Case 12

"Running Away from Home"

Andrea felt as if she had reached the Promised Land when she unlocked the door to her new house for the first time in 2006. The bungalow in Kings Beach, a small California town on the north shore of Lake Tahoe, meant she no longer had to commute over the Mount Rose Summit (8,911 feet) to her job in Incline Village. Sure, she reasoned, she was now spending close to 50% of her income on her mortgage, property taxes and homeowners insurance, but her commuting costs had dropped significantly and the singular location of her home protected her from taking a loss when it was time to sell. In addition, her home, and those surrounding it, had deed restrictions that prohibited renting. Just another hedge against falling home prices, she reasoned.

Four years later, just after New Years 2010, it was time to move back over the Carson Range for graduate school. So Andrea listed her home for sale "by owner" for a modest 6% over what she bought it for in 2006 ($411,300). After all, the economy had soured in the interim so she couldn't expect the kind of appreciation others experienced earlier in the decade. After her property listing generated little interest, she sought the help of an appraiser and learned to her dismay that her home was probably worth only $288,000. The housing bubble had indeed burst everywhere.

"Options, options, options," Andrea thought, panicked. According to her calculations it would be 2025 before she could sell her home for what she paid for it. Or maybe 2035. Andrea first tried to have the renting restrictions removed from her deed. This, she soon learned, was a long and expensive process with very little likelihood of success. Deed restrictions are valuable precisely because they run with the land in perpetuity.

Andrea's friends all advised her simply to walk away from her home, since California is a non-recourse mortgage state. Essentially, these states prohibit deficiency judgments–a judgment against a debtor when a foreclosed home does not sell for enough at auction to pay the mortgage in full. There are 12 non-recourse mortgage states. These are commonly known as jingle mail states because the borrower can effectively void an obligation to pay a mortgage by placing the keys to the property (the jingle) in the mail to the lender.

Jingle mail sounded like the way out, but it troubled Andrea. After all, her mortgage was a promissory note–a written promise to repay a loan under specific terms. Since the lender didn't violate those terms and she had the means to make her mortgage payments, how could she justify breaking such a promise?

Andrea's Dad suggested a short sale, where she would negotiate with the lender to sell her home at a price lower than the outstanding principal on her mortgage, and the lender would accept the sale proceeds to settle her debt. This seemed like a reasonable solution to Andrea; unfortunately her lender didn't agree. The risk management officer at the bank explained that they would not begin negotiations on a short sale until she was at least six months in arrears. This, too, was essentially a broken promise (not paying her mortgage), but she seemed to get permission from the bank for doing so.

After six months of not paying her mortgage, Andrea had saved a considerable sum (over $13,000) and now lives "rent-free" with impunity. The bank still refuses to negotiate, yet isn't in any hurry to foreclose and evict Andrea. "Am I doing the right thing?" Andrea wonders. "When did figuring out the right thing become so hard?"

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