Alternatives to Foreclosure

The Fed's Profitwise Newsletter recently addressed home foreclosure alternatives. The newsletter states "There are workout options available to lenders to help borrowers keep their home. However, some lenders do not inform borrowers that alternatives are available, in part because not all lenders are fully aware of alternatives to foreclosure."

This is key information for anyone who finds that they are falling behind in their mortgage payments.

Below is an except from the Profitwise Newsletter:

What follows is an overview of foreclosure alternatives. It should be noted that these options work best when the loan is only one or two payments behind. Borrowers delinquent beyond two payments severely limit their options.

For Temporary Setbacks

Reinstatement: Accepting the total amount of back interest and principal owed by a specific date. This option is often combined with forbearance.

Forbearance: Reducing or suspending payments for a short period, after which another option is agreed upon to bring the loan current. A forbearance option is often combined with a reinstatement, when it is known that the borrower will have enough money to bring the account current at a specific time in the future. The money might come from a bonus, investment, insurance settlement, or a tax refund.

Repayment Plan: With a repayment plan, the bank agrees to add, for example, half the amount of the first missed payment onto each of the next subsequent two payments. These plans provide some relief for borrowers with short-term financial problems, such as expensive car repairs that make it too difficult to pay the mortgage in a given month.

For Long-term or Permanent Set Backs

Mortgage Modification: If the borrower can make the payments on the loan, but does not have enough money to bring the account current or cannot afford the total amount of the current payment, a change to one or more of the original loan terms may make the payments more affordable. The loan terms could be changed in one or more of the following ways:
- Adding the missed payments to the outstanding loan balance;
- Changing the interest rate, including making an adjustable rate into a fixed rate;
- Extending the repayment term.

Short Refinance: Forgive some of the debt and refinance the rest into a new loan, usually resulting in lower financial loss to lender than foreclosing.

Claim Advance: If the mortgage is insured, the borrower may qualify for an interest-free loan from the insurer to bring the account current. Full repayment of this loan may be delayed for several years.

For Older Homeowners

Reverse Mortgage: Reverse mortgages allow older homeowners (with little or no outstanding mortgage debt) to convert the equity in their homes to cash while retaining ownership. With a regular mortgage, the borrower makes monthly payments to the lender. But with a reverse mortgage, the borrower receives money from the lender and generally does not have to repay it for as long as they live in the home. In return, the lender holds some — or all — of the home’s equity. For more information on reverse mortgages, go to www.ftc.gov.

If Keeping the Home is Not an Option

Sale: If the borrower can no longer afford to repay the mortgage, the lender agrees to give the borrower (or their agent) a specific amount of time to find a purchaser and pay off the total amount owed. If the borrower can no longer afford to repay the mortgage, the lender agrees to give the borrower (or their agent) a specific amount of time to find a purchaser and pay off the total amount owed.

Pre-foreclosure Sale or Short Payoff: If a property’s net sales proceeds do not cover the loan in full, the lender may accept less than the full amount owed. Though the lender takes a loss on the sale, the additional cost of foreclosing on the property is avoided.

Assumption: Allow a qualified buyer to assume the mortgage, even if the original loan documents state that it is non-assumable.

Deed-in-lieu: Agree to allow the borrower to voluntarily surrender the property and forgive the debt. This option may not be available if other liens such as judgments of other creditors, second mortgages, and IRS or state tax liens exist.

Note: both a short sale and a deed-in-lieu damage the borrower’s credit rating less than a foreclosure as they reflect efforts by the borrower to come to terms with the lender. But the short sale is less damaging than a deed-in-lieu, because it indicates recognition by the lender that the event was caused by factors outside of the borrower’s control.To read the complete newsletter, click here.

ACCESS Comments: It's important to remember, that if a creditor should foreclose on your home and they are unable to recover all monies due, you will still owe the balance. In that situation, you no longer own a home but still owe the debt.Foreclosure is a lengthy and expensive process. Most creditors will work with you to avoid the situation.