Module 5.3
Study Guide

# HUD Housing Counselors Training

U.S. Department of Housing
and Urban Development

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# Module 5.3 Avoiding Foreclosure/ Disposition Options

## Module Introduction

### Module Introduction

Module 5.1 provided an overview of foreclosure, regulatory measures to protect consumers, and where counselors can go to find more information on available loss mitigation/retention programs and resources. Module 5.2 covered retention strategies to help clients remain in their homes and discussed mortgage default scams and how to report them.

In this module, you'll learn how housing counselors can provide options and resources to help clients who are unable to maintain their homes or decide to leave them. You'll learn about the costs and consequences of disposition options such as foreclosure, short sale, and deed-in-lieu. You'll also learn about the steps involved in transitioning away from the home, through foreclosure or other methods, and programs that can assist in the process.

### Lesson Objectives

By the end of this module, you'll be able to:

1. Explain the costs and consequences of a foreclosure (judicial and non-judicial), short sale, or deed-in-lieu.
2. Analyze a client's information if the client seeks to transition away from homeownership, demonstrating knowledge of programs that offer alternatives to foreclosure.
3. Apply knowledge of the foreclosure timeline, processes, and next steps to occur if a client is unable to stay in the home, devising appropriate action steps to assist the client in recovering from a mortgage default as soon as possible.

## Costs and Consequences of Foreclosure, Short Sale, and Deed-in-Lieu

Sometimes a client's financial situation changes so drastically that homeownership becomes unaffordable, causing the client to move out of the home. In these cases, housing counselors can provide guidance on how to make the transition.

Each option has costs and consequences to take into consideration, and counselors must be aware of these so they can help their clients make the best decision based on their situations. Let's take a look at the options.

### Foreclosure

A legal process in which mortgaged property is sold to pay the loan of the defaulting borrower. Foreclosure laws are based on the statutes of each state.

### Short Sale/Preforeclosure Sale

Also called a preforeclosure sale, a short sale is a procedure in which a borrower sells a property for an amount less than the outstanding mortgage balance to avoid a foreclosure. Basically, the mortgage company allows the homeowner to sell the house for an amount that falls "short" of the amount still owed. Except in certain states or by agreement between homeowner and servicer, the sale does not necessarily satisfy the borrower's debt and may result in a **deficiency judgment**.

**Deficiency Judgement**

Assessment of liability by a court against a homeowner for the unpaid balance owed to the servicer after a foreclosure, short sale, or deed-in-lieu if the sale does not cover the full amount owed.

### Deed-in-Lieu

A process that allows a homeowner to avoid foreclosure by providing a deed "in lieu" of foreclosure to the lender. The homeowner gives the title back and effectively transfers ownership to the mortgage company. Except in certain states or by agreement between homeowner and servicer, the sale does not necessarily satisfy the borrower's debt and may result in a deficiency judgment. Though it helps to avoid foreclosure, the process does not allow the homeowner to stay in the home.

## Alternatives to Loan Modification

Let's sit in on a session where a counselor, Michele, helps one of her clients, Penelope, decide on the best option for transitioning away

*A Client, Penelope, and a Counselor, Michele* from home ownership, keeping in mind the associated costs and consequences.

Penelope is a year behind on her mortgage due to illness and will not be able to return to work full-time. She has sought two loan modifications to avoid foreclosure. Let's join them now.

> MICHELE. Hi, Penelope. I don't have good news. Your second modification request was also denied. Since you are a year past due on your mortgage and are unable to return to work because of your illness, the bank is concerned about your ability to repay even a lower amount. I think we need to begin considering other options.
>
> PENELOPE. If the bank won't work with me on my new budget, I think I have no choice but to move somewhere else.
>
> MICHELE. I'm sorry to have to agree with you. Your income has decreased to $1,800 a month, and your expenses have increased to $2,800 a month—your bills are unaffordable. Your mortgage alone is 80% of your income, which is much higher than it should be.
>
> PENELOPE. I really am ready for this to be over. What are my options?
>
> MICHELE. I understand. You have a conventional mortgage, which means your options include foreclosure, short sale, and deed-in-lieu, but each has costs and consequences. Unfortunately a straight sale is not possible since there is no equity in the property.

## Costs and Consequences of Foreclosure, Short Sale, and Deed-in-Lieu

Michele then explains the common costs and consequences associated with the option of foreclosure. She also explains ways that Penelope can avoid some costs and consequences in order to ease the financial burden of foreclosure.

### Costs and Consequences of Foreclosure

- Will remain on credit report for up to seven years and lowers credit score significantly
- Will typically prevent the option to buy another home for several years—extenuating circumstances like co-borrower death, illness, severe injury, or job transfer can lessen the waiting period
- May limit how much time there is to vacate the property after the sale date
- May require paying taxes on the lender's losses from the process
- May lead to a deficiency judgment if sale doesn't cover the full amount owed
- Will cause loss of accumulated equity/investment
- May lead to children attending new schools

## Options to Reduce Financial Burden of Foreclosure

- Will receive financial assistance that can be used for relocation costs or other expenses.
- May receive **tax relief** from paying taxes on the bank's losses in the foreclosure. Visit IRS.gov and search for "Forgiven Mortgage Debt" for more information about availability.
- Can make a request to the lender that the option for a deficiency judgment be removed.

> **Tax Relief**
>
> Refer to the Internal Revenue Service, or IRS, for information about tax consequences for each disposition option.

PENELOPE. What if I tried to do a short sale or deed-in-lieu rather than foreclosure? Would either of those be better?

MICHELE. Many of the costs and consequences are the same—the main difference is the impact on your credit profile. It may be easier to qualify for your next home loan with a short sale or deed-in-lieu as opposed to a foreclosure; but for all three options, the negative information remains on your credit report for seven years.

We can call the bank together and discuss what approvals it requires, the procedures, and see if it would be open to either of those options instead of foreclosure.

## Manufactured Home Foreclosure And Reposession Processes

Whether a manufactured home is subject to the state foreclosure process or repossession process depends on several factors, including how it is titled and financed as well as whether or not it is permanently attached to the land. For example, if a borrower defaults on a mortgage loan in which the manufactured home is mortgaged as real property, the state foreclosure process typically applies.

The state foreclosure process may also apply when a manufactured home is considered a **fixture** to the real property and collateral for the mortgage loan, even if the manufactured home is classified as personal property and the mortgage loan funds were not used to purchase the home. For example, if someone paid cash for a manufactured home then permanently affixed it to land already secured by a mortgage, the manufactured home may become a fixture to the mortgaged real property which could be foreclosed on with the land. Conversely, a manufactured home is typically not considered a fixture and can be removed from the land upon foreclosure if the tongue, wheels, and axle were never removed.

> **Fixture**
>
> Physical property that is permanently attached to real property. A manufactured home is typically considered a fixture to real property and collateral for any mortgage on the land if it is permanently attached, even if the manufactured home is classified as personal property and the mortgage loan funds were not used to purchase the home.

Generally, the foreclosure process does not apply to manufactured homes classified as personal property and financed through a chattel loan or personal loan. Borrowers who default on a chattel or personal loan typically must navigate the repossession process similar to that of a vehicle loan.

Unlike vehicles, manufactured homes are not typically subject to **self-help repossession** in which a repossession agent can take the collateral away from the borrower without a court order. Self-help repossession laws state that repossession must not breach the peace or cause a public disturbance and prohibit agents from removing any personal property inside the home, which makes self-help repossession difficult for manufactured homes. To repossess a manufactured home, lenders often use a process similar to judicial foreclosure, called **replevin**, in which the lender files a lawsuit in court and requests the court grant an order for repossession.

Most states require lenders to provide borrowers with notice of impending repossession as well as the opportunity to pay off the outstanding balance to keep their home. Generally, a lender will not start the process of repossession until the borrower is behind on three or more payments.

Manufactured-home owners also have the option of **voluntary repossession** in which the surrender of the home is negotiated with the lender. Similar to a short sale on a mortgaged home, the lien on the home would be released for less than the borrower owes. The lender would then sell the home, which may result in a deficiency judgment for the difference between the sale price and the amount owed in addition to any storage charges or lot rent paid by the lender.

In the event a manufactured home on leased land is repossessed, the landlord or manufactured home community owner have the right to evict the homeowner and the home. Additional considerations for manufactured-home owners related to eviction from leased land are discussed in Module 6.2.

### Self-help Repossession

A type of repossession in which a lender's agent can take collateral away from the borrower without a court order, as with a vehicle repossession. Agents must not breach the peace or cause a public disturbance during a self-help repossession and are not permitted to take personal property other than the collateral.

### Replevin

A legal action to recover the possession of items of personal property used as collateral for a personal or chattel loan. The lender files a lawsuit in court and requests the court grant an order for repossession.

### Voluntary Repossession

The manufactured-home owner voluntarily surrenders the home to the lender outside of court. Similar to a short sale on a mortgaged home, the lien on the home would be released for less than the borrower owes. The lender would then sell the home, which may result in a deficiency judgment for the difference between the sale price and the amount owed in addition to any storage charges or lot rent paid by the lender.

## Knowledge Check 1

Below are the different options for a client considering a transition out of the home. Match each option with its definition.

A. Deed-in-Lieu
B. Foreclosure
C. Short Sale

___ 1. A legal process in which mortgaged property is sold to pay the loan of the defaulting borrower. Laws are based on the statutes of each state.

___ 2. A procedure in which the borrower is allowed to sell a property for an amount less than the outstanding mortgage balance owed to avoid a foreclosure. Also called a preforeclosure sale.

___ 3. A process that allows a homeowner to avoid foreclosure, providing a deed to the lender instead. Though it helps avoid foreclosure, the process does not allow the homeowner to stay in the home.

## Knowledge Check 2

Which potential outcome of a deed-in-lieu is considered beneficial to the homeowner?

A. Negative impact on credit for several years
B. Short-term inability to secure a new prime mortgage
C. Potential loss of equity built up in home
D. Financial assistance for relocation

## Knowledge Check 3

Review each manufactured-home owner situation to determine which disposition process typically applies to the manufactured home if the borrower defaults. For those covered by the state foreclosure process, place an "F" before the description. For those covered by the replevin process, place an "R" before the description.

___ A. The manufactured home was purchased separate from the land mortgage and the tongue, wheels, and axle were never removed.
___ B. The manufactured home is taxed and titled as real property as part of a mortgage.
___ C. The manufactured home is attached to leased land in a manufactured home park.
___ D. The manufactured home is part of a Resident Owned Community, or ROC.

## Transitioning from the Home

### Steps to Transition from Homeownership

In Module 5.1, we covered the general timeline for the foreclosure process. Let's build on that information as we discuss transitioning from the home.

Note that with conventional loans the processes for short sale and deed-in-lieu transactions vary greatly and do not have a fixed timeline. With a short sale, the homeowner will contact the servicer and determine if this option is available; submit a hardship letter and financial information; and provide a requested sales price based on comparable sales in the area, which the lender must approve. Though extensions may be granted in certain circumstances, lenders initiate foreclosure once an FHA loan has been in default for six months, so FHA pre-foreclosure sale and deed-in-lieu options must be evaluated before foreclosure can begin.

The lender will also give a homeowner a certain amount of time to secure a short sale offer, typically four to six months. An FHA pre-foreclosure sale allows 120 days for the sale and establishes minimum sales amounts based on appraisal values. If the homeowner cannot secure an offer, a deed-in-lieu can be requested, which turns the deed or title over to the lender. A deed-in-lieu can sometimes be requested without first attempting a short sale. In this situation the homeowner must show why the home is unaffordable and have the lender approve the request.

When a client decides to transition from the home through a foreclosure, short sale, or deed-in-lieu, the counselor can help the client by explaining the steps involved. This can make the transition go more smoothly and minimize the financial and credit damage. Though the transition options available through the Making Home Affordable, or MHA, program expired in December 2016, many states and localities have programs for homeowners facing foreclosure and proprietary programs may be available as well. Let's look at the steps to transition from homeownership.

| Steps to Transition from Homeownership | Who is Involved? | |
|---|---|---|
| | Client | Counselor |
| Determine servicer options based on type of mortgage. | X | X |
| Apply for desired option and applicable transition assistance. | X | X |
| Establish a budget for new housing. | X | X |

| Steps to Transition from Homeownership | Who is Involved? | |
|---|---|---|
| | Client | Counselor |
| Secure new housing prior to the sale date. | X | |
| Pack belongings and prepare for the move. | X | |
| Move into new housing. | X | |
| Begin to improve credit. | X | X |
| Discuss long-term plan for new home purchase, if applicable. | X | X |

## Foreclosure Alternative Programs

Although the MHA program that offered short sale or deed-in-lieu options, Home Affordable Foreclosure Alternatives, or HAFA, expired in December 2016, Michelle knows that is is beneficial to understand the concept of the program because some states and localities provide similar assistance.

The purpose of HAFA was to provide homeowners who could not afford mortgage payments the assistance needed to transition away from the mortgage into more affordable housing. Benefits for short sale programs may include completely releasing the homeowner from mortgage debt, or a deficiency judgment. This short sale option would have a less negative effect on a credit score than a short sale conducted directly with the servicer. Programs might also provide cash benefits to homeowners for relocation assistance.

Michelle is aware that borrowers with mortgages owned by a government sponsored entity, or **GSE**, may be eligible for programs through Fannie Mae or Freddie Mac, and she finds some helpful information. Let's take a look at the details.

**GSE Loan or Mortgage**

A government-sponsored enterprise, or GSE, is a financial services entity created by Congress. A GSE loan or mortgage refers to a mortgage owned by Fannie Mae or Freddie Mac.

### GSE Mortgage Disposition Options

The available short sale and deed-in-lieu options, which share some common elements, may be good for a borrower who:

- Is ineligible to refinance or modify the mortgage
- Is facing long-term hardship that qualifies under specific program criteria
- Is behind on mortgage payments, or in some cases, is at risk of falling behind in the near future

- Owes more on the home than it's worth, also known as an "underwater" mortgage
- Can no longer afford the home and is ready to leave

Counselors can research specific exceptions to most criteria on the Fannie Mae and Freddie Mac websites.

**Benefits:**

- Eliminate or reduce mortgage debt
- Avoid the negative impact of foreclosure
- Repair credit sooner than with a foreclosure
- Reduce time before eligibility to purchase a home again (in as few as two years, whereas foreclosure is seven)
- Be eligible for up to $3,000 in relocation assistance in some cases. (In certain states, relocation assistance for a deed-in-lieu may be as high as $7,000 for Freddie Mac mortgages and $10,000 for Fannie Mae mortgages.)

| | Short Sale | Deed-in-lieu or Mortgage Release |
|---|---|---|
| **Criteria for Fannie Mae & Freddie Mac** | **Purpose:** Allows a homeowner to sell the home for less than the balance owed, though a financial contribution, or a deficiency judgment, may apply depending on the situation.<br>**Process:** Typically, a homeowner considering a short sale has tried to sell the home but was unable to sell at a price that covers the mortgage balance.<br>A short sale may take up to 120 days. It is similar to a normal real estate sales transaction, though the mortgage company will work with the borrower and real estate agent on steps from setting the price to finalizing the sale. | **Purpose**: Allows a borrower who cannot afford the mortgage payments to voluntarily sign the house back over to the lender.<br>**Process:** Typically, a homeowner seeking a deed-in-lieu does not want or has not been able to sell the home. Homeowners will often attempt a short sale first.<br>A mortgage release usually takes about 90 days. Borrower qualifications determines the next steps, and qualified homeowners may be eligible for flexible exit options<br>• Immediately vacate home<br>• Stay in home for up to 3 months (no rent)<br>• Lease home at a market-based monthly rent for up to a year |
| **Eligibility Specific to Freddie Mac** | • Borrower has an eligible hardship<br>• Sale is an arm's length transaction (buyer and seller have no relationship to each other)<br>• Borrower previously listed home for sale with a licensed real estate broker according to specific criteria<br>• Borrower did not enter a program or arrangement where a third party takes the property title and arranges a short sale in exchange for a fee<br>• If borrower is current on mortgage or has been delinquent for less than 31 days, borrower must<br>• Occupy home as primary residence<br>• Have a monthly DTI ratio greater than 55% | • Servicer complied with the evaluation hierarchy<br>• Borrower has an eligible hardship<br>• Borrower can convey clear and marketable title to the property<br>• If borrower is current on mortgage or has been delinquent for less than 31 days, borrower must<br>• Occupy home as primary residence<br>• Have a monthly DTI ratio greater than 55% |

## Determining Servicer Options

The first step is to discuss the situation with the servicer to see if any of the three options—foreclosure, short sale, or deed-in-lieu—are available to the client. Then, the counselor and client evaluate available options and determine which to pursue. The next step involves formally applying for the option and any related financial transition assistance. Let's rejoin Michele and Penelope in their counseling session.

Michele. Now that we have determined that you have a conventional mortgage owned by Freddie Mac, let's go through your options for transition. The state offers financial transition assistance through funds received from the federal government. Your servicer may allow you to consider a short sale or deed-in-lieu, which could work in conjunction with the transition assistance.

Penelope. I was hoping that I could request a short sale option. Then I might not have to move out immediately, right?

Michele. Well, it depends. If no one presents an acceptable offer for a short sale by the lender deadline, that could give you more time. Also, a deed-in-lieu could become an alternative option.

At this point, it is likely you can avoid foreclosure. However, if foreclosure does become necessary, assistance may be available through initiatives such as "**cash-for-keys**," a last resort program to reduce the cost of an eviction. Your servicer would give you cash if you turn the property over in good condition.

Michele. Now, let me point out the Transitioning Program offered by our state. We're fortunate to have one, not every state does.  Let's look at the options and see which is best for you.

## State Transition Assistance Programs

Counselors must know what transition assistance programs are available to their clients. SProgram availability depends on several factors, including national economic conditions and general need. To find out what programs are available in your state, check with the state agency that governs foreclosures. This will typically be your state's Housing Finance Agency, Department of Community Affairs, Housing Department, or Attorney General's office.

## Selecting a Transition Assistance Program

Now that Penelope has had a chance to review the information on transition assistance programs. Let's rejoin her counseling session.

Michele. Since your servicer does not have a specific program, the state program looks like a good option. Do you want to apply for it?

Penelope. Yes, it sounds like it will be a straightforward process and seems to be the best long-term decision for me.

Michele. I agree. Over the next few days, let's work on putting the application together according to the guidelines. Right now, I'd like to create a new budget with you and help you determine how much you can afford to spend on rent.

**Cash-for-Keys**

An alternative to a legal eviction following foreclosure. The occupant receives cash funds from the servicer in exchange for turning in the keys and vacating the property. Certain conditions apply, such as returning the property in broom-clean condition with all appliances.

Penelope. Okay. I'd like to know what I could really afford.

Michele. With $1,800 in income, you should be paying no more than $540, or 30% of your gross income, on rent. I know this is low; we can apply for rental assistance programs to help.

Penelope. That amount won't go very far around here. I looked at one apartment in that price range, and it wasn't nice, and there were so many upfront costs, I could never afford it. They wanted $2,040 up front: $1,200 for security deposit, $540 for first month's rent, and $300 for a move-in fee. Maybe I should consider my daughter's offer to move in with her for a while and save some money.

Michele. That's an excellent option. While you think about that, let's look at how we can reduce your expenses and maybe find a way for you to bring in some income given your new work restrictions.

Michele and Penelope work together to create a budget that Penelope is comfortable with and that will enable her to pay down debts and save some money.

## FHA Transition Assistance Programs

Clients with FHA mortgages may be eligible to take advantage of other options. FHA offers preforeclosure sale (short sale) and deed-in-lieu options for its borrowers. As a prepared foreclosure counselor, Michele knows about these programs as well, and she has counseled other clients to help them with these transactions. Here is a brief description of them. HUD's Guidance for Homeowners and Loss Mitigation for Homeowners provide more information.

**Rent: 30% of gross income**

In general, clients should spend no more than 30% of their gross income on rental housing. In Penelope's case, $540 is 30% of her gross monthly income of $1,800.

## FHA Disposition Options

### Preforeclosure Sale (Short Sale)

**Purpose:** Allows a borrower in default to sell a home and use the proceeds to satisfy the mortgage debt, even if the proceeds are less than the amount owed

**Benefits:** Up to $1,000 in financial assistance

**Eligibility:**

- Property must be owner-occupied.
- Borrower must be 31 days delinquent or more at the time of the closing.
- Borrower must provide documentation substantiating a reduction in income or an increase in living expense and documentation that verifies the borrower's need to vacate the property (if applicable).
- Borrower must meet requirements for acceptable sales price and number of days on market.

### Deed-in-Lieu

**Purpose**: Allows a borrower who cannot afford the mortgage payments to voluntarily sign the house back over to the lender

**Benefits:** Up to $2,000 in financial assistance

**Eligibility**:

- Property must be owner-occupied.
- Borrower must be 31 days delinquent or more at the time of the deed-in-lieu.
- Borrower must provide documentation substantiating a reduction in income or an increase in living expense and documentation that verifies the borrower's need to vacate the property.
- Lender will develop a written Deed-in-Lieu of Foreclosure Agreement, to be signed by both the borrower and lender, which contains all of the conditions under which the Deed will be accepted.

Counselors who are well-versed on the transition assistance programs available on the federal, state, and local levels can help clients find the best option to match their circumstances.

## Transitioning Timeline, Process, and Next Steps

Now let's continue with the remaining steps to help clients through the transition from their homes through a foreclosure, short sale, or deed-in-lieu.

| Steps to Transition from Homeownership | Who is Involved? | |
|---|---|---|
| | Client | Counselor |
| Determine servicer options based on type of mortgage. | X | X |
| Apply for desired option and applicable transition assistance. | X | X |
| Establish a budget for new housing. | X | X |
| Secure new housing prior to the sale date. | X | |
| Pack belongings and prepare for the move. | X | |
| Move into new housing. | X | |
| Begin to improve credit. | X | X |
| Discuss long-term plan for new home purchase, if applicable. | X | X |

## Knowledge Check 4

What does it mean for a mortgage to be underwater?

A. A mortgage required for any structure built at or below sea level

B. A home suffered flooding and resulting damages caused mortgage delinquency

C. A mortgaged property is worth less than the balance owed to the lender

D. A borrower is drowning in late payments and trying to become current

## Knowledge Check 5

When a borrower is trying to avoid foreclosure, a mortgage company will usually consider a ______ before a ______.

A. deed-in-lieu, short sale

B. short sale, deed-in-lieu

## Knowledge Check 6

Lenders often offer short sale or deed-in-lieu options for homeowners trying to sell the home quickly before attempting a regular home sale.

A. True

B. False

Michele and Penelope meet again a week later and discuss these steps. Let's listen to their conversation.

MICHELE. With our goal of a short sale in mind, and with the application for financial transition assistance submitted, let's talk about the moving process. Have you decided if you will move in with your daughter or if you want to find a rental?

PENELOPE. I'm going to move in with my daughter. It will let me save money for a little while and pay off my debts.

MICHELE. This is a good decision, and it will make the transition easier. You can live in your home and pack for the move until the short sale goes through, which could take a while. This will help you save even more money.

## Transitioning Obstacles and Solutions

By moving in with her daughter, Penelope will not be affected by the uncertainties that come with transitioning to a new home. Let's take a look at some of the uncertainties and issues that clients may face when looking for a rental home.

**Client: Drew**

**Issue Faced When Looking for Rental**

**Limited Time to Secure Housing**

Drew was behind on his mortgage and went through the foreclosure process. On the day his home was sold, he received a notice that he had three days to vacate the property.

**Limited Time to Secure Housing**

Though clients in foreclosure may have limited time and options, clients who select short sale or deed-in-lieu often have more time to secure their next housing arrangement.

**Solution:**

**Plan Ahead for the Unexpected**

Because  clients in foreclosure may have little notice and **limited time to vacate the property** after the sale date, it is important to have an emergency plan in place, including designated short-term housing.

**Live with a Friend or Relative**

Clients may opt to stay with someone temporarily, paying no rent or contributing a reduced rent, which would allow them time to save money as well.

## Client: Penelope

### Issue Faced When Looking for Rental

**Limited Savings for Upfront Rental Expenses**

Penelope found an affordable apartment, but she did not have enough savings to cover the upfront rental costs and moving expenses.

**Solution:**

**Begin Saving Early for Upfront Rental Expense**s

Clients can benefit from taking the servicer's guidelines for transition programs into consideration and begin saving money as soon as it becomes clear that transitioning from the home is the only option.

**Live with a Friend or Relative**

Penelope chose to move in with her daughter temporarily in order to pay her debts and save money. Once her debts are paid, she will be in a better position to rent a unit on her own.

## Client: Danita

### Issue Faced When Looking for Rental:

**Poor Credit to Apply for New Housing**

Danita had delinquent mortgage payments, overdue medical bills, and other late items that had negatively affected her credit score even before her short sale was finalized. She tried to rent an apartment but struggled when her application was denied or the landlord charged high deposits that she could not afford.

**Solution:**

**Add a Lease Co-Signer or Pay Deposits**

Clients who cannot live with a friend or relative are often able to secure rental housing despite their bad credit. They may agree to pay higher security deposits or monthly rent, or they might add a co-signer to the lease.

**Live with a Friend or Relative**

Clients may opt to stay with someone temporarily, paying no rent or contributing a reduced rent, which would allow them to save money for upfront rental costs.

## Client Action Plan

Before Michele and Penelope finish their session, they discuss the next steps. Michele records these steps on a Client Action Plan that she began filling out at the beginning of their session. If Penelope follows the steps outlined, she will be able to pay off her debts, increase her credit score, and build savings so that she can eventually move out of her daughter's home.

Let's take a look at the Client Actions/Tasks portion of the client action plan.

**Client Actions/Tasks and Time frames:**

1. Pack up home and move in with daughter (by August 3, 2020)
2. Take steps to improve credit score, including:
   - Add a source of income in order to pay off medical bills and credit cards faster (by September)
   - Monitor credit by ordering free credit reports (bi-annually)
   - Pay debts on time (always)
   - Begin using credit cards wisely (beginning July 23, 2020)
3. Put 15% of income into savings each month (begin immediately)

Penelope. Do you think that I'll be able to look into buying again eventually?

Michele. It might be possible a few years down the road if you follow through with the steps on your action plan.

Short sales have a negative impact on credit standing, and lower credit scores may affect down payment requirements. It may take longer to save enough for a down payment if lenders require higher amounts.

Penelope. That's a good idea. For now I just want to get through this short sale and the move so I can start rebuilding my credit.

Michele has counseled Penelope through some very difficult decisions. Foreclosure counseling is not easy, and new options become available as often as others are removed. To best assist their clients, counselors need to dedicate time to learning about programs, eligibility criteria, and trends.

## Knowledge Check 7

What is the correct order of steps for clients that will transition out of the home?

A. Client secures new housing prior to the sale date.
B. Counselor and client formally apply for the desired option, as well as any financial transition assistance, and receive a response.
C. Client packs the home to prepare for the move, especially in foreclosure cases, because the client may not have much time to vacate the property after the sale date.
D. Counselor and client discuss the possibility of purchasing a new home if and when client is ready.
E. Counselor and client reach out to servicer to discuss available options, and then determine which to pursue.
F. Counselor and client work on improving credit to reduce the negative effects of foreclosure on the credit report.
G. Counselor analyzes client's information, and together the counselor and client establish a budget to determine how much the client can afford for new housing.
H. Client moves into new housing.

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## Knowledge Check 8

After the sale date of a home, which scenario could result in an eviction, typically with little notice to the client and under the enforcement of a law officer?

A. Short sale
B. Deed-in-lieu
C. Foreclosure

## Knowledge Check 9

Which action should a client avoid to secure rental housing after a foreclosure, short sale, or deed-in-lieu?

A. Wait until the sale is finalized.
B. Prepare to have a co-signer.
C. Secure housing before the sale is finalized.
D. Save for a security deposit.

## Summary

In this module, you learned to:

1. Explain the costs and consequences of a foreclosure (judicial and non-judicial), short sale, or deed-in-lieu.
2. Analyze a client's information if the client seeks to transition away from homeownership, demonstrating knowledge of programs that offer alternatives to foreclosure.
3. Apply knowledge of the foreclosure timeline, processes, and next steps to occur if a client is unable to stay in the home, devising appropriate action steps to assist the client in recovering from a mortgage default as soon as possible.

# Appendix

## Knowledge Check Answer Key

1. **Correct matched items:**

   (B) Foreclosure: 1. A legal process in which mortgaged property is sold to pay the loan of the defaulting borrower. Laws are based on the statutes of each state.

   (C) Short Sale: 2. A procedure in which the borrower is allowed to sell a property for an amount less than the outstanding mortgage balance owed to avoid a foreclosure. Also called a preforeclosure sale.

   (A) Deed-in-Lieu: 3. A process that allows a homeowner to avoid foreclosure, providing a deed to the lender instead. Though it helps avoid foreclosure, the process does not allow the homeowner to stay in the home.

2. **(D) Financial assistance for relocation**

   Relocation assistance can be offered for homeowners considering deed-in-lieu and other disposition options.

   Incorrect answers: (A) Negative impact on credit for several years; (B) Short-term inability to secure a new prime mortgage; and (C) Potential loss of equity built up in home are all negative impacts of a deed-in-lieu and other disposition options that do not benefit the client.

3. **Correct matched items:**

| (F) Foreclosure | (R) Replevin |
| --- | --- |
| B. The manufactured home is taxed and titled as real property as part of a mortgage—Since the manufactured home is financed with a mortgage, the state foreclosure process applies. | A. The manufactured home was placed on mortgaged land, but the tongue, wheels, and axle were never removed—The mortgage for the land would be covered by the foreclosure process, but the home would not be considered a fixture of the land because it is not permanently affixed. The manufactured home would be subject to replevin if the borrower defaulted on the manufactured home loan. |

| (F) Foreclosure | (R) Replevin |
|---|---|
| D. The manufactured home is part of a Resident Owned Community, or ROC—a manufactured home in an ROC is typically classified as real property and can be financed through a mortgage. Therefore, the state foreclosure process would typically apply. | C. The manufactured home is attached to leased land in a manufactured home park—Manufactured homes on leased land are not typically eligible for a mortgage, so the replevin process would apply to this situation in most states. |

4. **(C) A mortgaged property is worth less than the balance owed to the lender**

   Incorrect answers: (A) A mortgage required for any structure built at or below sea level; (B) A home suffered flooding and resulting damages caused mortgage delinquency; (D) A borrower is drowning in late payments and trying to become current

5. **(B) short sale, deed-in-lieu**

   Most servicers will look for ways to sell the property instead of accepting responsibility for it through a deed-in-lieu.

   Incorrect answer: (A) deed-in-lieu, short sale

6. **(B) False**

   The term "short sale" refers to a shortage in the amount repaid, not the length of the sale period. A regular home sale is often the best option for both homeowner and lender, though underwater mortgages and other circumstances may require the evaluation of alternative options, such as a short sale or deed-in-lieu.

   Incorrect answer: (A) True

7. **Correct order:**

   (E) Counselor and client reach out to servicer to discuss available options, and then determine which to pursue.

   (B) Counselor and client formally apply for the desired option, as well as any financial transition assistance, and receive a response.

   (G) Counselor analyzes client's information, and together the counselor and client establish a budget to determine how much the client can afford for new housing.

   (A) Client secures new housing prior to the sale date.

   (C) Client packs the home to prepare for the move, especially in foreclosure cases, because the client may not have much time to vacate the property after the sale date.

   (H) Client moves into new housing.

(F) Counselor and client work on improving credit to reduce the negative effects of foreclosure on the credit report.

(D) Counselor and client discuss the possibility of purchasing a new home if and when client is ready.

8. **(C) Foreclosure**

   After a foreclosure sale, homeowners are typically given a certain number of days to vacate the property, but they should be prepared to leave with only a few days' notice.

   Incorrect answers: (A) Short sale and (B) Deed-in-lieu—In these transactions, the homeowner is given a date by which they are to vacate the property.

9. **(A) Wait until the sale is finalized**

   Because the client's credit score will be negatively impacted, s/he should try to secure housing prior to the finalization of the sale.

   Incorrect answers: (B) Prepare to have a co-signer—Because the client's credit score will be negatively impacted, s/he should be prepared to have a co-signer in case the landlord requires it; (C) Secure housing before the sale is finalized—Because the client's credit score will be negatively impacted, s/he should secure housing prior to the finalization of the sale; and (D) Save for a security deposit—Security deposits are a normal part of any rental, and the client might have to pay more due to bad credit.

## Resources

### Penelope's Client Action Plan

| Client Action Plan | | |
|---|---|---|
| **File #:** 000HUD899 | **Counselor:** Michele | **Client Name:** Penelope |
| **Date:** July 23, 2020 | **Purpose of Visit:** Foreclosure Counseling | |

**Housing Goal(s):**

1. Avoid foreclosure and transition away from homeownership within three months
2. Minimize impact to credit standing and overall financial health, ongoing
3. Secure new housing before moving out of house

**Obstacle(s):**

1. Income reduced; Penelope is unable to work due to illness
2.
3.

| **Financial Snapshot:** | | **Income Summary:** | |
|---|---|---|---|
| **Current Credit Score** | **---** | o | Full Time Employment |
| **Current Savings** | **$0** | o | Part Time Employment |
| **Gross Monthly Income (GMI)** | **$1,800** | o | Self-Employment |
| **Net Monthly Income** | **$1,800** | o | Child Support |
| **Current Monthly Expenses** | **$2,800** | o | Spouse/Partner Employ |
| **Monthly Debt Obligations** | **$360** | o | Pension |
| **Discretionary Income Left Over** | **n/a** | o | Retirement/Soc Sec |
| **Current Mortgage/Rent** | **$1,440** | x | Other |
| **Housing Ratio** | **80%** | | |
| **Debt-to-Income Ratio** | **100%** | | |
| **Housing & Transportation Ratio (renters)** | **n/a** | | |

| **Housing Preferences:** | *Needs* | *Wants* |
|---|---|---|
| *Types & Features* | n/a | n/a |
| *Location* | n/a | n/a |

**Counselor Actions/Tasks and Time Frames:**

1. Follow up with Penelope to review progress (by September)

| **Client Actions/Tasks and Time frames:** |
| --- |
| 1. Pack up home and move in with daughter (by August 3)<br>2. Take steps to improve credit score, including:<br>• Add a source of income in order to pay off medical bills and credit cards faster (by September)<br>• Monitor credit by ordering free credit reports (bi-annually)<br>• Pay debts on time (always)<br>• Begin using credit cards wisely (beginning July 23)<br>3. Put 15% of income into savings each month (begin immediately) |
| **Referrals:**<br>1. Keep Your Home California, keepyourhomecalifornia.org<br>2. |
| **Next Appointment: September 12, 2020** |
| **Client Signature:** *Penelope* **Date:** July 3, 2020 |
| **Counselor Signature:** Rebecca **Date:** July 3, 2020 |

## FHA's National Servicing Center

www.hud.gov/program_offices/housing/sfh/nsc

## HUD Guidance for Homeowners

www.hud.gov/program_offices/housing/sfh/owning

## HUD Loss Mitigation for Homeowners

www.hud.gov/program_offices/housing/sfh/nsc/lossmit

## IRS

www.irs.gov