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Banks Paying Homeowners a Bonus to Avoid Foreclosures: Mortgages

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Bloomberg

Accelerating efforts to move troubled mortgages off their books, banks are offering as much as $35,000 or more in cash to delinquent homeowners to sell their properties for less than they owe.

In the past, lenders routinely delayed or blocked such transactions, known as short sales, in which they accept less from a buyer than the seller's outstanding loan. Now banks have decided the deals are faster and less costly than foreclosures, which have slowed in response to regulatory probes of abusive practices.

As a result, banks are nudging potential sellers by pre-approving deals, streamlining the closing process, forgoing their right to pursue unpaid debt and in some cases providing large cash incentives, said Bill Fricke, senior credit officer for Moody's Investors Service in New York.

Losses for lenders are about 15 percent lower on the sales than on foreclosures, which can take years to complete while taxes and legal, maintenance and other costs accumulate, according to Moody's. The deals accounted for 33 percent of financially distressed transactions in November, up from 24 percent a year earlier, said CoreLogic Inc., a Santa Ana, California-based real estate information company.

Karen Farley hadn't made a mortgage payment in a year when she got what looked like a form letter from her lender.

"You could sell your home, owe nothing more on your mortgage and get $30,000," JPMorgan Chase & Co. said in the Aug. 17 letter obtained by Bloomberg News.

Farley, whose home construction lending business dried up after the housing crash, said the New York-based bank agreed to let her sell her San Marcos, California, home for $592,000 — about $200,000 less than what she owes. The $30,000 will cover moving costs and the rental deposit for her next home. Farley, who is also approved for an additional $3,000 through a federal incentive program, is scheduled to close the deal Feb. 10.

Tom Kelly, a JPMorgan spokesman, declined to comment on the company's incentives.

"When a modification is not possible, a short sale produces a better and faster result for the homeowner, the investor and the community than a foreclosure," he said in an e-mail.

A mountain of pending repossessions is holding back a recovery in the housing market, where prices have fallen for six straight years, and damping economic growth. Owners of more than 14 million homes are in foreclosure, behind on their mortgages or owe more than their properties are worth, said RealtyTrac Inc., a property-data company in Irvine, California.

Short sales represented 9 percent of all U.S. residential transactions in November, the most recent month for which data is available, up from 2 percent in January 2008, according to Corelogic. Bank-owned foreclosures and short sales sold at a discount of 34 percent to non-distressed properties in the third quarter, according to RealtyTrac.

As lenders shift their focus to sales, they are finding that some borrowers would rather risk repossession while they wait for a loan modification, according to Guy Cecala, publisher of Inside Mortgage Finance, a trade journal. In a loan modification, the monthly payment, and sometimes principal, is reduced to help prevent seizure. Homeowners facing foreclosure may live rent-free for years before they are forced out.

“That’s why the banks have got to pay the big bucks,” Cecala said. While JPMorgan is giving the largest incentive payments, other banks and mortgage investors are also offering them, according to interviews with 12 real estate agents in Arizona, California, Florida, New York and Washington. Lenders also provide incentives on loans they service and don’t own when the mortgage investor, such as a hedge fund, requests it.

Borrowers also can receive payments from the federal government’s Home Affordable Foreclosure Alternatives program, which in 2010 began offering as much as $1,500 to servicers, $2,000 to investors and $3,000 to homeowners who complete short sales.

For banks, approving a sale for less than is owned on the home can cut a year or more off the time it takes to unload a property. From listing to sale, the transactions took about 123 days on average at the end of last year, according to the Campbell/Inside Mortgage Finance HousingPulse Tracking Survey. Lenders spend an average of 348 days to foreclose in the U.S. and an additional 175 days to sell the property, according to RealtyTrac.