

# "Why did my monthly mortgage jump so high?"

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In the current housing crisis, many homeowners who are defaulting on their mortgages are actively seeking alternatives to foreclosure in the form of loan modifications or other repayment plans. However, after months of voluminous paperwork and processing time, many homeowners are surprised and disappointed to find that their mortgage payment has actually increased after being placed in a modification or repayment plan. Often times, the reason behind the increase in a homeowner's monthly payment is an escrow amount that is added to the principal and interest portion of the mortgage payment. Depending on the terms and provisions of the mortgage, this escrow amount can consist of past due and future projected property taxes and insurance, as well as related fees. The primary purpose of such escrow accounts is to ensure that a homeowner's mortgage, tax, and insurance payments are made on a timely basis.<sup>1</sup>

It is important to consider that mortgage escrow arrangements lead to vulnerability of the interests of both homeowners and lenders alike. A lender may be compelled to expend its own funds to protect its collateral if the homeowner is not making necessary payments at the appropriate time. On the other hand, a homeowner usually has little control or knowledge of how an escrow amount is calculated. Because of the lack of a homeowner's ability to determine a proper or improper escrow arrangement, a lender has the opportunity to require the homeowner to pay an amount that is more than necessary to cover the tax and insurance obligations on a property. A lender with thousands of customers could stand to gain substantial profits from the use of the funds gained through even small overcharges on escrow accounts.

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<sup>1</sup> *GMAC Mortg. Corp. of Pa v. Stapleton*, 236 Ill. App. 3d 486, 489 (1st Dist. 1992).

For this particular reason, and to protect the interests of borrowers, Congress enacted the Real Estate Settlement Procedures Act (“RESPA”)<sup>2</sup> to govern the procedures to be followed in connection with escrow accounts established for the payment of real estate taxes and insurance. After a homeowner has defaulted on their loan, RESPA authorizes a loan servicer to estimate the property taxes and insurance that will be due over the ensuing twelve months and to adjust the borrower's monthly escrow payments under the mortgage to cover the estimated expenses, subject to certain limitations.<sup>3</sup> More specifically, Section 10 of RESPA places limits on the amount a lender or servicer may require a mortgager to keep in his or her escrow account to cover the payments of taxes, insurance, or other disbursements.<sup>4</sup> This section also governs a lender's obligations with respect to providing an annual escrow account statement and notice of any shortage in the escrow account.<sup>5</sup>

Section 10 of RESPA states, in relevant part, that a lender may charge a borrower a monthly sum equal to one-twelfth of the total annual escrow payments that the lender reasonably anticipates paying from the account.<sup>6</sup> A lender may also add an amount to maintain a cushion equal to one-sixth of the estimated total amount of these annual payments from the escrow account.<sup>7</sup> Because of the cushion amount, lenders are allowed to collect monthly escrow payments in excess of the amounts actually necessary to pay the tax and insurance premiums as they become due. However, lenders are not permitted to collect greater than a two month cushion on the escrow amount.<sup>8</sup>

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<sup>2</sup> See 12 U.S.C. §§ 2601-2617.

<sup>3</sup> See *id.* § 2609(a)(1)-(2).

<sup>4</sup> See 12 U.S.C. § 2609(a).

<sup>5</sup> See 12 U.S.C. § 2609(b).

<sup>6</sup> See 12 U.S.C. § 2609(2).

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

Regulation X, RESPA's implementing regulation, also allows a loan servicer to conduct the analysis of the amount of money that will become due into the escrow account at either: 1) the beginning of the loan, 2) at the end of each computation year, or 3) “at other times during the escrow computation year.”<sup>9</sup> This limitation, however, is subject to an exception. RESPA and Regulation X authorize a lender to require the borrower to pay additional deposits if a deficiency or shortage exists in the escrow account.<sup>10</sup> If the lender determines that a deficiency amount exists, the lender may require the homeowner to make additional monthly deposits into the escrow account to remedy such deficiency, but must notify the homeowner of any shortage of funds.<sup>11</sup> A deficiency has been defined as the amount of a negative balance in an escrow account.<sup>12</sup> A shortage is defined as an amount by which an escrow account balance falls short of the target balance at the time of the escrow analysis.<sup>13</sup> RESPA further authorizes lenders to calculate and collect certain “advance deposits in escrow accounts,” or shortage contributions, in order to minimize any negative balance that may occur in a borrower's escrow account over the applicable 12 months.<sup>14</sup>

The two primary calculations for determining whether your account has been properly escrowed are described as follows:

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<sup>9</sup> See 24 C.F.R. Sect. 3500.17 (f)(1)(H).

<sup>10</sup> *Id.*, see also 12 U.S.C. § 2609(a)(2).

<sup>11</sup> See 12 U.S.C. § 2609(a)(2), (b).

<sup>12</sup> See 24 C.F.R. Sect. 3500.17.

<sup>13</sup> *Id.*

<sup>14</sup> *In re Rodriguez*, 391 B.R. 723, 727-28 (Bankr.D.N.J.2008).

“Under the first [method], often referred to as the aggregate method, estimated requirements for anticipated disbursements for the next twelve months are added, the balance in the [escrow] account at the time of the analysis is subtracted ... and the result is divided by twelve to arrive at monthly escrow requirements for the coming year.... In other words, all escrow obligations ... are lumped together to determine the required monthly escrow payment from the mortgagor, even if the individual escrow items are of great disparity in the amount and become due on different dates. Under the second method, commonly known as individual item analysis, the lender creates sub-accounts within the escrow account corresponding to each expenditure that must be paid out. The lender then calculates the escrow amount needed to ensure that each escrow sub-account never falls below zero.”<sup>15</sup>

Although these particular laws have been put in place to avoid over-escrowing situations, it is important for homeowners to carefully review the escrow provisions within their mortgage, and to monitor escrow accounts if they are put into place. Violations of the above-mentioned law could lead to a homeowner’s monthly payment increasing to the extent that he or she is forced into default and a subsequent foreclosure. Furthermore, if a lender violates escrow provision laws, it may be held liable for breach of contract, breach of fiduciary duty, unfair and deceptive business acts, claims for equitable and monetary relief, and any related attorney’s fees.

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<sup>15</sup> *Aitken v. Fleet Mortgage Corp.*, 1992 U.S. Dist. LEXIS 1687, at 5, n. 1.