

SPECIAL REPORT: DEALING WITH FORECLOSURE SCAMS

This special report was written from two perspectives. The first is to alert homeowners to the dangers of foreclosure scams. The second is to make investors aware of situations they may encounter when trying to negotiate deals with homeowners. Whichever perspective is most appropriate for you, make sure you understand the material in this report so that you yourself won't get scammed.

Foreclosure Scams

According to federal government and news reports, "foreclosure scams" are targeting consumers whose home mortgages are in trouble. Scam operators advertise over the Internet and in local publications, distribute flyers, or contact consumers whose homes are listed in the foreclosure notices. The scam artist's appeal is sometimes directed to specific religious or ethnic groups.

The fraudulent operators may promise to take care of your problem with your mortgage lender or to obtain refinancing for you. Sometimes they also ask you make mortgage payments directly to them. They have even been known to ask the homeowner to hand over their property deed, claiming that if the homeowner then makes the mortgage payments to them, they will be able to in stay in their home. Instead of contacting your lender or refinancing your loan, the con artist pockets all the money you paid, and then files a bankruptcy case in your name - sometimes without your knowledge.

A bankruptcy filing often stops a home foreclosure, but only temporarily. If a bankruptcy is filed in your name but you do not participate in the case, the judge will dismiss the case and the foreclosure proceedings will continue. If this happens, you will lose the money you paid to the scam operator - and you could lose your house. You will also have a bankruptcy listed on your credit record for at least 10 years.

Proceed with Care

The Better Business Bureau (BBB), the Federal Trade Commission (FTC), and other federal and local government organizations have stepped-up the pace in warning borrowers about foreclosure scams and the associated dangers. You should proceed with care if you are approached in any of the following ways.

- **Mortgage Consultant.** Someone contacts you and identifies himself as a "mortgage consultant," "foreclosure service" or similar name. Ask for more identifying information and some references, then check them out.
- **Fees before Services.** Someone wants to collect fees from you before he provides any type of loan services. The challenge is that you could lose your fees and still not get the services.
- **Payment Redirection.** You are told to start making your home mortgage payments directly to the individual or company, who in turn will make the payments to the original lender for you. Yeah right! This doesn't make any sense, does it?

- **Deed Transfer.** You are told to transfer your property deed or title to the individual or company, and they will handle all the paperwork details with the lender. This also doesn't make sense. It's like giving away your property.

If you are having trouble paying your mortgage, contact your lender or an attorney for assistance.

Mortgages

The credit marketplace appears to be highly competitive for consumers who are thinking about buying a home or refinancing an existing home loan. Mortgage loan rates can often be found in most newspapers and on the Internet, making it easier to comparison shop. But, for consumers with low or irregular income, tarnished credit reports and limited financial knowledge, finding an affordable loan can be a difficult task. These consumers oftentimes turn to more marginal or "sub-prime" sources for their credit.

Home loans are available in the sub-prime market, but borrowers will pay more for the loan. There are sub-prime mortgage lenders who may charge points and origination fees in excess of 10% of the loan amount and then finance those fees at high interest rates. In addition to paying more, the sub-prime borrower may be subject to the following predatory practices:

- **Excessive Mortgage Broker Compensation.** In the sub-prime market, there are mortgage brokers who will attempt to sell the borrower on a loan with the most fees and highest interest rate possible so that he/she will get more compensation. Some of these brokers may charge fees of 8 to 10 points. That means that on a \$100,000 loan, the borrower is paying and financing an additional \$8,000 to \$10,000.
- **Excessive Points and Fees.** Most borrowers can expect to pay a 1% origination fee and possibly another 1% of the loan amount in points, as well as basic closing costs, which would include appraisal and attorney's fees. Some predatory lenders load up loans with these up-front charges and charge additional "junk fees" to pad the closing costs.
- **Sell the Monthly Payment.** Many brokers and lenders advertise "bill consolidation" home equity loans. Predatory lenders encourage consumers to pay off all their debts by consolidating them into one home loan with the promise to reduce the monthly debt payment. The problem with this is that the consumer is trading short-term debt for long-term debt. Instead of paying off consumer credit bills in three to four years, the new consolidation loan will take 15 to 30 years to pay off. To avoid becoming a victim, consumers must look beyond the monthly payment and analyze all the terms of the loan.
- **Balloon Payments.** Another way for a predatory lender to reduce the monthly payment on a home loan is to have the borrower pay off only the accrued interest each month. This method of financing will result in a huge balloon payment at the end of the repayment term, usually after 15 years. If the borrower is elderly, it will be very difficult to refinance the loan, and foreclosure may become inevitable.
- **Equity Stripping.** An unscrupulous lender targets consumers with a significant amount of equity in their home and offers to lend an amount that is more than the borrower can financially handle. The borrower defaults and the lender then forecloses and sells the house, stripping the homeowner of all the equity he has earned over the years.
- **Flipping.** This occurs when predatory lenders encourage consumers to repeatedly refinance their loan. Each time the loan is refinanced the lender charges more fees, placing the borrower further in debt over a longer period of time.

Advance Fee Loans

The scenario is all too common: a consumer receives a call or e-mail or sees an advertisement for a pre-approved loan or credit card and calls to receive an application. The company says yes, they can offer you a loan regardless of your credit history, if you pay an up-front "insurance," "security," or "processing," fee in advance. Too often, those with bad credit - who can least afford it - end up losing their up-front fee and never hear from the company again.

According to the Telemarketing Sales Rule, if someone guarantees or suggests that there is a strong chance they can get or arrange a loan or other form of credit for you, it's against the law to ask you to pay - or accept payment - for their services until you get your loan or credit.

The BBB and the Federal Trade Commission (FTC) offer the following points to keep in mind before you respond to ads that promise easy credit, regardless of your credit history:

- **No Guarantees.** Legitimate lenders never "guarantee" or say that you are likely to get a loan or a credit card before you apply, especially if you have bad credit, no credit, or a bankruptcy.
- **Legitimate Fees.** If you apply for a real estate loan, it is accepted and common practice for lenders to request payment for a credit report or appraisal. However, legitimate lenders never ask you to pay for processing your application.
- **Protect Your Information.** Never give your credit card account number, bank account information, or social security number over the telephone or Internet unless you are familiar with the company and know why the information is necessary.
- **Get It in Writing.** If you don't have the offer in hand - or confirmed in writing - and you are asked to pay, don't do it. It's fraud and it's against the law.

Up Front Fee for a Loan?

The government and now the lenders have stepped up its efforts to educate consumers on how to make smart money decisions and avoid scams in the marketplace. One problem area consumers should watch out for is advance fee loan scams.

Despite these cautions, consumers continue to fall for advance fee loan offers in record numbers. The scenario goes something like this: A small printed advertisement appears in the newspaper or on the Internet suggesting

“Money to lend, debt consolidation, personal car and small business loans for people who have good/bad credit and past bankruptcies. Call Toll-Free Now!”

The caller contacts the number and receives forms asking the consumer to submit personal information, including copies of driver's licenses, employment records, Social Security numbers, bank account information and credit card numbers. This is the same approach scam artists use to commit identity theft.

More Up Front Fees

A few hours or days later a friendly, polite telephone caller responds with the good news. The loan has been approved, but an insurance fee, processing fee or three months advance payment is

needed before the loan is released and the check delivered. The consumer is asked to pay the fee immediately through electronic transfer of the money. The money is picked-up by the “loan” broker, but the promised loan never arrives and the up front fee paid by the consumer (which can total several thousand dollars) is lost.

Many fraudulent loan offers are made by scam artists operating out of Canada and other countries. Attempts to contact the individuals in question usually prove unsuccessful. It is very seldom that the company can be located to get the loan fees returned to the consumer.

Consumers in need of extra cash are well advised to thoroughly investigate all advertised offers of “easy credit” or “easy loans” from unfamiliar loan brokers, particularly those originating out-of-state or out-of-country.

You need to ask yourself, why is this company, which I have never heard of, and which does not know me, willing to give me a loan?” The following are signs of advance fee loan fraud:

- Pressure to act immediately. Advance fee loan schemers will try to get you to send money or give out personal information (credit card number, bank account information and social security number) before you get any paperwork. Insist on receiving the necessary paperwork before deciding whether to apply for credit.
- Will not provide location information. If the loan broker hesitates to tell you their physical location, beware that this is a common ploy to avoid law enforcement detection. Refuse to do business with the broker until you have their physical address or location and can check them out carefully. There are consumer advocate organizations throughout the U.S., Canada, and other parts of the world.
- Questionable connections to established financial institutions. Many of these schemers are merely telephone sales operations, so no connection will exist to an established financial institution. Ask which lenders the “loan broker” deals with, and ask for the physical address of the lender. Then contact the BBB in that city to request information on the lender.

Points to Keep in Mind

Consumers should keep the following points in mind before responding to ads that promise easy credit, regardless of your credit history:

- Legitimate lenders never “guarantee” or say that you are likely to get a loan before you apply, especially if you have bad credit, no credit or a history of bankruptcy.
- If you apply for a real estate loan, it is accepted and common practice for lenders to request payment for a credit report or appraisal. However, legitimate lenders never ask you to pay for processing your application.
- Never give your credit card account number, bank account information or Social Security number over the telephone or Internet unless you are familiar with the company and know why the information is necessary.
- If you do not have the offer in hand – or confirmed in writing – and you are asked to pay, do not do it. It is fraud and it is against the law.

Foreclosure 'Rescue' Scams on the Rise

Consumers facing the threat of losing their homes should be wary of individuals and companies offering to "help" them out of their difficult financial situation. Consumer advocates continue to report increases in complaints about foreclosure "rescue" scams. These scams specifically target homeowners who are in financial distress. Scam operators advertise over the Internet and in local publications, plaster posters on telephone poles and at bus stops, stick flyers in people's front doors or contact people whose homes are listed in public foreclosure notices. Sometimes they direct their appeals to specific religious or ethnic groups.

In one scenario the scam operator offers to "buy" the homeowner's property by paying off the amount that is overdue on the loan. He convinces the homeowner to move out and deed the property over to a third party. The homeowner is given the option of renting the property with the option to buy it back later. The rent payment on the home is often higher than the homeowner can afford. Often times, the original homeowner cannot make the rent payment and is evicted from their home. Or, if the homeowner expresses a desire to buy back the property, the scam operator usually sets the price of the home higher than the homeowner can afford.

The unfortunate homeowner can lose his equity and his home. Sometimes, the homeowner's troubles go even deeper. In many cases the initial mortgage has not been paid off and the deed was never transferred, as promised. Not only is the homeowner faced with eviction from the home, but he still owes the original loan amount.

Getting Behind on Mortgage Payments

Consumers who are tempted by such offers should recognize that they are at real risk of losing money, equity, their home or all three. Carefully consider the following if your mortgage is in arrears or you are facing foreclosure:

- Talk to your lender. Ask about how to restructure your loan payment or refinance. Some foreclosure "rescuers" will offer to "negotiate" with your lender or lawyer. Know that such an offer is likely to involve a significant fee. If you are hesitant to talk to your lender yourself, engage the assistance of a trusted family member.
- If that proves to be unfeasible, try selling the house on your own to pay off the lender. Signing over a deed in no way releases you from your mortgage responsibilities!
- Some schemers will offer to complete paperwork for you, or ask you to sign a stack of documents, supposedly to secure a new mortgage. Victims have later learned that they signed a quit-claim deed to their home.
- Beware the personal approach. Some less-than-ethical businesses will stuff a handwritten note in your front door or mailbox that implies that "help" is available from someone you know or who has your interests in mind. Foreclosure scam artists know exactly what neighborhoods to blanket with their offers.
- If a foreclosure "rescuer" instructs you not to contact your mortgage company or your attorney, beware. Your mortgage company is the very business that you should be in touch with! Furthermore, why would you agree to cease contact with your attorney when dealing with complicated financial matters that involve perhaps your biggest investment, your home?

- You should never sign a contract under pressure and never sign away ownership of your property. Ask a trusted family member, your attorney or a financial professional to review any paperwork you may be asked to sign.
- Before signing any deals with a potential buyer, contact your BBB to request a report on the company and check with your state Attorney General and state Real Estate Commission.

Mortgage Choices

You've found the house of your dreams and now all you need is a loan. With dozens of competing lenders and mortgages to choose from, you may think that today's home loan market is very confusing. The challenge is to match the mortgage to your personal situations. Though many mortgage choices are available, they all fall into two categories:

- Fixed Rate Mortgages: the interest rate and the principal and interests payments do not vary
- Adjustable Rate Mortgages: the interest rate and payments can vary

There are also a number of "creative financing" alternatives that can be combined with either fixed or adjustable rate mortgages including shared appreciation, wraparounds, assumable loans, seller financing, "convertible" mortgages and/or buy-downs.

For years the fixed rate mortgage was the most popular choice among home buyers and sellers. The advantage is that neither the interest rate nor the monthly payment changes. These mortgages are no longer limited to 30 years. Other variations include 10-, 15-, 20- and even 40-year maturity periods. You can also negotiate bi-weekly mortgages, which will shorten the term of your loan.

Okay News in Ordinary ARMs

An adjustable rate mortgage (ARM) is popular because of the lower initial interest rate, as compared to an often higher interest rate for fixed-rate financing. The lower interest rate makes it easier to qualify for a loan because less income is needed. In addition, the lower interest rate may allow you to borrow more money and purchase a larger or nicer home. ARM borrowers, generally, are not "locked-in" to high marketplace interest rates that may occur at the time they obtain their loans, since ARMs will decrease if rates decrease.

Also, if you only expect to live in your house for three to five years, an ARM may be the best choice because the initial interest rates are lower. On the other hand, an ARM does not allow the borrower to anticipate precisely what mortgage costs will be over the life of the loan. At each adjustment period, your ARM interest rate and monthly payment may change. As a result, it may be difficult to plan your finances.

Bad News in Option ARMs

Note that there is a significant and growing problem of Option ARMs, in which the borrower is allowed to make interest only payments (sometimes the offer is as low as 1%) for an initial period (often 1-2 years). The problem is that the dollar amount based on the remaining interest that the borrower should have been paying is added on to the original balance.

So the borrower is getting a reprieve on the interest being paid but not on the balance due, which continues to increase beyond the original balance. This is known as negative amortization, and it is very dangerous for the borrower. Ultimately, when the loan resets (goes from 1% back to the original rate or higher), the borrower gets a double whammy. So not only does the borrower owe more than he initially borrowed, he now has to make a significantly larger payment.

Considering Refinancing

Homeowners anxious to lower their mortgage interest rates are refinancing in record numbers, according to industry experts. While refinancing may save you perhaps hundreds of dollars off your existing mortgage, it is not for everyone. If you are considering refinancing, you should shop around, compare prices and negotiate. But also move with caution when dealing with some lenders.

Refinancing Tips

Here are some tips to help homeowners decide whether or not to refinance their current mortgage.

When you refinance your home, you simply apply for a new mortgage at the lower rate in order to pay off the old loan. This means that, for many lenders, you will again be required to pay most of the costs you originally incurred to get your first mortgage - loan application fees, title search, appraisal, credit check, lawyer's services, discount points (in many cases) and other finance charges. But, many institutions offer plans where most of these fees are folded into the loan, reducing your actual "out of pocket" cash to a minimum. Most consumers are able to take a tax deduction on the interest. Ask your tax advisor if this applies to you.

Before you go through the expense of refinancing, check the interest rates to make sure they have dropped to a level that makes refinancing worthwhile. Conventional wisdom states that a two or three percent difference between the rate on your current mortgage and the new rate over a period of time - generally several years - usually offsets the costs you must pay at closing. The ultimate amount you may save depends on many factors, including your total refinancing, whether you sell your home in the near future and the effects of refinancing on your tax situation.

If you decide to refinance, obtain information from several lenders. Knowing just the amount of the monthly payment or interest rate is not enough. Ask for information about the same loan amount, loan term and type of loan so that you can compare the information. Remember, you do not have to refinance your mortgage with the same lender that provided your original mortgage.

Beware of Smooth Talkers

Also, be cautious of smooth-talking lenders that call you on the phone or come to your door offering easy credit, guaranteed low-interest loans or loan terms that sounds too good to be true. Fraudulent lenders often prey on people who are desperate for cash to pay bills, make home repairs or who do not understand the mortgage loan process.

Their loan terms can include excessive fees, high interest rates and provisions that can make it expensive for you to get out of the loan. If a lender ask for an up-front fee before you can obtain

the loan, look elsewhere. Be sure to check with the Better Business Bureau and your state attorney general for a reliability report on the lending institution (s) your are considering.

Once you know what each lender has to offer, negotiate for the best deal that you can. Have the lender or broker write down all costs associated with the loan. Be sure to read the loan documents carefully and be certain that all spaces are filled in before you sign them. Always assume that any document you sign is a contract. If you do not fully understand it, do not sign it!