Many go bust in mortgage meltdown

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The mortgage crisis that sparked a wave of foreclosures is now responsible for a rising tide of bankruptcies across the city.

Fueled in large part by the number of homeowners who could not keep up with monthly payments on subprime loans, 14,407 people filed for bankruptcy in the New York area during the first seven months of this year, compared with 11,026 in that period last year, according to bankruptcy court records.

While the number of bankruptcies is not as high as it was during the previous economic downturn in 2001, the filings this time around are increasing at a greater rate, rising 31% from January through July versus the year-earlier period.

"I've never seen it this bad," says Gregory Messer, a Brooklyn bankruptcy attorney. "There were times where there were more bankruptcies, but I don't know if I've ever seen so many people prepared to walk away from their houses."

Bankruptcies are typically prompted by catastrophic events such as accidents, illnesses or divorce. The latest wave is different because the driving force is the mortgage crisis. Hit with monthly payments on subprime loans that suddenly increased by hundreds of dollars or more, many New Yorkers, already squeezed by rising gas and food prices, maxed out their credit cards in order to meet their obligations.

Some have given up completely—even if it means losing their homes—to get out from under their debts. Others hope to keep their homes while reorganizing their finances.

In the past, in stronger housing markets, homeowners could refinance their homes. But now, the value of a debtor's house is often less than the amount of the mortgage.

"Because of these no-income-verification, no-asset loan products that were popular, people have no equity and never did," says Michael Siegel, a Manhattan bankruptcy attorney. "Even in the real estate downturn in the '90s, you didn't have people with no equity in their homes."

Real estate speculators

Some New Yorkers find themselves mired in debt because the wide availability of credit turned average wage earners into eager real estate speculators. They bought investment properties in the suburbs, or in places like Florida and North Carolina, hoping to get rich. Then mortgages adjusted upward or their tenants, hit by the economic downturn, stopped paying rent. And the real estate bubble burst, sending home values spiraling downward, particularly outside of the city.

Noel, a 28-year-old math teacher from Harlem who asked that his last name not be used, always thought it would be smart to invest in real estate. So when his cousin introduced him to a mortgage broker who promised he wouldn't have to put a penny down on a $1 million piece of property in New Rochelle, he jumped at the chance. Then, the same broker told him about a home in Yonkers. Again, he didn't have to put any money down.

In over his head

Before he realized what he was getting into, Noel says, he was scammed into signing two mortgages totaling more than $1.5 million. The mortgage broker even provided a lawyer for the closing.

"I make $50,000 as a schoolteacher," he says. "There's no way I should have been approved for loans that big."

Hemmed in by monthly payments totaling more than $10,000 and bills for maintaining a third property on Long Island, Noel had no choice but to file for bankruptcy, he says. He filed without the help of a lawyer—he couldn't afford one—and he plans to walk away from the three homes and get a fresh start, this time without dreams of making it big.

"I thought real estate was a good business," he says. "But I guess it's not for me. I'm not buying property again—ever again."

The rising number of bankruptcies certainly won't help the economy.

Jay Fleischman, a Brooklyn bankruptcy lawyer, says his clients are completely tapped out.

"People will eat out less, buy fewer flat-screen TVs, take fewer vacations," he says. "I've seen so many people just tightening their belts to the absolute limit. There's simply no disposable income for a lot of people anymore."

With more mortgages due to adjust upward in 2009 and 2010, credit card companies reducing limits, and Wall Street layoffs certain to rise, bankruptcy filings will surely increase, experts say.

"I really think things are going to get a lot worse before we see any light at the end of this tunnel," Mr. Fleischman says.

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