When Mortgage Woes Hit Home

If you, like millions of Americans, have trouble making your payments, here's help

In September 2006 Joan Smith (not her real name), a nurse in rural New Jersey, bought a piece of the American dream: a four-bedroom house for $269,000–with no money down. Smith had hoped to obtain a 30-year fixed-rate loan but since she had once declared bankruptcy, she qualified only for a subprime adjustable-rate mortgage (ARM), so called because the borrower's credit is less than "prime," or perfect. These loans come with steep interest rates. Smith's was set with an initial rate of 9.85 percent for two years; for each of the remaining 28 years of the loan, it will readjust based on a fluctuating index, and is likely to be higher.

Smith is current on her mortgage of $2,909 a month, which includes local taxes, but when the interest rate adjusts later this year, her payment could increase by $300 to $400–an amount she may not be able to afford. "It's already a stretch, and I don't have much left over after all the bills are paid," says Smith, 36, a single mother of five children who earns $65,000 a year. Refinancing isn't an option: Three lenders have turned her down because of her poor credit rating. "Unless I improve my financial situation, I'm afraid I'll lose my house," she says.

Smith isn't alone. The "teaser" rates on many subprime ARMs–issued at the height of the housing boom in 2005 and 2006 to borrowers with low credit scores–are set to expire this year. And when the higher rates kick in, the mortgage meltdown that has rocked Wall Street and driven up foreclosures nationwide stands to get even worse, experts agree. People all over the country, and in all income brackets, are being affected.

Of course, subprime borrowers aren't the only ones who have to worry about defaulting: Anyone experiencing a cash flow problem, whether due to job loss, illness, death or divorce, can have trouble making payments. If you're facing a mortgage crisis or if you're already in default, all hope isn't lost. Here are six steps you can take right now to get back on track and delay foreclosure: CONTINUED

ILLUSTRATION, TIM MARRS

WHY GETTING A HOME LOAN JUST GOT HARDER

Are you in the market for a home-equity loan to reduce credit card debt, build a new deck on your house or help fund your child's college education? Well, not so fast! Home-equity loans have long been popular—the interest can be tax-deductible and the rates are affordable—but may not be an option for Americans with badly damaged credit.

"The credit markets have tightened as a result of the mortgage crisis, so it's now harder to get a home-equity loan," says Susan Martin, executive vice president for consumer education at Countrywide Financial.

What's more, property values have declined in some areas of the country, which lowers the equity you can borrow against. If your credit is strong, you're still likely to qualify for a home-equity loan. But don't borrow too much—and certainly not 100 percent of your home's value. "If the price of your home goes down and you try to sell, you'll end up owing more on your home-equity loan than what your house is worth—and the difference will have to come out of your pocket," cautions Fran Fusco, senior vice president for retail at Continental Bank, in Plymouth Meeting, Pennsylvania.

#1: Talk to a housing counselor. Though it's hard to know exactly where to turn for guidance, a neutral third party trained to help homeowners can point you in the right direction. The Department of Housing and Urban Development (*www.hud.gov*) maintains a nationwide directory of 2,300 HUD-approved agencies where counselors can evaluate your situation and recommend a multistep action plan, which may include negotiating a loan modification with your lender, slashing monthly expenses and referring you to an attorney if it seems that you're the victim of a mortgage scam.

Though you shouldn't get scolded for your past financial mistakes, you will hear tough talk from counselors about what you must do to dig yourself out. Counseling services are free, though there may be charges of up to $30 if the counselor runs your credit report. Call for an appointment at the first sign of trouble. Depending on their state, borrowers who are in foreclosure may have as few as 30 days before their home is sold, so the more time you have to work on a recovery plan, the better your chance of keeping your house, says Jerri Scott, a housing counselor with Iowa Citizens for Community Improvement, in Des Moines.

#2: Contact your lender. "If you can't make your mortgage payment and feel as though you're marching toward foreclosure, your natural instinct may be to hide under the bed," says Susan Martin, executive vice president for consumer education at Countrywide Financial, in Calabasas, California. But that's the worst thing you could do. Though the loan won't be forgiven, lenders often make accommodations to help you through a financial squeeze–or the rest of the life of the loan–but it's up to you to be proactive. When you call the lender's customer service center, you should disclose how you got into a mortgage crisis and provide documents that substantiate the reason (such as medical bills if you've lost income due to illness). Be prepared to submit a copy of your monthly household budget and explain your strategy for financial recovery. "The lender needs to know that you're not taking trips to the Caribbean instead of paying your mortgage," Scott says. Here are some options you can present to the mortgage company:

• Request a forbearance. This would enable you to skip payments or make partial payments while you get back on your feet–then add the outstanding amount to the end of the loan.

• Negotiate a loan modification. It's a temporary or permanent change in one or more of the loan's terms to make the monthly payment affordable. The lender might lower the interest rate, extend the life of the loan or re-amortize the loan balance.

• Try to refinance the loan to one with a fixed rate. Your monthly payment could be less than the amount you'd pay after the ARM with the higher interest rate adjusts. But if your credit rating is sufficiently damaged, warns Scott, you may qualify only for a higher mortgage rate than the one you currently have.

• Set up a repayment plan. This is a formal arrangement between you and the lender that outlines how you'll spread the delinquent amount over a period of time–perhaps several months or longer, while making your regular payments–until everything is repaid and the loan is current.

Mortgage companies are motivated to come up with creative solutions for cash-strapped borrowers: A report by the mortgage financing company Freddie Mac noted that lenders lose an average of $58,782 per property that goes CONTINUED ON PAGE 52

into foreclosure, because of the expenses involved: legal fees, insurance, taxes and maintenance. Ask a housing counselor to help you negotiate a solution with your lender, and if that fails, consider hiring an attorney to make your case.

#3: Seek government assistance. HUD's Federal Housing Administration (FHA) has enhanced its refinancing program to help 240,000 low- to moderate-income families avoid foreclosure in 2008. Under the new FHASecure plan, borrowers who were current on their mortgages before their ARMs reset—but are now in default because the payment skyrocketed beyond their means—may qualify to refinance to 30-year fixed-rate loans that are insured by the federal government. This option is also available to borrowers who haven't fallen behind on their mortgages but still want to refinance. To be eligible, you need to have 3 percent cash or equity in your home, ongoing employment, enough income to make the mortgage payment and a loan that either reset or will reset between June 2005 and December 2008. For more information, go to *www.fha.gov* or call 800-CALL-FHA.

Meanwhile, some states are establishing "rescue funds" to allow struggling homeowners to refinance into fixed-rate loans. Check with a housing counselor to learn what's available and how to qualify.

#4: Reduce credit card debt. If your payment history is good, ask your credit card company to lower its interest rate on your monthly balance. By putting more money toward the principal, you'll reduce your credit card balance—and ultimately improve your credit score and debt-to-income ratios. "When you try to refinance your mortgage you'll have a better shot at qualifying for a lower-interest rate when you have a strong credit score and manageable debt-to-income ratios," says Stephanie Bittner, a credit and housing counselor at the Consumer Credit Counseling Service of Delaware Valley, in Cherry Hill, New Jersey. A free copy of your credit report is available at *www.annualcreditreport.com.*

#5: Sell your house. When you're several months delinquent on your mortgage and foreclosure seems unavoidable, you might have no choice except to put your home on the market to preempt a sheriff's sale.

In today's buyer's market—where housing prices are tumbling and inventory is rising—you might have to sell your house at a loss to get a quick deal. Still, this strategy could be the answer. If you owe $250,000, and the highest bid you get for your house is $240,000, the mortgage company might conduct a "short sale," agreeing to take $10,000 less to avoid the expense and legal hassles of foreclosure, Bittner says. Before you stick a for-sale sign in your front lawn, ask the lender whether it will accept a reduced payoff amount and then send documentation that proves you're working with a real estate agent.

#6: File for Chapter 13 bankruptcy. This option may be worth deliberate consideration, but it's also a serious catch-22. On the positive side, declaring bankruptcy will delay foreclosure, as it gives you up to five years to get current on your delinquent mortgage payments (while staying current on the regular payments). It also enables you to consolidate unsecured debt, such as credit card bills, and negotiate a court-approved payment plan. In some cases a judge may even forgive all of your unsecured debt—or a significant portion, though you'll be subject to a means test set by Congress. "If you're earning a good income and don't fall below the means, the court will make you pay it back," says Brian Mildenberg, a real estate and consumer rights lawyer in Philadelphia.

On the downside, declaring bankruptcy will further damage your already-tarnished credit score—and stay on your credit report for seven years. Plus, it can prove costly. As a result of recent changes in bankruptcy laws, it's now more complicated for individuals to file without an attorney, and they're prone to making mistakes that can delay the process at a time when every day counts, according to Bittner. The new laws have also made it a more time-consuming project for lawyers: In Philadelphia, notes Mildenberg, lawyer fees have doubled from $1,500 to $3,000 in bankruptcy cases.

Boost Your Credit Score

If you're plagued by debt, your mortgage payments are just one part of the monthly tally. Learn how to regain solid financial footing, boost your credit score and avoid bad family spending habits. It's all at **WWW.LHJ.COM/DEBT**