



UNIT 8 – 2

When Foreclosure Is Inevitable

This unit is all about plan B.

Plan A, of course, was to stay healthy, earn a decent income, pay the bills on time, keep up with the mortgage, and eventually retire the mortgage. Then if everything works out as planned, you will be able to enter your retirement years with the house paid off and enjoy life like you always thought you would. Life doesn't always unfold as planned, however, and so some people have tragically reached the point of foreclosure, a formal legal procedure in which the lender seeks to regain property pledged as collateral against a mortgage because the borrower has defaulted on payments.

Nobody ever thinks about losing their family home, but it can happen and so if you ever find yourself in that situation, there are still some things you should know, and there is still some advice that you should follow. After all, no matter how bad things seem to be, they can always get worse. Hopefully this will never happen to you, but sometimes it helps to know about your options just in case.

Foreclosure, of course, is not inevitable, but if you get too far behind you may well feel that you have no other choice. Still, there are some things you can do, and staying in close contact with your lender is actually one of them. After all, your lender really wants a portfolio of active loans, not abandoned repossessed properties – and so the two of you have a mutual interest in getting things worked out. Of course you may attract some interest along the way from scammers who would like nothing more than to profit from your distress, but you should be able to dodge them if you know what to look for.

Case Study Application

The couple in the case study are clearly beginning to slide into Plan B. Let's see if we can help them out.



CASE STUDY: THE NEIGHBOR'S DILEMMA

In spite of all the warning signs, and in spite of all the efforts to straighten out their budget situation, Bill's next door neighbors are starting to fall hopelessly behind on their payments.

Rules on default differ from state-to-state, but now they are nearly 90 days behind on their monthly mortgage payments and they really need to do something. They still don't have any equity in the home because of their I-O mortgage, but they don't want to become deadbeats either like some other people who have simply walked away from similar situations. On top of that, they want to do what they can to preserve what is left of their credit rating.

As much as it hurts to admit failure, they need to do something – only what to do at this point?

What to Do When You Get Behind

It's clearly a difficult situation when you can't make your monthly mortgage payments – but believe it or not, there is still some hope. When the situation starts to look troublesome, Freddie Mac offers the following advice:¹

- **“Call your lender.**
This is the single most important thing you can do. Lenders want borrowers, not properties – they would prefer to see you keep your home. Most will work with you while you get back on your feet.
- **Be honest with your lender.**
Different situations require different solutions. It will matter to your lender to know if your financial problems are temporary, for example, due to an injury that puts you out of work for a few months, or are more long term, such as a cut in pay or a layoff.
- **Know what you owe.**
Have a clear picture of what your debts are and make your mortgage the priority if you have to make choices. Debt collectors can be very aggressive, but if you can't pay all your debts, make sure your home is protected from foreclosure by paying your mortgage.

¹ http://www.freddiemac.com/corporate/buyown/english/avoiding_foreclosure/early_steps.html



- **Talk to a housing counselor.**
A non-profit housing counseling agency may be able to help you restructure your bills so that you have an easier time paying them. Additionally, they can help you create a budget that suits your specific needs.
- **Contact a housing non-profit.**
A housing non-profit can give you valuable advice. The HOPE National helpline, 888-995-HOPE, is dedicated to helping homeowners facing foreclosure 24 hours every day. Spanish – speaking counselors are available.”

Remember that the worst thing you can do now is to ignore the problem. The longer you wait to address the issue, the fewer options you will have. If you are behind in your monthly payments, get some professional advice as soon as you can.

- Have Bill’s neighbors reached the point where they need to contact their lender yet?
- If they do contact their lender, what information should they provide?

Consider Selling Your Home

Another thing to consider is selling the home. After all, if you have owned the property for some time, and if you had a mortgage that reduced the principal each time you made a monthly payment, you may have some **equity**, or residual value after all of the obligations and fees are subtracted from the proceeds of the sale. You may even have some equity in the home if you had an interest-only mortgage, assuming that the market value of the home went up while you were making the payments. The equity won’t be as great in this case, but there still may be something to salvage.

Also, remember that your losses may be smaller if you sell the house yourself rather than wait for repossession. After all, about the only thing the lender can do with the house is to put it back on the market again, and the lender is likely to assess you with a number of fees and penalties that you would not have to pay if you sold it yourself. And, if the proceeds from the sale do not cover the amount owed on the principal, you will still be liable for the difference.

If you can sell the house, and if you can salvage your credit reputation, you may well be able to buy a smaller one that you can afford.

- What kinds of mortgages are most likely to reduce the principal owed over time?
- What kinds of mortgages are the most likely to be troublesome in times of rising interest rates?



When Foreclosure Is the Only Option

Anyone facing foreclosure probably thinks that things can't get much worse, when in fact they can. Here are some tips to help you from making things worse:

- Contact your lender and let him know about your situation. Ask if there is anything you can do to try to work things out. Different lenders will have different policies, and while there are no guarantees, it won't hurt to ask. Also remember to be absolutely honest with your lender and don't make any claims that you can't substantiate (like "the check is in the mail").
- If you have stopped making payments, or if you are hopelessly behind, be sure to continue to answer your mail and your phone just in case your lender is trying to contact you. There is always the chance that your lender may be trying to help you work things out.
- Don't move out of your home as you normally have to be living there in order to qualify for assistance. This may vary from state-to-state, but you can go to a site like <http://www.lsc.gov/index.php> to see what the situation is in your area.

Beware of Foreclosure Scams

It probably comes as no surprise to hear that there are a variety of scam artists who thrive on other people's misfortune – and foreclosures are no exception. Foreclosure is an extremely serious situation; and numerous scams are popping up all the time. Some of the more popular ones are described below:

- **Equity capture** – In this variation, a scammer may ask you to turn over the deed to the home so that he can "sell it for you" and then pay off the mortgage. However, the scammer then keeps the proceeds of the loan without paying it off, leaving you *without* the home and *with* the obligation of paying off the mortgage. The scammer may even ask you to move out of the house while he takes care of things – and then after you leave he may rent the house to someone else and keep the proceeds.
- **Phony counseling scam** – Rather than take the title to your home, the scammer may, for a steep initial fee of course, offer to "fix things up" with the lender. The scammer does little work other than have you fill out numerous forms and place a few phone calls that you could do yourself while the property slides into foreclosure. Separating the legitimate help from the fraudulent ones is a daunting task, but also one that should not be ignored.
- **Lender/refinancing scams** – Someone may offer to arrange for a new mortgage that is easier to pay. For example, if you already have a mortgage that pays down the principal, the new mortgage may be an I-O which has lower monthly payments. Or, the new mortgage could have a **balloon**



payment, or a requirement for a single lump sum payment that would fully pay off the remaining principal in a set number of years. So if the I-O balloon is due in 10 years, you have to repay the full amount of the principal at that time or lose the property. While this may be legal, little is gained while the obvious problem, the principal repayment, is only delayed.

- **Cash back loan flipping scams** – In this scam the lender offers to refinance your loan while simultaneously giving you some cash. However, this scheme may put you into a worse mortgage with higher points, fees and higher prepayment penalties. The scam artist gets a fee for generating a new loan, passes on some of the profit to you in the form of cash, but leaves you with a more burdensome mortgage that could lead to an earlier foreclosure than you would have otherwise faced.
- **Internet/phone phishing scams** – In this case a person seeking help responds to an internet site or a phone call and ends up filling out paperwork or otherwise giving up information regarding their name, address, bank account number, social security number, and other key financial information. All of this can lead to identity theft, and once you have given this information to the wrong party, you have more than a mortgage to worry about.

Foreclosure is a grave issue and, if not taken care of immediately, can leave you evicted from your home along with a damaged credit score. The best way to save your home is to learn everything possible about foreclosure and track down appropriate mortgage counseling companies that will help you out of this jam. The instant you stop giving proper attention to this predicament, fake foreclosure companies will try to exploit you.

There are even more refinancing scams than this, of course, but the main thing to keep in mind is this: *if the deal seems too good to be true, it probably is*. And, like anything else, it doesn't hurt to do some comparison shopping. For example, after someone explains how they plan to restructure your debt to get you out of trouble, take the time to ask a competitor how they would do it. You'd be surprised how effective this strategy can be, and you'll be pleased to learn what one competitor is likely to tell you about the problems with their competition.

Finally, if anyone ever asks you to sign documents that turn the title of your property over to someone else, it's time to get a separate legal opinion. There are a number of experts that you can talk to, and you can always consult an attorney in your area.

- Which of these scams are likely to be the most effective with a majority of homeowners?
- Have you or any of your family seen ads promoting what could easily turn out to be mortgage refinancing scams? What were they?

