Can Debtors Afford MORTGAGE-MODIFICATION PROGRAMS?

BY IGOR ROITBURG, MANAGING DIRECTOR, STRETTO &
ROBERT M. GELLER, ATTORNEY, THE LAW OFFICES OF ROBERT M. GELLER

As more bankruptcy courts consider adopting mortgage-modification programs, one frequently-asked-question is whether a distressed homeowner can afford to pay for such a program. Some look at the additional out-of-pocket expenses and reflexively conclude that debtors "cannot afford" to participate. Such an approach, however, is myopic and ignores the savings debtors achieve as well as the costs they incur when a mortgage-modification program is not utilized or available—i.e., the "cost of doing nothing."

COMPARING MORTGAGE PAYMENTS—TRADITIONAL CHAPTER 13 VS. MODIFIED

In a traditional Chapter 13, a debtor is required to pay their post-petition mortgage payment plus their arrears over the life of the plan. Assuming an average borrower with a $300,000 mortgage and $20,000 in arrears, the debtor can expect to pay about $2,133 per month to keep their home in a traditional Chapter 13 plan. On the other hand, the same debtor can expect to pay about $1,450.00 *towards* their mortgage if it is modified—a savings of $683 per month.

The savings are even more pronounced when viewed over the life of the plan. While it will typically take the debtor just a little more than three months to recoup their out-of-pocket program expenses, they will save more than $40,000 as compared to a traditional Chapter 13 plan. It is a win-win for the debtor.

THE SUCCESS OF MORTGAGE-MODIFICATION PROGRAMS

Of course, spending any money on a program only makes sense if the program offers something the debtor cannot achieve without the program. Bankruptcy court-based mortgage-modification programs have traditionally reported success rates of about 70%. On the other hand, while many consider Chapter 13 to be a "save your home" procedure, a Harvard Business Law Review study found that nearly 75% of Chapter 13 debtors lost their homes to foreclosure within three years of filing Chapter 13[1]. In other words, not only are modification programs significantly better at reducing the debtor's mortgage costs, but they are also more effective in allowing the debtor to save their home over the life of the Chapter 13 plan.

HIDDEN FORECLOSURE COSTS

When a family loses their home to foreclosure, they're not only affected by the actual displacement. Every aspect of their financial lives is affected, from increased future borrowing costs to housing affordability struggles. A foreclosure on one's credit report means higher borrowing costs. This includes credit card and auto loans that could potentially increase up to 10% in higher interest rates, and mortgage rates with up to 3% higher interest rates. Insurance premiums could potentially double and any new rent agreements will likely require higher security deposits not to mention the cost of moving itself. Furthermore, if the debtor plans to purchase a new home in the future, they may face up a seven-year waiting period to secure a new home mortgage following a foreclosure. These amounts are estimated to be in the tens of thousands for debtors.

In addition to these quantifiable costs, the absence of a mortgage modification could increase the likelihood of the failure of Chapter 13 proceedings, which can have a cascading effect on all involved parties when the debtor defaults on their obligations.

COVERING EXPENSES OVER THE LIFE OF THE BANKRUPTCY PLAN

As noted above, a mortgage modification clearly reduces the monthly payment for the debtor in the Chapter 13 plan. Concerns about the cost of obtaining the modification should also be discounted. Most modification programs inside of a Chapter 13 bankruptcy allow attorney's fees to be paid over the 60-month plan payment. With average legal fees ranging from $1800 to $2500, these fees can be spread out so that the debtor is only paying $30 per month—a relatively minor expense compared to the savings achieved.

MORTGAGE-MODIFICATION PROGRAMS SAVE HOMES AND MONEY

While the initial cost to participate in a mortgage-modification program may seem expensive for a distressed homeowner, it is an investment worth making to save money and avert even greater financial burdens down the road. As legal professionals guide their clients through the labyrinth of decisions to resolve their home-mortgage debt obligations, the potential cost savings of a home-mortgage modification and the hidden cost of doing without one should be evaluated to ensure clients can stay in their homes without sacrificing a sustainable and healthy financial future. ■

FOOTNOTE

1. Joshua Boehm, *Chapter 13 Debtors' Home Loss in the Foreclosure Crisis*, Harvard Business Law Review, 2013 Vol 3 at 185.

BANKRX/SHUTTERSTOCK.COM