Reduce Your Mortgage Payment

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- As mortgage rates have declined over the past several years, many homeowners have refinanced their mortgages to benefit from the drop in interest rates.
- However, for those who wish to pay-down their mortgage balance to benefit from a lower monthly mortgage payment, especially in a rising interest rate environment, another technique can be pursued, called "recasting".

Recently, a client was interested in paying down their mortgage with the goal of reducing their monthly mortgage payment. As I explained to the client, you have two general options to reduce your mortgage payment: (1) refinance your existing mortgage at prevailing interest rates for a term of your choosing or (2) request that your current mortgage company "recast" your mortgage.

You could also make a lump sum payment to the mortgage company and request that the payment be applied to your outstanding balance. However, such a request will reduce the principal due on your existing mortgage and the remaining term (that is, the years left on your mortgage), but it will not reduce your monthly payment. To reduce your monthly payment without refinancing, you would need to pursue a recasting of your mortgage.

Since most people are familiar with the refinancing process, but many are unaware of the recasting process, the focus of this article is on recasting your existing mortgage.

What Is Recasting?

To recast is to ask your mortgage company to re-amortize your existing mortgage while incorporating your lump sum payment. The lump sum payment is often the result of receiving an employment bonus or inheritance. Whether you are allowed to recast is dependent on your mortgage company or the investors who may have purchased your mortgage from the original mortgage company. If a mortgage is allowed to be recast, a non-refundable processing fee of $150 - $250 is normally charged.

Since recasting is really a re-amortization of an existing mortgage, depending on how much you pay-down your mortgage, as well as your remaining term and interest rate, you could end up paying greater interest subsequent to the recasting. How? When you take out a fixed-rate mortgage, your total monthly payment of principal and interest is fixed. However, the interest portion of that payment dwarfs the principal portion of that payment in the early years of the mortgage. As time passes, the amount of your monthly payment that is dedicated to your principal increases and the amount dedicated to interest declines. When you proceed with a recasting, you are resetting this amortization process, whereby the mortgage payments in the initial years (following recasting) are heavily weighted to interest once again, but are calculated on a lower principal balance (because you have pre-paid a portion of the prior principal balance).

The mortgage servicer should be able to provide you with a summary of the interest you would pay under your existing mortgage versus how much you would pay if the existing mortgage was recast. Remember that the interest that you pay on your mortgage is normally a tax-deductible expense and that a recasting does not change your existing mortgage's interest rate or remaining term.

Recast Versus Refinance

The traditional means of reducing your monthly mortgage payment is to pay-down and refinance your existing mortgage. As interest rates have declined over the past few years, this has been a favored technique. However, this option requires a successful underwriting process and has greater up-front costs than a recasting (for example, appraisal fees and closing costs).

In addition, as current mortgage rates may now be higher than the interest rate on your existing mortgage, you may want to recast rather than refinance if you have cash to pay-down your mortgage balance and wish to reduce your monthly payment.