

What is a foreclosure?

Let's use this example: Bill buys a house for \$50,000. At "Closing" the seller gives Bill a "Deed" to the house. That means Bill owns the house. A Deed may be called a

- *Warranty Deed*
- *General Warranty Deed*
- *Special Warranty Deed, or*
- *Quitclaim Deed*

The closing costs were \$2,000. (\$50,000 + \$2,000 = \$52,000 Total) Bill paid \$3,000 in cash. \$52,000 - \$3,000 = \$49,000 that Bill still owes. American Mortgage Trust Bank loans Bill the \$49,000. Bill signs a lot of papers to get this loan. Two documents are very important: (1) The "Promissory Note" says that Bill agrees to pay the loan back. (2) The "Deed of Trust" says that the lender may sell the house to raise money to pay the loan if Bill does not pay. When the lender sells the house, it is called a "Foreclosure." The Deed of Trust also lets the lender foreclose on the house if Bill fails to do other things he agrees to do, such as pay for insurance.

Can the lender foreclose if I am just one month behind? The lender may foreclose if you are "in default." Most Deeds of Trust say that you are "in default" if you miss one payment. However, most lenders choose not to foreclose after you miss just one payment.

Does the lender have to tell me before foreclosing? It depends on what the Deed of Trust says. The Deed of Trust might say that the lender does not have to tell you before foreclosing. However, most lenders will tell you before they foreclose.

Most lenders send several letters before they foreclose. Let's say that Bill's mortgage payment is \$320 per month plus a late fee of \$16 per month. He owes \$320 + 16 = \$336 for each month he is behind.

Bills gets letter #1 from the lender after he has missed two payments:

"You are behind in payments. Please pay \$320 + \$16 = \$336 x 2 months = \$672 now.

Bill gets letter #2 from the lender after he has missed three payments:

"If you do not pay \$1,008 immediately, we will foreclose."

If Bill paid \$1,008 would the lender stop the foreclosure? Yes. The lender must stop the foreclosure if Bill catches up the payments -- unless the lender has sent letter #3.

Bills gets letter #3 from the lender after he has missed four payments:

"You have to pay \$49,400 within 30 days. If you don't, we will foreclose."

IMPORTANT: The lender might foreclose before sending three letters.

How did the amount Bill owed go from \$1,008 to \$42,438.15? When the lender decided to foreclose, the lender made the entire loan due immediately.

If Bill paid \$1,008, would the lender stop the foreclosure? Maybe. After the lender demands payment in full, the lender is allowed to continue with the foreclosure unless the entire loan is paid off. But the lender might choose to let Bill just pay the past-due payments. Of course, if Bill pays off the entire loan, the lender must stop the foreclosure.

WHAT TO DO WHEN YOU CANNOT PAY

STEP 1. Talk to the lender. If you know you can't make a payment on time, tell the lender. Explain the problem. The lender will probably send you a long application to fill out. Be sure you

- *Fill in all blanks on every form.*
- *Send a copy of all records the lender wants (such as tax returns and pay stubs).*
- *Keep a copy for your records.*
- *Get a delivery receipt from the lender. You can do this through the Post Office or a courier (such as Federal Express).*

Many times, the lender loses your papers after you send them back. It is not fair, but you must send them again.

IMPORTANT: The lender might tell you not to make your regular payment while they review your application. Make sure they tell you that in writing. You might have to make up the full payment later. You should put as much money as you can into a savings account so you can pay it later if you have to.

IMPORTANT: Write down what was said in every phone call you have with the lender. Include the date and name of the person you talk to. Keep all letters you get from the lender. Make a copy of all letters you send the lender.

What if the lender will not work with me? Most lenders do not have to work with you. But if you have a VA or FHA loan, the lender must consider your application.

STEP 2. If the lender will not help you, call a HUD Housing Counselor. You can find a Housing Counselor at www.HUD.gov or call 1-800-225-5342 (TTY 1-800-877-8339).

TYPES OF HELP THE LENDER MAY OFFER

"Forbearance Agreement" means you will catch up late payments over time. *Example:* You owe \$1,200 in back payments. Your regular mortgage payment is \$300 per month. You agree to pay \$400 per month (an extra \$100) for 12 months. After that, your payment will go back down to \$300. If you miss one of the \$400 payments, the lender may foreclose.

"Mortgage Modification" means you change something about your loan to make your payments lower. *Example:* A lower interest rate will lower your payments. *Example:* "Extend the term" of the loan. You will pay the loan for a longer time, but it will reduce the amount of your monthly payments.

"Short Sale" means the lender lets you sell the house for less than you owe on the mortgage. This keeps a

foreclosure off your credit report. Be sure the lender agrees in writing that you will not owe the rest of the loan later. **IMPORTANT:** If the lender cancels part of your loan, you might owe income tax. Talk to a tax expert.

“Deed in Lieu of Foreclosure” means you give the property back to the lender without a foreclosure sale. Be sure the lender agrees in writing that you will not owe the rest of the loan later. **IMPORTANT:** If the lender cancels part of your loan, you might owe income tax. Talk to a tax expert.

MAKING A DEAL WITH THE LENDER

Do not promise too much. If you promise the lender that you will do something, but you do not do it, the lender probably will not help you later. Do not promise to pay more than you can afford. Do not promise to pay sooner than you can pay.

Follow the agreement. If you miss a payment under the new agreement, the lender may foreclose.

Write down your agreement. If the lender does not send you a written agreement, you should send the lender a letter. The letter will say, “This is what we agreed.” Then, say what your agreement is.



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