Suicide Loans: Piggyback Mortgages Default by up to 50%

by PR Newswire

"This is precisely what I have been warning the public about. It's the first sign of the tsunami of defaults and foreclosures that are coming," cautions Consumer Advocate and International Mortgage Reduction Expert, Harj Gill.

Gill, who is also the Founder, President and CEO of American Mortgage Educators, Inc., has been on a one-man crusade warning homeowners of the risks associated with exotic mortgages and urging them to take immediate action to avoid going into default.

According to Gill, piggyback mortgages, which are a combination of two loans packaged together and closed simultaneously, represent just one of many non-traditional mortgages that have put homeowners at risk of losing their homes.

Typically for people with little or no down payment, the amount for the first mortgage is set so it does not exceed 80% of the home's value. This allows the borrower to avoid paying Mortgage Insurance (MI). The remaining loan amount is financed as a second mortgage by way of a Home Equity Loan or a Home Equity Line of Credit (HELOC) and "piggybacked" onto the first.

"I have always said this is a good solution to avoid MI, but a terrible long term strategy," said Gill.

Gill's assertion is supported by the latest analysis by Standard & Poor's, an influential Wall Street ratings agency, which analyzed nearly 640,000 piggyback first-lien mortgages in bond pools. S&P discovered that first-lien mortgages connected with piggyback loans are 43% more likely to go into default than stand-alone first mortgages of comparable size. The default rate increases to a whopping 50% for borrowers with a FICO credit score of 660 or less.

According to SMR Research, lenders and mortgage brokers whose commissions are based on loan size, have aggressively promoted these loans because the first-lien portion of piggybacks tends to be larger than standard first mortgages.

Gill warns that borrowers with these loans should be ultra concerned because they are concentrated in metropolitan areas with the greatest risk of experiencing a fall in housing prices.

"If borrowers start to go into default in a declining property market, they will be committing financial suicide by having their credit destroyed and still being burdened with a debt well after they lose their homes," said Gill.

A 2005 SMR Research study confirmed that many of the largest U.S. counties in population and mortgage market size have huge portions of home loans as piggybacks, some by as much as 62%. These include California, Washington, Colorado, Virginia, Arizona, Nevada, Oregon, Illinois, Georgia, Massachusetts, North Carolina, Utah, Florida, Texas, and Missouri.

The danger, according to Gill, is that unlike standard mortgages with fixed-interest rates, borrowers with adjustable rate piggybacks are not prepared for rate hikes that increase their payments.

Gill's recommendation is for borrowers to immediately reduce their interest payments and get a forecasting tool to determine the critical interest rate at which they are likely to go into default.

He says those with HELOCs can use a little known Banking Principle to reduce their interest payments.

"Interest on your HELOC is calculated on the Daily Balance. So instead of having your income sitting in a checking account earning no interest, borrowers should 'park' those funds in their HELOC to immediately reduce the daily balance and thereby reduce the amount of interest they pay," advised Gill.

Of course borrowers need to ensure they have a HELOC with the right features and proper setup to take advantage of this strategy. For those without a HELOC, Gill recommends refinancing the second mortgage into one with features that enables this.

"By asking the right questions, you should be able to refinance the second mortgage at almost no cost," advises Gill.

To assist borrowers, he has prepared a Critical Report explaining how to apply this strategy and refinance the second mortgage on his Consumer Information Center www.MortgageFreeUSA.com

"I expect every mortgage broker, loan officer, lender and real estate agent that knowingly put a client into a piggyback mortgage to contact them and tell them to read this Critical Report," said Gill.

"Not doing this truly shows that you were only in it for the money and not to help your clients."