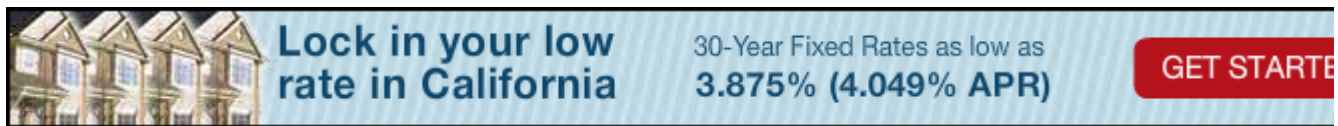


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What Happens When You Walk Away From Your Home?



By Chris Taylor | Reuters – Mon, Jan 30, 2012 4:43 PM EST

It was just last summer that Charlotte Perkins made the hardest decision of her life as she was caught in the vise of the housing bust.

Wanting to downsize their lives as they headed toward retirement, they bought a new home and sold the old one, also in Mesa. Their previous home had been appraised at nearly \$400,000, but as the housing crisis ravaged Arizona, they were told they'd be lucky to get \$200,000.

"They were carrying a loan of \$260,000 on their original home alone, meaning they were carrying more than it was worth. Combined with the mortgage on the new house, their housing payments were around our necks," she says, threatening to gobble up all their retirement savings and leave them with nothing.

The couple made a difficult call: They would do a 'strategic default,' and simply stop paying the mortgage. "I had to wrestle with it," said Perkins, 60. "We had worked all of our lives to build good schools for our children and good people. But it came down to, 'Can we keep doing this?' We had to say 'No.'"

As the housing bust drags on, many homeowners are thinking like Perkins. Almost 11 million homeowners are behind on their mortgage payments, says financial information provider CoreLogic. Around 3.5 million homeowners are behind on their mortgage payments. 1.5 million homes are already in the foreclosure process, according to online marketplace Zillow.

As banks start to work through their backlog of distressed properties, the New York Federal Reserve estimates that 1.5 million foreclosures will take place during the next couple of years.

So, the question is: Does it make sense to keep paying a massive mortgage, knowing that the house is worth less than the loan?

home regains its prior value? Or is that akin to - as columnist James Surowiecki recently "setting a pile of money on fire every month"?

"I constantly get the saddest e-mails from people saying, 'I've exhausted all my life saving now I have to default,'" said Jon Maddux, CEO of YouWalkAway.com,

a foreclosure agency that helps clients with strategic default (and charges a fee for it). "I the wall a couple of years earlier, stopped paying the mortgage and stayed in the home I would be in a much better financial position."

Moral Quandary

There's a moral component to that decision, of course. People naturally feel embarrassed not paying their bills; no one wants to be branded a deadbeat. But remember that comp when it makes financial sense for them to do so, via the bankruptcy process. Even the M in a flourish of irony, arranged for a short sale of its Washington headquarters.

It's not personal; it's business. So think of strategic default as a business decision, and c of whether it makes sense for you, advises Carl Archer, an attorney with Maselli Warrer

[Also see: [Small Money Missteps That Can Cost You Big](#)]

"People think it reflects on their integrity, and say 'I wasn't raised this way,'" said Arche attitude is to say that there's a contract, there are penalties for violating that contract, a financial sense to break it."

The penalties largely revolve around your credit record, which admittedly gets blown up you can likely forget about qualifying for a mortgage or a car loan. When lenders are rea you'll have to pay for the privilege, with stiff interest rates due to your default history.

What Happens to Scores

Charlotte Perkins watched her credit score go from a pristine 800 to 685, dropping even

Credit-scoring firm FICO estimates that someone with a 680 score would see that number drop after a strategic default, and someone with 780 could crater 140-160 points.

Not desirable, of course, but not the end of the world either. For Perkins, for instance, she had to refinance her mortgage on her new house, before she even started the default process on her credit cards since, in terms of limits or interest rates.

Now that the previous home was auctioned off in December, she can start slowly rebuilding her credit. It should take about seven years.

Strategic default isn't a decision to be taken lightly, of course. If everyone did it, the housing market would be in much worse shape than they already are.

The following are some of the issues to keep in mind:

1. Look to it as a last resort, not a first option. Your financial troubles could be alleviated, especially since 30-year mortgage rates are near record lows of below 4 percent. If the bank forecloses on your loan, look into the number of government programs designed to keep you in your home. Visit MakingHomeAffordable.gov.

2. Location, location, location. Each state has its own rules and regulations regarding the length of the process and what you could be liable for in the end. In so-called 'non-recourse' states like California and Texas, a lender cannot come after you for any deficiency (for instance, if they're only able to sell the property for \$200,000). In other states they can pursue the deficiency. Some homeowners opt to file for bankruptcy, to free themselves from those potential obligations.

3. Use the interim to save like a demon. If you're in a state like New York or Florida, where you can't walk away from every foreclosure, it might be a couple of years before you actually have to pack up. In the meantime, be disciplined about stockpiling cash. That will help you with a down payment for a rental, or to clear up other debts you might have. "Save money as if you were still paying the mortgage. If you don't, then you'll run out of both time and money, and then you'll be in a real tough spot."

4. Know the tax implications. Historically, if you have a debt that's forgiven, the canceled debt is considered income.

taxable by the IRS. In the wake of the housing bust, though, the Mortgage Forgiveness L
spare you those taxes. That legislation expires at the end of 2012, though - so if it's not e
face a tax bill for the difference.

5. Talk to a professional. A bankruptcy or real-estate attorney can help you through
Association of Consumer Bankruptcy Attorneys, for instance, has a searchable database

"Strategic default is not an easy decision, and there's a cost either way," said Gerri Detw
education for Credit.com. "Would you rather be \$200,000 underwater, or would you ra
your credit report? It depends whether you're finally at the point where enough is enou

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