After foreclosure or short-sale: How long until you can buy again?

Walking away from a mortgage you can still afford to pay has consequences; everyone knows that. It's almost certain that your credit score will suffer, perhaps significantly and it could be a long time before you can qualify for another home loan.

Some homeowners believe that the credit score hit is worth getting out from a deeply underwater mortgage. They may owe, say, $500,000 when their house is only valued at $350,000. And, they figure, there's no way it will ever be worth what they owe so it's better to be a 'walkaway', to get out from underneath the burden and sell the home on a 'short sale' or let it go to foreclosure.

What might be the challenges if they want to eventually finance another home purchase? Credit scores will clearly be impacted by a foreclosure or a short sale, but they are only one component of a complete credit decision. By themselves, they are not a good indicator of a borrower's willingness to continue to pay their mortgage.

What's the impact on credit scores from different events?

The three credit rating agencies do not publicize the impact on credit scores but the best estimates we have are as follows:

- **One 30 day late = 10-110 points**
- **One 90 day late = 70-135 points**
- **Short Sale, Foreclosure or Deed-In-Lieu = 130-240**

In the future, loan underwriters, those who analyze risk and determine if the lender should grant a loan, will have to make some judgment decisions about whether borrowers who defaulted did so due to economic hardship, such as a job loss or divorce, or whether they were 'walkaways', who made the strategic decision to not pay their mortgage even though they had the ability to pay.

They will likely scrutinize their records very closely and, if they find no precipitating factors leading to the defaults, such as job loss or health issues, a higher credit score, even if repaired, might not overshadow the black mark of a ‘walkaway’.

Lenders may be far more lenient and approve a loan within two to five years for those who experienced economic hardship, compared to seven or eight years before the ‘walkaways’ can get a new loan. In addition to credit scores, several factors are analyzed, such as the amount of money borrowers have in the bank, employment history and payment history.

But, that said, it'll likely not be impossible to get a loan, because banks will still be in the business of making loans and collecting interest payments, so they might be willing to gamble with a ‘walkaway’. It might be a little more difficult to get the loan, but the drive to profit from making loans may very well trump caution.

It's hard enough to foresee the state of mortgage lending six or seven months from now, let alone seven or eight years from now. It’s very possible that lenders may look at applications from one-time strategic defaulters and say, "Yes, they walked away but it's a whole different market now."

They might not approve a loan with the lowest possible down payment, but they might make a loan with a larger down payment, perhaps 20% or more, because the lender’s risk is lower with a larger down payment. Another alternative is that, other things being equal, lenders might charge ‘walkaways’ a slightly higher interest rate than someone with economic justification for their former problems.

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