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Prime Borrowers Beware - The Foreclosure Crisis is Spreading

If you are a home owner with a prime rate mortgage, you may have passed over news about mounting problems in the subprime market, assuming those troubles had nothing to do with you. Unfortunately some of the latest market research is pointing to a spillover effect into the prime mortgage market, revealing that many prime borrowers, especially those with second mortgages or home equity loans, may be at risk of defaulting on those second liens.

Indeed this newest foreclosure problem seems to lie with those took on “second-lien loans” during the past few years. (A lien is a claim on a property. First mortgages hold a first lien on homes, meaning the first mortgage lenders have first claim on the house if the borrower goes into foreclosure. Any secondary liens must try to recover losses from the property after the first lender has already collected his due.) Many home buyers even with good credit resorted to taking out second mortgages on top of their first mortgages in order to get into a home with little or no down payment. This was especially true of those buying in real estate hot spots like California and Florida where rapidly rising home prices made traditional mortgage borrowing impossible for middle- to low-income buyers. Now that market conditions have turned, man y of these borrowers are finding it hard to keep with both home loans.

Even many of those who were able to get into homes with more conventional means have since turned to home equity loans or home equity lines of credit to help pay off their costly first mortgages. “Unable to afford their own homes, [borrowers] turned to increasingly risky mortgage products,” said House Representative Amy Klobuchar (D-Minnesota), Wednesday before a hearing of the Joint Economic Committee looking at the national foreclosure crisis. These “risky mortgage products” included second lien loans with adjustable interest rates. Now that market rates gave been rising for the past several months, those secondary loans are becoming increasingly pricey for homebuyers already stretched to their financial limits.

These prime rate borrower struggles are having a real effect on the mortgage market. Countrywide Financial, for example, the nation’s largest mortgage lender, announced Tuesday that it saw a major profit loss (a 33 percent drop from the first quarter) during the last quarter as a result of the rise in late payments and foreclosures on second lien loans. Borrowers with two loan commitments tend to let the secondary loan lapse before defaulting on the primary mortgage, as has been reflected by current foreclosure data.

So, if you have found yourself in this boat, what should you do to avoid foreclosure on either of your loans? One of the most popular options is to refinance both mortgages into just one home loan, hopefully reducing the total interest and monthly payments. Another option, however less appealing, is to sell the home to recover some profit before losing it all in foreclosure proceedings. And at the very least, you should be in close contact with both of your mortgage lenders. Let them know the extent of your financial straits. Most will be willing to work with you to arrange a modified payment schedule until you can resume the regular one; they also want to avoid foreclosure at almost any cost. If you are having difficulty paying both your primary and second mortgage or home equity loan, the key is to act immediately to remedy the situation before you end up as just one of the sad prime mortgage foreclosure statistics.