for housing lenders. Spokesman John Mechem said he believed that walkaways by homeowners who could afford their payments were "becoming more prevalent." But he said that was based on "anecdotes we're hearing from our members and what we're reading in the newspapers."

Wachovia's Truslow acknowledged during the bank's conference call April 14 that walkaways were "hard to quantify." A bank spokesman said this week that "we have heard anecdotally that people are walking away" but that Wachovia had no hard numbers.

Bank of America Chairman and Chief Executive Kenneth Lewis, whose company is acquiring mortgage lender Countrywide Financial Corp., complained about "a change in social attitudes toward default" in an interview with the Wall Street Journal in December.

In response to questions from The Times, Bank of America spokesman Terry Francisco said the bank had seen indications that some homeowners were taking pains to keep their credit card accounts current at the expense of their mortgage balances, often by raiding their home equity lines to pay their cards, a reversal of traditional customary customer priorities.

But he said the bank did not have "firm figures" on how many homeowners were unnecessarily defaulting on their mortgages.

"We are working hard with our analytics to get at how much that is happening," Francisco said. Others suggest that it may be impossible to find out.

"How would you know what someone's true ability to pay would be?" asked Todd Sinai, an associate professor of real estate at the Wharton School of the University of Pennsylvania. "I'm not sure you could even come up with a definition."

At Fannie Mae, the government-chartered company that owns or guarantees billions of dollars in home mortgages, Senior Vice President Marianne Sullivan conceded that there was growing "folklore" about residential walkaways but said that the phenomenon was more likely connected to investors than people who live in their homes, or "owner-occupants."

"The vast majority of borrowers we find have been acting in good faith," she said. "If they get behind, they are interested in working with their lender."

Bruce Marks, CEO of Neighborhood Assistance Corp., a Boston-based nonprofit agency that helps strapped homeowners, says flat out that the notion that legions of borrowers are simply deciding not to pay is an "urban myth" that largely reflects the mortgage industry's desire to blame homeowners, rather than their lenders, for the surge in problem loans.

Marks and others assert that mortgage bankers have an incentive to blame the rise in delinquencies and foreclosures on borrowers skipping out on obligations they're financially able to meet, because that diverts attention from the lenders' own role in the mortgage crisis.

"So many of the loans made were irresponsible -- for the borrowers and for the lenders," said Kurt Eggert, an expert on predatory lending at Chapman University Law School in Orange County. "Lenders have an interest in painting themselves as responsible, even caring entities. They want to cast blame for the sub-prime meltdown as much as possible on their borrowers."

It is generally agreed that the real culprit in the meltdown is the proliferation of exotic mortgages that hit borrowers -- many with paltry down payments and therefore almost no equity in the home -- with huge payment shocks in the early years of the loan. The new payments are often raised to levels that the borrowers could never have afforded but expected to escape via a refinancing or a sale of the house into a rising market.

When home values fell instead, their exit strategy evaporated. But that does not necessarily mean that they can afford to keep paying.

"Who do you see walking? They're people whose rate is about to reset and they see no way out," Marks said. "People who have a fixed-rate mortgage that was initially affordable and continues to be affordable don't walk away from their home, even when it's underwater. They are always willing to withstand the ups and downs of the housing market if their payments remain affordable."

Experts say some supposed owner-occupants who are "walking away" may in fact be speculators in disguise: buyers who acquired properties as investments to resell for a fast profit. Investors, unlike genuine homeowners, will treat their purchases strictly as economic transactions; their decisions to abandon payments shouldn't be seen as a sign that American homeowners no longer feel obligated to pay their debts, says Stuart Gabriel, director of the Ziman Center for Real Estate at UCLA's Anderson School of Management.

"A number of [foreclosed] properties are actually investor-owned, not owner-occupied, and we have to be careful that we're not attributing to homeowners the actions of investors," Gabriel said.

Sinai of the Wharton school points out that homeowners have long been known to do whatever it takes to avoid foreclosure -- they're concerned with maintaining their credit ratings and building equity in their homes, and are typically invested not only in their property but in their communities.

Historically, owner-occupants didn't default on their mortgages except in a handful of extraordinary situations, such as death, divorce, illness or job loss. Their predictable behavior helped keep mortgage rates low.

"If it's correct that there's a change in behavior, all the default and credit risk models will have to be recalibrated," Gabriel said. But he added: "I have not seen one shred of data that conclusively or systematically speaks to that point." On the contrary, analyses of the most troubled segments of the mortgage markets suggest that the problem is still rooted in borrowers' financial distress rather than their cynicism.

In a survey issued this week of Alt-A mortgages originated in 2006 and 2007 -- these are nonstandard mortgages often marketed to buyers with less-than-prime credit -- Fitch Inc. analysts found that a rise in delinquencies could still be traced to "borrowers who purchased a home they could not afford or those engaged in mortgage fraud for the purpose of property speculation." Legitimate homeowners, the analysts said, "rarely view the home as a short-term investment ... they do not default based solely on a drop in value."

Fitch has also found a high level of misrepresentation in loan applications "by borrowers, brokers, and other parties." When Fitch analysts subjected 45 sub-prime loans to detailed examination late last year, they found "the appearance of fraud or misrepresentation in almost every file," a situation they termed "disconcerting at best" in a report in November.

Some 66% involved "occupancy fraud" -- that is, the borrower misrepresented his or her intention to live in the home, rather than to buy it as an investment. That finding underscores the possibility that bankers are blaming owner-occupants for the more common, and not unexpected, phenomenon of "walking away" by real estate investors.

One source of walkaway "folklore" may be services that purport to help homeowners skip out on their mortgages without long-term harm to their credit ratings. Among them is San Diego-based You Walk Away, which launched a website in January offering to help homeowners "unshackle yourself from a losing investment and ... Walk Away."

Co-founder Jon Maddux acknowledged in an interview, however, that the firm's typical clients are people facing genuine financial stress, whether because they cannot make their current mortgage payments or know that an upcoming raise in their interest rate will make default all but inevitable.

"We do have a lot of people who cry to us on the phone," he said. "They're under stress and don't know what to do. A lot of these people should never have got the house."

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