



Financing Issues in Today's
Market
VREB Approval #: 58071

Potomac Real Estate School
Box 494
Oakton, Virginia 22124

Telephone: (703)758-0034

Fax: (703) 758-0044

info@PotomacRESchool.com

Instructions for 5 Hour Financing Issues in Today's Market Correspondence Course

You have chosen to take the 5 hour Financing Issues In Today's Market course by correspondence. You may either read it online or print it. After you complete each section, take the quiz. Blank answer sheets are provided for you at the end of this packet; please record your answers there. **You must answer the questions for all 3 sections.** The Virginia Real Estate Board requires a passing grade of 75% or higher.

Complete the Certification Sheet. **Have the Student Declaration notarized.** The Virginia Real Estate Board has given you the option of either sending the notarized affidavit to us or keeping it with your records.

Mail, fax, or scan and email the completed answer sheets, certification sheet and Student Declaration to us. Our mailing address is Box 494, Oakton, Virginia 22124. Our fax number is 703-758-0044. Our email address is info@PotomacRESchool.com.

Your information will be held in the strictest of confidence.

You will not be charged unless you pass the exam. If you do not pass, you will be notified immediately.

Once we have received the required paperwork from you and you have been charged, we will report your hours to DPOR and email your certificate to you. The Real Estate Board requires that we report your hours to DPOR within 5 days of receipt of your paperwork. If you need reporting in less than 5 days, please let us know.

If you have any questions, please call or email us. Our phone number is 703-758-0034. For questions of a general nature, you can call or email us at info@PotomacRESchool.com. If you have questions about the content of the course, you can call or email me at patti@PotomacRESchool.com.

Thank you.

Patti Chapell

Patti Chapell
Director

Linking Learning To Success®

TABLE OF CONTENTS

Name of Course	Page
Predatory Lending	4
Mortgage Fraud	13
Ins and Outs of Short Sales	23

Predatory Lending

1 – Responsible Lending

- According to NAR, in testimony before the U.S. Senate Committee on Banking, Housing and Urban Affairs, abusive and predatory lending practices are putting our nation's communities at risk. These practices can cause more families to lose their homes and savings through higher foreclosure rates.
 - All Realtors should seek to prevent abusive lending because abusive lending erodes confidence in the Nation's housing system
 - Not all sub-prime lending is predatory or abusive, and NAR supports federal legislation and regulation that prevents predatory lending while maintaining a role for responsible sub-prime lending.
- What are responsible lending principles?
 - NAR supports the general principle that all mortgage originators should act in "good faith and with fair dealings" in a transaction and treat all parties honestly.
 - Affordability
 - NAR supports strong underwriting standards that require all mortgage originators to verify the borrower's ability to repay the loan based on all its terms, including taxes and insurance, without having to refinance or sell the home.
 - Underwriting Sub-prime Loans with "Teaser Rates"
 - Some sub-prime loans are structured with a significant jump in monthly payments often resulting in "payment shock" for the borrower. While these mortgages may be a reasonable choice for sub-prime borrowers who can afford them, a majority of sub-prime borrowers do not understand the unique terms and conditions of these risky mortgage products that can result in a significant "payment shock." Therefore, lenders (including mortgage brokers) should exercise more caution when underwriting such loans to sub-prime borrowers to make sure the borrower is able to afford the mortgage. Examples of these risky mortgage products include loans with a short-term interest "teaser" rate for the first two or three years (known as 2/28s and 3/27s), loans with an initial interest-only period and mortgages that negatively amortize.
 - Reasonable debt-to-income ratio
 - NAR supports requiring lenders to make sub-prime loans that have a reasonable debt-to-income ratio. Borrowers should have enough residual income after making their monthly mortgage payment, including taxes and insurance, to meet their needs for food, utilities, clothing, transportation, work-related expenses and other essentials. Requiring underwriting at a fully amortizing, fully indexed rate is meaningless if the lender uses such high debt-to-income ratios that the family doesn't have enough income remaining to pay for other necessities.
 - Escrow/Reserve for payment of taxes and insurance

- Lenders that make sub-prime mortgage loans should generally require that the monthly payment include an amount to be held by the mortgage servicer in an escrow/reserve/impound account for the payment of the borrower's periodic payments, such as taxes and insurance. Similar to the exception for prime loans in some jurisdictions, borrowers that make at least a 20 percent down payment should have the option to budget for these payments independently.
- Limit Stated Income/Stated Assets Underwriting
 - Because mortgages underwritten based on "stated income" and/or "stated assets" (also known as "no income verification" or "no doc" loans) typically have higher rates, lenders making sub-prime loans should, as a general rule, underwrite loans based on verified income and assets. The main exception should be for borrowers whose incomes derive from hard-to-verify sources (such as self-employed borrowers).
- Flexibility for Life Circumstances
 - NAR believes that a standard for determining a borrower's ability to repay must be flexible to accommodate borrowers with unique circumstances, such as
 - Borrowers who have demonstrated the ability to make monthly payments over a long term, that are higher than underwriting standards would otherwise allow. Lenders should consider, for example, the borrower's history of making rent and student loan payments.
 - Borrowers with high assets but low income who, for cash management or other financial planning reasons, elect a mortgage with a monthly payment that their current income is not sufficient to cover.
 - Borrowers who anticipate a jump in income or assets due to life events such as graduation, completion of professional training, completion of payment obligations for student or car loans, another member of the household entering the work force when young children start school or an inheritance.
- Anti-Mortgage Flipping Policy
 - NAR supports an anti-mortgage flipping rule requiring mortgage originators making or arranging for a loan that refinances an existing residential mortgage, to verify that the new loan provides a significant benefit to the borrower. The lender should consider the circumstances of the borrower and all terms of the new loan including taxes and insurance, fees and other costs of refinance, prepayment penalties and the new interest rate compared to that of the refinanced loan.
- Bar Prepayment Penalties
 - NAR opposes prepayment penalties for all mortgages. Prepayment penalties often work to trap borrowers in loans they cannot afford by making it too expensive to refinance. If complete prohibition of prepayment penalties is not feasible, NAR supports permitting prepayment penalties for the shortest time and the lowest amount possible. For example, a borrower in a 2/28 mortgage should be able to refinance by the end of the initial two-year "teaser" rate period without having to pay a prepayment penalty.
- Improvements for Assessing Creditworthiness
 - Borrowers with little or no credit history, as traditionally measured, usually have lower credit scores and must pay more every month for their mortgage than those with higher scores. NAR supports ongoing efforts to take into account consumer payment history not typically

considered, such as rent, utility, telephone and other regular payments and urges HUD, the regulators, the GSEs (government-sponsored enterprises), and lenders to work to strengthen these efforts. Use of alternative credit approaches will be especially beneficial for low- and moderate- income first-time homebuyers and borrowers with problematic loans that need to refinance their mortgage to avoid foreclosure.

- Another public policy issue associated with credit histories is the failure of furnishers to report good payment histories to the consumer reporting agencies. NAR has heard reports that many problematic sub-prime lenders purposefully withhold information on timely mortgage payments from the credit bureaus in order to prevent their customer from refinancing with another lender. The result is obvious – the borrowers with no positive payment histories for their sub-prime loan keep treading the waters of high-interest rates and expensive credit products. NAR supports requiring all institutional mortgage lenders, or the mortgage servicers acting on their behalf, to report payment history of all borrowers to at least the three national credit bureaus on a monthly basis.

2 - Responsible Lending

- Mortgage Choice for Borrowers
 - NAR supports requiring mortgage originators to offer borrowers one or more mortgages with interest rates and other fees that appropriately reflect the borrower's credit risk. It remains the responsibility of borrowers to decide which is the best mortgage for their needs and circumstances, but they may only do so if they understand all the facts so they can make an informed decision. For originators who offer nontraditional mortgage products, the originator should
 - Offer all borrowers a choice of several significantly different mortgage options
 - Include at least one traditional loan product as one of the options for the borrower to consider, if the borrower qualifies for such a product offered by the originator and,
 - Before application acceptance, disclose information about the maximum potential payment over the life of the loan and the date the initial payment will increase to a fully amortizing, fully indexed payment amount.
 - For sub-prime borrowers, originators that offer FHA insured mortgages or VA home loan guaranty mortgages, should consider whether these types of mortgages should be offered as an appropriate option
 - If the originator does not offer mortgages with rates and fees appropriate for the borrower's credit risk, the originator should inform the borrower a lower interest rate may be available from another originator or that the borrower may wish to seek housing counseling to allow the borrower an opportunity to shop elsewhere or receive counseling before proceeding.
 - For loans originated by a mortgage broker, the broker should offer mortgage options that are among the lowest-cost products appropriate for the borrower.
- Enforcement/Remedies

- NAR supports enactment of strong remedies and penalties for abusive acts by mortgage originators. Among the options for consideration are
 - Criminal penalties similar to those under RESPA
 - Civil penalties similar to those under RESPA
 - Prohibition of mandatory arbitration clauses that bar victims' access to court
- Improved Consumer Mortgage Disclosures
 - Lenders have a responsibility to ensure that consumers understand the loans they receive, including their terms and all costs. Consistent with this principle, NAR recommends that HUD improve consumer disclosures under the Real Estate Settlement Procedures Act (RESPA). In particular, NAR believes that consumers should receive a Summary GFE (Good Faith Estimate), accompanied by a detailed GFE with explanations for each subcategory of fees to help consumers more fully understand the services they are receiving and the cost of each service. The revised GFE should closely parallel the HUD-1 settlement form so consumers can compare the GFE they receive when they apply for a loan to their closing documents at settlement.
- Strengthen Appraiser Independence
 - NAR believes that the independence of appraisers should be strengthened to ensure that appraisals are based on sound and fair appraisal principles and are accurate. There are reports that appraisers have been pressured to meet targeted values or risk losing business. Appraisal pressure undermines the integrity of the mortgage lending process if the result is a mortgage loan made based on an inaccurate property valuation. NAR recommends the following measures to strengthen the appraisal process:
 - Require lenders to inform each borrower of the method used to value the property and give the borrower the right to receive a copy of each appraisal
 - Establish enhanced penalties against those who improperly influence the appraisal process. Those with an interest in the outcome of an appraisal should only request the appraiser to
 - consider additional information about the property
 - provide further detail, substantiation or explanation for the appraisal and
 - correct errors
 - Provide federal assistance to states to strengthen regulatory and enforcement activities related to appraisals
 - Support enhanced education and qualifications for appraisers

Copyright National Association of REALTORS, Reprinted with permission

3 – Predatory Lending

- What are “prime” and “sub-prime” loans?
 - Until fairly recently, only a borrower with good credit could purchase a home. Those with poor credit were prevented from obtaining a loan. Loans to these creditworthy borrowers were called “prime” loans.
 - In recent years, some lenders decided to take on those with poor credit and offer them “sub-prime” loans. Borrowers obtaining sub-prime loans posed more of a risk to lenders; therefore, measures were taken to compensate the lenders of these loans for the added risk taken.
 - Usually the interest rate was higher than that for a prime loan.

- Pre-payment penalties were stiffer.
 - In some, interest rates fluctuated more frequently.
- What is predatory lending?
 - According to the Federal Trade Commission, a predatory loan is “an unsuitable loan with abusive terms.” NAR lists nine possible warning signs that may indicate an abusive loan:
 - Interest rates or fees that are much higher than the local market average
 - Balloon payments or payments that will greatly increase over the life of the loan
 - A balloon payment is a loan with periodic payments that are not enough to fully amortize the loan by the time the final payment is due; therefore, the final payment is larger than the others.
 - Pre-payment penalties or other barriers to refinancing
 - “No down payment” loans
 - Short “Introductory Rate” periods
 - Inflated property appraisal
 - Offers to lend more money than the borrower has the ability to repay
 - Fees for nonexistent products or services (“junk fees”)
 - Unethical loan document management
- Who is affected by predatory lending?
 - Usually, first-time homebuyers
 - Borrowers refinancing on the verge of losing their homes
 - Elderly
 - Minorities
 - Immigrants
 - Individuals with Low Credit Scores
 - Low income buyers
 - Predatory lenders target certain groups of people and use pressure tactics to force borrowing decisions that are not in the best interest of those people.
- What has precipitated predatory lending?
 - Appreciation in the price of homes has brought about these abusive loans in an effort to get people into houses they cannot afford.
- FBI tips to protect the consumer from becoming a victim of predatory lending
 - Before purchasing a home, the consumer should research information about prices of homes in the neighborhood.
 - The purchaser should shop for a lender and compare costs. He also needs to beware of lenders who tell him that they are his only chance of getting a loan or owning his own home.
 - The consumer should beware of “No Money Down” loans. This is a gimmick used to entice consumers to purchase property that they likely cannot afford or are not qualified to purchase. The consumer should be wary of the mortgage professional who falsely alters information to qualify him for the loan.
 - The consumer should not let anyone convince him to borrow more money than he can afford to repay.
 - The consumer should not let anyone persuade him into making a false statement such as overstating his income, the source of his down payment or the nature and length of his employment.
 - The consumer should never sign a blank document or a document containing blanks.
 - The consumer should read and carefully review all loan documents signed at closing or prior to closing for accuracy, completeness and omissions.
 - The consumer should be aware of cost or loan terms at closing that are not what he agreed to.
 - The consumer should not sign anything he does not understand.

- If it sounds too good to be true, it probably is.
- How can we, as Realtors, help prevent predatory lending?
 - Recognize the warning signs.
 - Educate our buyers about the mortgage lending process.
 - Ensure that our clients fully understand all aspects of the home buying process.
 - In some cases, refer our buyers to a financial advisor or counseling organization.
 - Share resources, such as the following, with our buyers:
 - Freddie Mac – “Don’t Borrow Trouble” campaign
http://www.dontborrowtrouble.com/en/anti_predatory.html
 - National Community Reinvestment Coalition – Anti-Predatory Lending Toolkit:
<http://www.ncrc.org/policy/predatoryLending.php>
 - My Money – the Federal Government’s Website with links to many sites, including those on the following subjects: Budgeting and Taxes, Credit, Financial Planning and Homeownership.
www.MyMoney.gov
 - HUD’s Website – a wealth of information about home buying
www.hud.gov/buying/index.cfm
 - Freddie Mac’s Credit Smart Program – helps consumers understand, build, and maintain better credit
www.freddiemac.com/creditsmart
 - FDIC’s Money Smart Program – “a training program to help adults outside the financial mainstream enhance their money skills and create positive banking relationships”
www.fdic.gov/consumers/moneysmart/overview.html
 - Credit-Power – targets students and contains information about credit and homeownership
www.credit-power.org/default_eng.asp
 - A brochure, “Shopping for a Mortgage? Do Your Homework First,” produced jointly by NAR and the Center for Responsible Lending, identifies the warning signs of predatory loans. It outlines interest-only mortgages, negative amortization mortgages and option payment ARM mortgages. It also gives consumers tips on how to avoid these loans, and includes questions consumers should ask when shopping for a mortgage. Questions include
 - “How much can my monthly payments increase, and how soon can these increases happen?”
 - “Do I expect my income to increase, or do I expect to move before my payments go up?”
 - “Will I be able to afford the mortgage when the payments increase?”
 - “Am I paying down my loan balance each month, or is it staying the same or even increasing?”
 - “Will I have to pay a penalty if I refinance my mortgage or sell my house?”
 - “What is my goal in buying this property? Am I considering a riskier mortgage to buy a more expensive house than I can realistically afford?”
 - Anyone can get a copy of this brochure by going to
<http://www.coloproperty.com/links/specialtymortgage.pdf>

*Copyright National Association of REALTORS,
Reprinted with permission*

- The Homeownership Preservation Foundation is a non-profit group that offers free counseling for victims of predatory mortgage lending. It can be contacted at 1-888-995-HOPE.
- On July 11, 2007, the NAACP filed a Federal class action lawsuit against fourteen of the country's largest sub-prime mortgage lenders.
 - This lawsuit is designed to bring about equitable lending practices that do not adversely affect borrowers based on their race.
 - In a 2006 study, the Center for Responsible Lending found that when creditworthiness and credit risk were equal, African-Americans were still 31 percent to 34 percent more likely to receive higher rates and more expensive sub-prime loans than Caucasians.
 - The National Community Reinvestment Coalition revealed that lenders on average made high-cost sub-prime loans to higher-qualified African-Americans 54% of the time, compared to 23% of the time for Caucasians, even when the Caucasian applicants were less qualified.
 - These and other studies demonstrate that African-American homeowners are paying higher mortgage interest rates than their Caucasian counterparts.
- The Mortgage Bankers Association reported that at least 1.3 million home mortgage loans were either seriously delinquent or in foreclosure at the end of September, 2007.
- Deal brokered with mortgage industry in December of 2007
 - Froze certain sub-prime loans – those offered to borrowers with weak credit histories – for five years if the borrowers could not afford the higher monthly payments as those loans adjusted after being at lower introductory rates
- Project Lifeline
 - Announced February 12, 2008
 - Program was put together by six of the nation's largest financial institutions, which service almost 50 percent of the nation's mortgages.
 - Homeowners who are 90 or more days overdue on their monthly mortgage payments would be able to put the foreclosure process on hold for 30 days while they attempt to work with the lenders to make their mortgages more affordable.
 - The group, calling themselves the "Hope Now Alliance," are comprised of the following banks:
 - Bank of America Corporation
 - Citigroup, Inc.
 - Countrywide Financial Corporation
 - J.P. Morgan Chase and Company
 - Washington Mutual, Inc.
 - Wells Fargo & Company
- Predatory Lending Legislation
 - Congress and many individual states have passed and are continuing to pass legislation to fight predatory lending.

Predatory Lending Final Quiz

1. Prevention of predatory lending is in the best interest of
 - a. Realtors
 - b. The public
 - c. Both a and b
 - d. Neither a nor b

2. Would a predatory loan be one which a consumer cannot afford?
 - a. Probably
 - b. No
3. The current housing crisis can be blamed on
 - a. Predatory lending
 - b. High rate of foreclosures
 - c. Shortage of building materials
 - d. a and b
4. All might be examples of predatory lending except
 - a. No documentation loan
 - b. 30 year fixed rate loan
 - c. No down payment loan
 - d. Loan with balloon payment coming after first two years
5. What is sub-prime lending?
 - a. Extending a loan whose rate is at least 5 points below prime.
 - b. Lending to high risk borrowers.
 - c. A loan that is available only to people who make over \$200,000 annually.
 - d. All of the above
6. Loan flipping is the practice of
 - a. Selling your home after the first month
 - b. Lowering the interest rate on a loan
 - c. Repeatedly refinancing a loan, often in the favor of the lender.
 - d. None of the above
7. What is a balloon payment loan?
 - a. A loan in which the required payments do not exceed the interest charged, often resulting in a large payment of the entire principal at the end of the loan term
 - b. The practice of adding extra charges, such as unemployment insurance, to the principal of a loan in order to increase the interest accrued
 - c. A special offer where the lending institution gives out promotional balloons to your children every time you refinance a loan
 - d. a and b
8. Which of these are warning signs of a predatory lending deal?
 - a. The lender tells you to misrepresent or falsify information on your loan application.
 - b. The lender pressures you into applying for more money than you need.
 - c. The lender fails to provide required loan disclosures or tells you not to read them.
 - d. All of the above
9. Why do sub-prime loans have higher interest rates than prime loans?
 - a. They are better loans.
 - b. Mortgage companies don't like them.
 - c. Both a and b
 - d. They are riskier loans; the higher interest rates help compensate the lender for the added risk.
10. Who would probably not be affected by predatory lending?
 - a. Middle-aged couples with a large down payment

- b. Immigrants
 - c. First-time homebuyers
 - d. Minorities
11. NAR is in favor of
- a. Barring pre-payment penalties
 - b. Eliminating the use of the HUD-1
 - c. Eliminating use of the Good Faith Estimate
 - d. None of the above
12. What is a pre-payment penalty?
- a. Extra fees that may be due if you pay off a loan early
 - b. Extra fees charged to sub-prime loans before the loan is approved
 - c. Another term for the points on a mortgage
 - d. None of the above
13. Why should the payment history of rent, utility and telephone bills be considered as part of certain borrower's credit history?
- a. Prompt payment of telephone bills is not essential
 - b. Some borrowers have lower than desirable credit scores just because they have little credit history
 - c. Both a and b
 - d. None of the above
14. What is the result of mortgage companies not reporting good payment histories to the consumer reporting agencies?
- a. Those with sub-prime loans can never refinance with a more favorable loan product
 - b. Those with sub-prime loans cannot raise their credit scores
 - c. Both a and b
15. For originators who offer nontraditional mortgages, the originator should
- a. Offer all borrowers a choice of several significantly different mortgage options.
 - b. Offer just one mortgage product
 - c. Always offer an FHA product
 - d. None of the above
16. If the loan originator does not offer mortgages with rates and fees appropriate for the borrower's credit risk, he should
- a. Offer the borrower one of his best products
 - b. Tell the borrower that he will not qualify for any type of mortgage.
 - c. Inform the borrower that a lower interest rate may be available from another originator.
 - d. None of the above
17. NAR supports enactment of strong remedies and penalties for abusive acts by mortgage originators. Among options for consideration are
- a. Civil penalties similar to those under RESPA
 - b. Criminal penalties similar to those under RESPA
 - c. Prohibition of mandatory arbitration clauses that bar victims' access to court
 - d. All of the above

Mortgage Fraud

Part 1 – What is Mortgage Fraud?

- What is mortgage fraud?
 - Mortgage fraud, according to the FBI, is “any material misstatement, misrepresentation or omission relied upon by an underwriter or lender to fund, purchase or insure a loan.”
 - Mortgage fraud is not the same thing as predatory lending. Mortgage fraud is when one or more individuals defraud a financial institution; predatory lending is when a dishonest financial institution willfully misleads or deceives the consumer.
 - Mortgage fraud may be perpetrated by one or more participants in a loan transaction, including the borrower, a loan officer who originates the mortgage, a real estate agent, appraiser, title representative or attorney or by multiple parties as in a fraud ring described below.
 - The mortgage industry estimates that 10 – 15 percent of the mortgage loans processed annually involve some type of fraud.
- There are two types of fraud.
 - Fraud for the home
 - According to the FBI’s “Financial Crimes Report To The Public Fiscal Year 2006,” 20 percent of today’s mortgage fraud stems from a home buyer lying about income, debt or other information in order to buy a home.
 - This involves the purchaser falsifying the loan application in order to buy a home that he cannot afford.
 - By inflating the income or omitting debt on the application, the purchaser can buy a more expensive home.
 - Typically, these buyers are sub-prime borrowers and don’t plan to default. Whether they are investors or homeowners, their intention is not to walk away with cash but to get a roof over their or someone else’s head. Sometimes real estate agents coach these purchasers to fill out the applications not according to the truth but according to what the banks want to see.
 - Fraud for profit
 - 80 percent of all mortgage fraud involves fraud for profit.
 - This typically involves a number of professionals who conspire to inflate the price of the home, such as an appraiser, a mortgage broker, an outside investor and straw buyer, real estate agent, title company representatives and even representatives of the lenders.
 - Fraud for profit is also called “Industry Insider Fraud”.
 - This type of fraud is committed by the real estate professionals and involve making loans and reselling them, knowing that the purchaser of the loan might never be repaid.
 - A study by BasePoint Analytics, a fraud research company, provides evidence that fraud for profit is widespread. The study showed that 70% of “early payment defaults” or non-payments at the beginning of the mortgage term, could be traced to loan applications with significant misrepresentations.
 - In an especially hard hit region, the Southwest, experts claim that the biggest scam has involved cash back schemes where the price of homes has been artificially inflated in order to give cash back to purchasers.
 - Some of those charged with mortgage fraud try to hide behind the push for greater home ownership, claiming that they are just helping people get into homes.

Part 2 – Examples of Mortgage Fraud

- What are some examples of mortgage fraud?
 - Undisclosed kickbacks
 - When a seller gives money to a buyer for repairs that are not part of the sales contract, fraud is committed. The buyer and seller or the buyer and real estate agent collude to deceive the lender as to the true sales price of a property. The seller or the real estate agent gives the buyer a cash rebate which is not disclosed to the lender. As a result, the lender lends too much, and the buyer and/or seller pocket the overage.
 - All exchanges of money need to be approved by the lender and need to be on the HUD-1.
 - Foreclosure schemes
 - Homeowners who are in default are targeted by unscrupulous individuals who claim that the homeowners can save the house in exchange for a transfer of the deed and upfront fees.
 - Purchase loans disguised as refinance
 - Purchase loans that are disguised as refinances require less documentation and lender scrutiny.
 - Silent second mortgage
 - A silent second is a second mortgage given the purchaser by the seller, used as the purchaser's down payment, and hidden from the lender.
 - Falsifying employment income occurs
 - Anytime that a purchaser inflates his income, whether he is self-employed or employed. This often occurs in "stated income" or low doc or no doc loans, which do not require verification. In some cases, the borrower alters an employer-issued W-2 to overstate income.
 - Failure to disclose liabilities
 - Some borrowers may conceal other mortgages or recent additional credit card debt in order to obtain larger loans.
 - Occupancy fraud
 - This occurs when an investor is purchasing a property and claiming on the sales contract and loan application that he is planning to occupy the property. This is done to obtain a loan with more lenient down payment guidelines and lower interest. The lender is defrauded because he is making a riskier loan and is not being compensated for the additional risk.
 - Mortgage fraud rings
 - Multiple parties are involved in financially motivated attempts to defraud lenders of large sums of money.
 - Some schemes involve a straw borrower whose credit report is used, a dishonest appraiser who intentionally and significantly overstates the value of the subject property, a dishonest attorney who prepares two sets of HUD closing documents and a property owner, all in a coordinated attempt to obtain an inappropriately large loan. If undetected, a bank may lend hundreds of thousands of dollars against a property that is actually worth far less. The parties involved split the illegal gains and disappear without making one payment on the mortgage.
 - Shotgunning
 - There are two types of shotgunning
 - When a person simultaneously takes out multiple loans with different lenders for the same home, he is shotgunning. Typically

- after committing the mortgage fraud, the person leaves the country.
 - Shotgunning also takes place when there are multiple sales of the same house.
- Air Loans
 - Air loans are non-existent property loans where there is no collateral. The property is fictitious.
- Identity Theft occurs
 - When a person assumes the identity of a homeowner and takes out a mortgage on his property. Sometimes this is part of a mortgage fraud ring where a seller assumes the identity of the home owner, and a buyer who seeks the mortgage to buy the house, both of whom are using false identities, share the illegal gains and disappear without making payments on the mortgage.
- Nominee Loans/Straw Buyers
 - The true borrower is concealed through the use of this "nominee" or "straw buyer," who allows the borrower to use the person's name and credit history to apply for a loan.
- The purchaser receives a gift he plans to repay for the down payment.
 - A gift letter states that there is no intent on the recipient's part to repay the loan and the giver of the loan does not expect re-payment. When the agreement between giver and recipient is that the recipient will repay the loan, but the gift letter says otherwise, this is loan fraud.
- Inflated purchase price is
 - When there are two sales contracts for the same property and the agent sends the higher, false one to the lender in hopes of obtaining a better appraisal.
- Property flips
 - The property is purchased, falsely appraised at a higher value, and then quickly resold.
- Appraisal fraud
 - If a home's appraised value is deliberately overstated, more money can be obtained by the borrower in the form of a cash-out refinance or obtained by the seller in a purchase transaction. A dishonest appraiser may inflate the value, or someone with knowledge of graphic editing tools such as Adobe Photoshop can alter an appraisal. In many cases of mortgage fraud, the appraisal is involved.
 - Studies show that more than 50% of appraisers say they have been pressured to overstate property values.
 - Even fairly honest lenders will use a "special appraiser" who they know will bring in a higher appraisal than their "honest appraiser."

Part 3 - Remedies and Reasons

- What should the consumer or agent do if he suspects mortgage fraud?
 - If the consumer is approached by a real estate professional who asks him to become part of a mortgage fraud scheme, he should report the person to the FBI.
 - Federal Bureau of Investigation (FBI)
935 Pennsylvania Avenue, NW
Washington, D.C. 20535
202-324-3000
<http://www.fbi.gov/whitecollarcrime.htm>
 - OR
 - Contact the FTC

- The Federal Trade Commission (FTC)
600 Pennsylvania Avenue, NW
Washington, D.C. 20580
Identity Theft Clearinghouse: 877-438-4338
Consumer Response Center: 877-382-4357
<http://www.ftc.gov> or
<http://www.ftc.gov/bcp/edu/microsites/idtheft/>
- OR
- Talk to a reputable real estate lawyer or the state licensing authority.
- OR
- Contact the Mortgage Bankers Association's (MBA) website dedicated to stopping and reporting mortgage fraud at
www.stopmortgagefraud.com
800-348-3931
- Why is mortgage fraud so prevalent?
 - A recent study by Demos, a research firm in New York City, states that Americans have more debt now than ever. They have been taking equity out of their homes in record amounts to consolidate debt, and Americans actually own less of their homes today than thirty years ago. This climate (frequent refinancing) depends heavily on a continuing appreciating real estate market. In the current declining market, many homeowners have taken on mortgages that exceed the true market value of their homes, thanks to appraisal fraud. The report asserts that mortgage fraud exists because the financial incentives of those involved in the mortgage loan process often work against the very idea of securing an honest appraisal.
 - Since loan officers are paid on a commission basis, their livelihood depends upon having loans close without problems.
 - In the refinancing situation, the appraisal must come in at a certain level in order for the refinancing to occur. Therefore and ironically, the lender's own rules contribute to the necessity to hit a dollar figure with the appraisal.
 - Loan originators don't really care if the loan defaults since most loans are sold to the secondary market and are not held by the institution at which the loan officer is employed.
 - The livelihoods of appraisers depend upon a steady flow of work from lenders. If an appraiser has a practice of bringing in low appraisals, he will soon find himself out of business.
 - Consumers often think only of the short-term when purchasing or refinancing. They want the house, or they want the money from the refinance. They don't think in the long term about the possibility of being, at some point, "upside down" with a loan balance that is higher than the value of the house.
 - Appraisers agreed to inflate property value since the market was appreciating.
 - Agents wrote offers with increasing amounts of cash back.
 - Mortgage lenders told borrowers that they would get the loan for them no matter what.
 - During the housing boom, "no documentation" mortgages grew in popularity, because, as home prices rose, qualifying for a traditional mortgage became more and more difficult.
 - Also, during the hot sellers' market, relaxed underwriting standards were introduced to give previously underserved consumers a better shot at home ownership. However, this easy money allowed too many loans to go to purchasers who could not afford them.
 - In some cases, sub-prime mortgage fees can be as much as a third of the value of the home.
 - The strong seller's market caused an increased reliance by both financial institutional and non-financial institutional lenders on third-party brokers.

- A significant portion of the mortgage industry is void of any mandatory fraud reporting.
- Who is involved in mortgage fraud?
 - The perpetrators of mortgage fraud span the entire spectrum from the innocent consumer to organized crime.
 - The FBI states that, based on existing investigations and mortgage fraud reporting, 80 percent of all reported fraud losses involve collaboration or collusion by industry insiders.
- What are the consequences of mortgage fraud?
 - Mortgage fraud is a prosecutable crime and is against the law.
 - Fines and prison sentences are stiff. According to the FBI, sentences can be up to 30 years and fines up to one million dollars or both.
 - If the lender subsequently discovers that any part of the consumer's loan application is false, he can demand immediate full payment of the loan.
 - When homes were appreciating, homeowners with unaffordable mortgage payments could either refinance or sell their homes, often at a profit, so these fraudulent scams went unnoticed.
 - Everything came crashing down when the market turned. Foreclosures, bankruptcies and short sales have been the result.
 - When applications inflate income and/or omit debt, this is a recipe for default.
 - These foreclosures, bankruptcies and short sales have contributed to a decline in the nation's median home price and forced contractors out of work.
- What is being done about mortgage fraud?
 - Unfortunately, during the hot real estate market, rising real estate covered up all of the illegal activities. Everyone was making money. Federal prosecutors claim that mortgage fraud has been around for years but has gone unnoticed.
 - The FBI is focusing its efforts on mortgage fraud schemes perpetrated by industry insiders. The FBI is identifying fraudulent trends within the mortgage industry and educating the public.
 - The U.S. Department of Housing and Urban Development (HUD) was the first agency to address flipping by establishing a rule stating that if a person receives an FHA home loan, they must own that house 90 days before reselling it.
 - The Veterans Administration (VA) now has the same rule.
 - HUD also will not allow someone to buy property and then resell it without going to settlement. Before this came about, agents were buying lease-purchase properties and then assigning their contracts to the new buyer of the home after flipping. HUD requires that in order to sell the property, the owner must have title to it first.
 - In 2007, Ohio passed a law that prohibits lenders from trying to influence appraisers. A common scam has been for purchasers borrowing more money than the home is worth.
 - New York, Baltimore and Cleveland are suing mortgage lenders for damages after a rash of foreclosures.
 - In a recent case, an attorney in Georgia was convicted of fraud and got 30 years in a federal penitentiary with no possibility of parole.

Part 4 – The Agent's Duty

- What are red flags that the real estate agent and consumer should look for?
 - The listing agent is asked to raise the list price in the computer after the sales contract has been ratified.
 - The buyer requests a specific appraiser.

- The mortgage broker tells the agent not to send a contract amendment to him.
- Hyped Appraisals
 - When the buyer is willing to pay more than the appraised value of the house, there may be a mortgage scam unfolding.
 - During the hot seller's market, it was difficult for lenders to spot appraisals that were higher than the value of the properties; however, with the cooling of the market, these inflated appraisals are easier to recognize.
- The property has been on the market for a long time but sells for significantly more than the list price.
- Bogus Fees
 - Mortgage fraud does not always involve millions or even thousands of dollars. It can simply be a matter of padding the paperwork. The real estate agent and the principals to the transaction should carefully review the pre-settlement HUD-1 and then compare it to the HUD-1 that is presented at settlement.
- No Name Vendors
 - Real estate sales associates should be careful to work only with reputable vendors. They should check these people out and get a referral from a trusted colleague.
- The agent's Instincts are Screaming at him that Something is Wrong
 - When the agent mentions it, those who are perpetrating the questionable act tell the agent that it's fine and that it is standard practice.
- The agent needs to make sure that the true facts of a transaction are reflected in the contract (with all its amendments) and on the HUD-1.
- FBI tips to protect the consumer from becoming a victim of mortgage fraud
 - Get referrals for real estate and mortgage professionals. Check the licenses of the industry professionals with state, county or city regulatory agencies.
 - If it sounds too good to be true, it probably is. An outrageous promise of extraordinary profit in a short period of time signals a problem.
 - Be wary of strangers and unsolicited contacts, as well as high-pressure sales techniques.
 - Look at written information to include recent comparable sales in the area, and other documents such as tax assessments to verify the value of the property.
 - The consumer needs to understand what he is signing and agreeing to--If he does not understand, he needs to re-read the documents or seek assistance from an attorney.
 - The consumer needs to make sure that the name on the application matches his name.
 - The consumer should review the title history to determine if the property has been sold multiple times within a short period--It could mean that this property has been "flipped" and the value falsely inflated.
 - The consumer needs to know and understand the terms of his mortgage and should check the information against the information in the loan documents to ensure they are accurate and complete.
 - The consumer should never sign any loan documents that contain blanks--This leaves him vulnerable to fraud.
 - The consumer should check out the tips on the Mortgage Bankers Association's (MBA) website at <http://www.StopMortgageFraud.com> for additional advice on avoiding mortgage fraud.
 - The consumer should beware of e-mails or web-based advertisements that promote the elimination of mortgage loans, credit card and other debts while requesting an up-front fee to prepare documents to satisfy the debt. The documents are typically entitled Declaration of Voidance, Bond for Discharge of

Debt, Bill of Exchange, Due Bill, Redemption Certificate or other similar variations. These documents do not achieve what they claim.

- There is no magic cure-all to relieve a person of debts incurred.
- Borrowers may end up paying thousands of dollars in fees without the elimination or reduction of any debt.
- Perpetrators mislead the homeowners into believing that they can save their homes in exchange for a transfer of the deed, usually in the form of a Quit-Claim Deed, and up-front fees. The perpetrator profits from these schemes by re-mortgaging the property or pocketing fees paid by the homeowner without preventing the foreclosure. The victim suffers the loss of the property as well as the up-front fees.
- The consumer should be aware of offers to "save" homeowners who are at risk of defaulting on loans or whose houses are already in foreclosure.
- The consumer should seek a qualified Credit Counselor or attorney to assist him in making some of the decisions.

Part 5 - Case Studies

➤ Case Studies

- A buyer has entered into a contract to purchase a property for \$200,000, but, after learning about a roof problem, asks for and gets a price concession of \$10,000 from the seller. At a \$190,000 sales price, the buyer might obtain a 90 percent loan-to-value mortgage for \$171,000 and bring approximately \$19,000 to close. However, the buyer has only \$10,000 in cash and needs to get a loan of \$180,000 to buy the property. The seller proposes a rebate plan to close the deal. On the sales contract, the seller will keep the price at \$200,000. In that way, the buyer will be able to borrow \$180,000 with a 90 percent loan. At closing, the seller rebates \$10,000 to the buyer. Aware that the lenders will probably treat the \$10,000 rebate as a price concession, the deal participants agree not to tell the lender about the rebate. That's fraud.
- A mortgage broker charges a borrower \$10,000 in points and fees (the charges are a disguise for fraud). The seller agrees to pay for those loan charges and discloses this payment to the lender. Unbeknownst to the lender, the mortgage broker then rebates the \$10,000 to the buyer outside of the closing. Again, this is fraud. Another example is that instead of the buyer bringing \$20,000 in cash to the closing, the seller agrees to carry a second mortgage for \$10,000. The seller discloses the second mortgage to the lender. However, the seller and buyer agree that the second mortgage will never be paid. Again, the buyer gets a loan based on an inflated price. Once more, it's fraud.
- One of the truisms about mortgage fraud is that if the seller's concession is shown on the HUD-1 settlement statement, there's no fraud. But that's true only if the description on the HUD-1 is accurate. Among the gimmicks used to create the illusion of disclosure is a debit from the seller's proceeds suggesting a charitable contribution by the seller or the payment of a debt owed by the seller. If the deducted money is being used to satisfy real debt of the seller or make a real contribution, then it's perfectly legal. But if the debit and payment to the third party are really a disguise to route money from the seller back to the buyer or other promoter of fraud, such as the mortgage broker, again, it's fraud.
Routing the payment through a so-called charitable organization

doesn't avoid the fraud because the stated contract price exaggerates the true price received by the seller.

Reprinted from Realtor® Magazine with permission of the National Association of Realtors®, Copyright 2008, All rights reserved.

- In 2007, four people connected with a San Marcos Realty office pleaded guilty to charges that they illegally secured mortgages for financially unqualified consumers, thereby pocketing more than one million dollars in fraudulent commissions.
 - "Straw buyers," purchasers with higher credit scores and income, were substituted for less qualified buyers on mortgage applications.
 - Financial information was falsified on loan applications, indicating higher balances on bank statements.
 - Employment was falsified.
 - Bank statements, social security cards and other documents were falsified.
- Johnson Cuffy, a Florida real estate investor, bought a house in 2005 for \$245,000. Then, Cuffy obtained an inflated appraisal of \$340,000. Cuffy then recruited a straw buyer, Kervyn Harris. Then he arranged for Fremont Investment & Loan of California to lend Harris \$340,000. When the sale closed on December 30, 2005, Cuffy walked away \$95,000 richer. Cuffy divided the proceeds among his father, sister and the man who provided the straw buyer. The house went into foreclosure. The Florida Department of Financial Services' fraud division arrested all involved.
- REO FLIPWAGON (JACKSONVILLE): In December 2003, the FBI initiated a UCO to address the massive amount of mortgage fraud in the Jacksonville area. On September 16, 2004, as a result of this investigation, seven search warrants were executed, and two arrests were made. Mortgage broker J. R. Parker and closing attorney, Dale Beardsley, were arrested via complaint, charging them with bank fraud for their role in this alleged scheme.
- OPERATION CLEAN DEED (CHARLOTTE): In November 2002, an FBI UCO was initiated utilizing a cooperating witness to introduce undercover FBI Agents into seven organizations involved in a multimillion-dollar mortgage fraud ring. Investigation led to the identification of fraudulent loans which exposed financial institutions and mortgage companies to potential losses of \$130 million. On September 16, 2004, information was filed in U.S. District Court, Western District of North Carolina, charging six individuals with bank fraud for their roles in a multimillion-dollar mortgage fraud.
- JAMES MCLEAN; PRESIDENT ET AL; FIRST BENEFICIAL MORTGAGE COMPANY - VICTIM (CHARLOTTE) A two-year joint investigation by the FBI, the Internal Revenue Service, and HUD-OIG revealed a fraud for profit scheme committed by several insiders of First Beneficial Mortgage Corporation. This two-year fraud was perpetrated against Fannie Mae and Ginnie Mae home loan programs resulting in losses exceeding \$30 million. Recently, the president of First Beneficial Mortgage Corporation and six others were convicted on conspiracy, bank fraud, wire fraud, and money laundering charges. The president was sentenced to 21 years in prison, ordered to pay \$23 million in restitution and forfeited about \$8 million in property.
- MAGGIE CUEVAS; FAG-HUD; FIF (LOS ANGELES) A joint investigation conducted by the Los Angeles FBI Office and HUD-OIG illustrated an extensive scheme in which fraudulent identification and employment documents were used to perpetrate mortgage frauds. The scheme was largely assisted by an individual who regularly manufactured false identity and income documents for a profit. This document forger created W-2s, pay stubs, credit letters and social

security printouts over an eight-year period. These documents were used by real estate professionals who knowingly submitted the falsified information to lending institutions. The loans were then insured by HUD and caused a loss to that agency of more than \$18 million. A search warrant executed during the investigation revealed more than 100 real estate professionals had ordered false documents in the past. To date, the document forger and six associates have been convicted in the scheme, as well as 14 real estate professionals.

- BRENT BARBER dba MIDTOWNE RESTORATION, L.L.C (KANSAS CITY) A two-year joint investigation conducted by the Kansas City FBI Office, IRS and HUD-OIG culminated on August 13, 2004 with the arrest of Brent Barber, real estate investor. Barber, along with his three business associates, was charged in U.S. District Court for their alleged roles in purchasing run-down properties, securing fraudulent appraisals and obtaining mortgages in the names of straw purchasers. It is alleged that the straw purchasers were paid \$2,000 for their role in the scheme whereby they placed properties in foreclosure, leaving Barber and his associates with the mortgage proceeds. This scenario was repeated approximately 300 times, resulting in losses to lending and financial institutions in excess of \$15 million.

Mortgage Fraud Final Quiz

1. Tom and Amy are purchasing a townhouse, which they plan to rent out. Which of Tom's following statements could indicate mortgage fraud?
 - a. "We'll probably have to put 10% or 20% down since this is an investment property."
 - b. "Let's fix it up before we put it on the market."
 - c. Both a and b
 - d. "We'll get a better interest rate if we say we're going to live in it."

2. Sally and John are purchasing a home in the Briarwood Subdivision. They love the home but have expressed concern about the condition of the carpet. They called the sellers and, during the conversation, the sellers indicated that they would be willing to commit mortgage fraud. Which of their statements indicate this?
 - a. "We'll give you a closing credit of \$2,000. Have your agent draw up an amendment to the contract and we'll sign it."
 - b. "We'll just give you a \$2,000 check for carpet outside of closing."
 - c. Both a and b
 - d. Neither a nor b

3. Does mortgage fraud always involve a lot of money?
 - a. Yes
 - b. No

4. Who is addressing the mortgage fraud epidemic?
 - a. HUD
 - b. VA
 - c. FBI
 - d. All of the above

5. Fraud for profit is
 - a. Fraud typically committed by the buyer
 - b. 20% of fraud committed
 - c. Fraud typically committed by real estate professionals.

- d. None of the above
6. How are mortgage fraud and predatory lending different?
- They're not. They're the same thing.
 - Mortgage fraud is when one or more individuals defraud a financial institution; predatory lending is when a dishonest financial institution willfully misleads or deceives the consumer.
 - Mortgage fraud is committed by the lender and predatory lending is committed by the buyer.
 - None of the above
7. Martin, a listing agent, sells a home for \$450,000. The appraisal comes in at \$420,000. Martin implores, even bribes the appraiser to raise the appraisal to \$450,00, which the appraiser does. Is this fraud?
- Yes. It is appraisal fraud.
 - No. This is done all the time.
 - Yes. It is shotgunning.
 - None of the above
8. Sue, a listing agent, sells a home for \$620,000. The appraisal comes in at \$605,000. Sue looks into the appraisal and sees that the appraiser, not familiar with the area, did not use the best comparables. Sue brings this to the appraiser's attention and asks her to take a look at these new comps. Is this fraud?
- Of course.
 - Yes, but Sue needed this sale in order to buy her new mink coat.
 - No. Sue is merely asking the appraiser to consider better comps.
 - None of the above
9. Donna and Mike sign a Sales Contract for a \$600,000 home. They barely qualify but just make it, according to their lender. Two days before closing, Mike purchases a boat, that he puts on his credit card. He tells Donna that they are not going to tell the lender because the added debt will prohibit them from getting the loan. Is this legally acceptable?
- No. It's mortgage fraud.
 - No. It's predatory lending.
 - Yes. What the lender doesn't know won't hurt him.
 - None of the above.
10. What are some of the causes of mortgage fraud?
- Greedy lenders and appraisers
 - Buyers who want a house that they cannot afford
 - Both a and b
 - Neither a nor b
11. A person committing mortgage fraud can
- Lose the house
 - Go to prison
 - Be fined up to one million dollars
 - All of the above
12. During the strong seller's market, mortgage fraud
- Went unnoticed
 - Was rampant
 - Did not exist
 - Both a and b

13. The following are red flags that mortgage fraud may be occurring except
 - a. The buyer requests a specific appraiser.
 - b. The loan officer tells the agent not to send a contract amendment to him.
 - c. In the Sales Contract, the purchaser requests that the seller pay \$1,000 toward closing costs.
 - d. The property sells for more than the list price after being on the market for a year.

14. The consumer can protect himself against mortgage fraud by being diligent and doing the following:
 - a. Obtaining a referral for real estate professionals
 - b. Not signing any document which contains blanks.
 - c. Both a and b
 - d. Neither a nor b

The Ins and Outs of Short Sales

Part 1 – Reasons for a Short Sale

- What is a Short Sale?
 - A short sale is a process where the lender will look at the loan which the owner has with them and determine whether or not the house owes more than its fair market value or has such a small amount of equity that if sold, could not cover the agent and closing costs. When the lender determines that to be true, they will consider discounting the loan to reflect a price which will facilitate the sale of the property. The lender then decides to receive payment on the note for less than the face amount.
 - A seller who would benefit from a short sale is a seller who, if he were to sell the home in the customary way, would have to bring money to settlement because he is “upside down.”
 - A short sale is a potentially high risk transaction for real estate agents and their clients.
- Other names for Short Sale
 - Short Payoff
 - Pre-foreclosure Sale
- In what type of real estate climate do we see short sales?
 - When there are a record number of listings in the market
 - When there are fewer buyers than in recent years
 - When credit standards are tighter than usual
 - When borrowers have more consumer debt than usual
 - When a large number of mortgages have been financed with 100% loans
 - When a large number of consumers have consolidated debt or pulled equity out of their homes by refinancing
 - When home prices have declined
 - When there are a record number of foreclosures
 - When there are a record number of adjustable rate mortgages refinancing due to spiking interest rates
- What is the result of the above described real estate climate?
 - Home owners can no longer make their mortgage payments.

- Home owners can no longer sell their homes, pay fees and closing costs and have enough to pay off the balance of their mortgages.
- There are a large number of listings with the key words:
 - “third party approval required”
 - “bank approval required”
- Homeowners can go into foreclosure in these cases; however there are alternatives to foreclosure.
 - Homeowners who do not want to sell may have the following options:
 - Move into a more affordable home and rent out their existing home
 - Take a roommate.
 - Seek out a HUD-approved housing counseling agency that offers default counseling (<http://www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm>)
 - The lender may agree to a short-term payment reduction plan.
 - The lender may agree to a repayment plan for the delinquency.
 - The lender may modify the loan and extend the amortization.
 - The lender might reduce the interest rate.
 - The lender might allow the homeowner to forgo a couple of monthly payments to help him get back on his feet.
 - The lender might agree to a forbearance plan.
 - The lender may agree to a deed in lieu of foreclosure
 - Short Sale
- Owners need to beware widespread predatory schemes.
 - In some, an investor offers to take over the loan payments and allows the owner to pay rent, then asks the owner to sign a quitclaim deed, transferring title to the investor.
 - A quitclaim deed transfers interest but not liability.
 - If the owner transfers himself out of title, the lender might decide to call the note due and payable.
 - The owner should never transfer his title.

Part 2 – Advantages and Disadvantages of a Short Sale

- What are the advantages of a short sale to the seller?
 - The seller may be able to avoid foreclosure and/or bankruptcy. With a short sale, the owner is back on his feet much faster than with a foreclosure.
 - In most cases, the seller does not have to bring money to the table.
 - A short sale can minimize the impact to the seller’s credit rating.
- What is the down side for the seller?
 - There’s no guarantee that the lender and other creditors will accept a short sale even under the most favorable terms.
 - The entire process can be overwhelming and embarrassing.
 - The process can take a very long time and discourage potential buyers.
 - Even where lenders cooperate, there is no guarantee that they will forgive the remaining indebtedness.
 - Due to the length of time a short sale can take, foreclosure may occur before short sale processing can be done.
 - The short sale must be disclosed to potential buyers. The listing agent should check his local MLS policies and procedures about disclosing the “short sale” terms to the other members of his MLS.
- What are the advantages for the buyer?
 - The buyer may be able to get the property at a very good price.
- What is the down side for the buyer?

- The home may hold hidden risks such as property defects, legal and tax issues and unforeseen expenses.
- What is the downside for everyone?
 - The short sale process is often misunderstood if the parties to the contract have not been fully educated. When this happens, attorneys report a large number of lawsuits.
 - Short sales often cause surrounding property values to drop.
- Advantages of a short sale over foreclosure to the lender
 - Often, a short sale has a far better return on an investment to the lender than a foreclosure. A study by the Tower Group estimates that the average cost of a foreclosure to the lender is \$58,000.
 - The lender is often paid much sooner with a short sale than with a foreclosure.
 - Attorneys' fees are lower with a short sale than a foreclosure.
 - The banks want to minimize the amount of real estate they own in this weak housing market with declining prices.
 - The banks do not want to own these homes because new homes are selling faster than existing ones, and often, the condition of the property is poor.
 - Foreclosed homes, which often continue to have heat, lights and water, have become home to many of the nation's homeless people, as reported by the AP on February 18, 2008 because these foreclosed homes often have an advantage over abandoned, boarded up and dilapidated houses.
 - Due to the above, many large lenders, such as Bank of America Corporation, Citigroup, Inc. and National City are reaching out to troubled borrowers, trying to help them head off delinquencies.
- What are the advantages to the agent?
 - The agent may be able to get a listing, earn a commission and help save the seller's credit (to a certain extent).
 - If the agent can get someone out of a difficult situation, he will have a client for life. They will refer people to him and will come back to him when they are ready to buy again.
 - The buyer agent may be able to find a good value for their client and expand the selection of available homes.
- Specializing in short sales can be a profitable niche for the real estate agent. Target marketing can include the following:
 - Using word of mouth
 - The agent can market himself and his expertise to other agents.
 - Attending credit counseling classes, which are required prior to filing bankruptcy
 - Targeting people who receive state notices of loan defaults
 - Targeting homeowners named on lists of ARMS that will be adjusted in the coming months
 - Targeting FSBOS, who are frequently "upside down" sellers who think they can't afford to pay a commission and, therefore, try to sell on their own. Many don't know that in a short sale, the lender pays the broker's commission.
 - Purchasing lists from foreclosures.com
 - Purchasing lists from ForeclosuresDaily.com
 - Marketing himself on his website as someone who specializes in short sales and/or foreclosures
 - Going to foreclosure auctions to find prospective buyers
 - Checking the Internal Revenue Service's property site (www.treas.gov/auctions/irs/index.html)
 - Forming bonds with mortgage brokers, bankers, lawyers and other real estate professionals, all of whom will refer business to the agent if they know that he can aid their customers

Part 3 – The Agent’s Role

- What does the listing agent need to do?
 - The prudent real estate agent will engage in short sales only after he has educated himself fully regarding his role and responsibilities.
 - The earlier the agent can start the process, the better chance there is of getting the short sale approved.
 - Most of the time, the real estate agent does not know that the owner is in trouble before the listing presentation and the completion of the seller’s net sheet.
 - Once it is determined that the cost of selling is more than the loan balance, the listing agent should have an open and frank discussion with the owner.
 - The listing agent and owner need to determine whether or not the owner must sell.
 - Is the owner yet delinquent on his payments?
 - What is the financial situation of the owner?
 - Current market value should be discussed with the owner.
 - At this point, if it is evident that the owner is in trouble and foreclosure or bankruptcy are likely to occur in the near future, the agent should discuss options with the owner. (Refer back to Section 1.)
 - If it is clear that the owner needs to unload the property, the short sale process should be explained in detail.
 - The listing agent can make the short sale process smoother if
 - He takes a checklist of documents needed to the listing appointment. This can prevent the listing agent from wasting his time if potential sellers do not want to be bothered with all of the paperwork.
 - It should be explained that the seller will have to negotiate with the lender. At this point, the agent should ask for written authorization to be included in the communication with the lender.
 - All of the pros cons should be explained.
 - The agent should explain that the property will have to be priced aggressively.
 - The agent should encourage the seller to contact an attorney, tax advisor or financial planner for advice on the financial implications of the sale relating to debt forgiveness.
 - The listing agent should build a relationship with the seller’s lender(s). Once credibility has been established, the entire process becomes easier.
 - The agent will have to call the lender for the loan balance.
 - Then, the agent contacts the bank’s short sale department (not the collection or customer service department, which is only interested in collecting past due loan payments), the group that will decide whether to accept a short sale. Finding the decision maker can be one of the biggest initial challenges in short sales. The agent may have to make a half dozen phone calls before finding the person responsible for handling short sales. The supervisor should be the one on the other end of the phone, the person actually capable of making the decision.
 - Then, the listing agent needs to submit a very specific financial proposal to the lender. This will expedite the entire process.
 - If the owner has been late with any payments, it should be written into the proposal that any late charges will be dismissed.
 - The listing agent submits a letter of authorization with the following information
 - Property Address
 - Loan Reference Number
 - Name of Owner

- Date
- Agent's Name and Contact Information
- Preliminary Net Sheet
- Hardship Letter
- Proof of Income and Assets
- Copies of Bank Statements
- Comparative Market Analysis
- In the proposal, the agent should request that the lender not report any more delinquencies (if there are any) to the credit reporting companies.
- Real estate investors are often willing to help the listing agent negotiate short sales with the banks so they can buy their listings.
- What should the buyer agent do?
 - The buyer agent might want to run two sets of comps, (homes that sold with a short sale and those that sold without a short sale) when preparing the offer.
 - The seller of the home might be using all of the comps to justify his price.
 - The two sets of comps might create a reality check for the seller.
 - The buyer agent needs to be patient and remember that to the lender, his transaction is just a number.
 - A lot of contingencies should be written into the offer but no one should expect the lender to agree to them.
 - The buyer agent should know the condition of the property through inspections so there are no surprises after settlement.
- Once the seller has accepted a contract, the listing agent should
 - Send the contract and listing agreement to the lender. Include an accounting of all expenses, which the seller will pay at settlement and a final number that the lender will receive when settlement takes place.
 - It is helpful for the listing agent and seller to have a HUD-1 settlement statement prepared.
 - The seller should be able to go to the settlement table knowing all the terms and conditions on which the lender will accept the short sale, including whether or not he will have to come up with money at the settlement table.

Part 4 - The Process

- Lender considerations before accepting a short sale
 - Is the seller legitimately suffering a financial hardship? Someone with the assets or the income to pay is unlikely to be considered.
 - Has the seller defaulted on the loan? Has the foreclosure process started?
 - Has the seller prepared a short sale package with the following:
 - Lender-provided short sale application
 - Hardship letter describing seller's situation
 - Financial documentation, which includes
 - Two years of tax returns
 - Two years of W-2s
 - Two months of bank statements
 - Two months of pay stubs
 - Broker Price Opinion (BPO) for the property
 - Has the seller given written authorization for the agent or attorney to communicate with the creditor(s)?
- What must the agent be prepared for?
 - A short sale involves a lot of paperwork.
 - The potential short sale must be disclosed.

- The agent needs to advise seller and/or buyer client of the need for third-party approval, possible time issues and other downsides.
- The commission may be reduced on both sides by the lender.
 - Potential commission reduction would have to be disclosed to both sides (brokers and parties to contract)
 - Or, the listing agent can state in the MLS that the commission is subject to third party approval.
- The settlement of the short sale might not take place due to the third-party approval process; the lender calls all the shots.
- The agent must be a facilitator, not a negotiator, of the seller's outstanding debts.
- The process will be much more time consuming than a typical transaction.
- There will most likely be time delays; it can take forever.
- This is a very risky transaction and all of the potential difficulties can result in the agent being blamed when the buyer or seller is disillusioned. (In 2007, E & O attorneys indicated that short sales resulted in many lawsuits and complaints being filed nationwide.) Agents are accused of
 - Not submitting offers
 - Not following up
 - Lying about offers being "accepted"
 - Lying about "highest and best" deadlines
- The parties to the transaction must be fully prepared as to what to expect!
- There is no uniformity in lenders' documents.
- The lender reserves the right to reject any offer.
- If there are two mortgages, both lenders have to agree to accept less than the payoff amounts. Property encumbered by a second mortgage might kill a short sale deal.
- If the short sale fails, the seller might face foreclosure.
- Closing will occur where the lender stipulates. Often, a quick closing is called for.
- In preparing the packet for the lender, the agent should look for any discrepancies between the seller's income and the income used to obtain the loan.
 - There is a large group of people who are finding themselves unable to make payments on loans that they initially qualified for by providing "stated income" without documentation. Much of the stated income was inflated.
 - A big gap might indicate mortgage fraud.
 - These owners are unlikely to have a short sale approved by the lender.
- The lender calls the shots
 - From purchase price to seller concessions
 - From timing of negotiation to time of closing
 - From "as is" addendum to broker commissions

What paperwork is necessary at the time of listing?

- Seller's statement of need or hardship
- Seller's current employment situation
- Seller's current income status/pay stubs
- Seller's financial statements
- Seller's tax returns
- Seller's credit analysis
- Property appraisal or BPO
- Listing paperwork
- Short Sale Brokerage Fee Agreement
 - This is the agreement between the listing and selling brokers and is initiated by the listing side
- Short Sale Listing Addendum

- Creditor Authorization and Release Form (This provides the authority for listing agent to contact the seller's creditors.)
- Addendum that states that lender can void sale if taking deed in lieu of foreclosure
- Statement of why owner needs to sell home
- An application, provided by the lender and completed and signed by the seller
- How should the short sale property be disclosed to potential purchasers?
 - Most experts favor disclosing that a property is a short sale in the comments section of the MLS listing.
- Paperwork at time of offer
 - Submission of offer
 - Net to seller
 - Lender addenda
 - Lender requirements
 - Short Sale Contingency Addendum to Sales Contract
 - This form is made a part of the sales packet. Without language in the contract stating that the lender must approve the offer and release all liens on the property, the seller could face a legal problem for failing to execute the contract if the short sale is not approved.
- What type of buyer does the lender favor?
 - A buyer who is willing to close in 30 days
 - A buyer who can make a substantial down payment
 - A buyer who has been pre-approved for a mortgage before submitting the offer
- Legislation that can aid the seller of a short sale
 - The Homes Affordable Program
 - It's a program that started in 2009 and allows home owners to refinance their mortgages at lower rates without having to show 20% equity in their home.
 - Only home owners with loans backed by Fannie Mae or Freddie Mac can participate.
 - It gives sellers up to \$3,000 for relocation expenses.
- Time Delays
 - A short sale involves as much if not more paperwork than an original mortgage application. That is due to the fact that, instead of proving creditworthiness and financial stability, the seller must prove that he is broke. He must be without cash flow, including savings, investments, trusts, liquid retirement funds or other finances to tap.
 - Most lenders require preliminary evaluation before an offer will be reviewed for approval.
 - The listing agent must receive written authorization from the seller to contact the loss mitigation supervisor of the lender at the earliest possible time.
 - This is only one of thousands of short sale requests being processed by the lender. This seller is just a number in the chain.
 - Lenders will typically not consider a short sale unless the owner has been delinquent at least 30 days. Many lenders wait 60 or 90 days before considering a short sale.
 - If the listing agent has not assisted the seller in submitting the required paperwork, approval of the short sale can take weeks and with no guarantee of approval. (Most delays are the fault of the listing agent.)
 - Sometimes, the lender intentionally delays the process hoping for a better offer to come along.
 - Most offers are not accepted as written but are countered.
 - It is recommended that any third party approval contingency be for at least 30 days, if not more.
 - The Homes Affordable Program can create more paperwork and slow down the short sale process

- The process can be expedited by using the Equator System.
 - The Equator System is a collection database for documents needed in a short sale.
 - No processor is necessary to collect the documents. It is completely computerized.
 - The agent does not deal with a person until all forms are in.
 - As a result, the usual four to five months previously needed to close is usually reduced to two to three months.
- Any delay might depend upon how much of the process has taken place prior to obtaining a ratified contract.
- Contract Negotiations
 - Acceptance by the bank is given in writing.
 - Commonly, the lender negotiates the price and terms agreed to by the buyer and seller.
 - Many lenders will limit or refuse to
 - Help with down payment assistance
 - Pay buyer closing costs
 - Make repairs
 - Most lenders' addenda state that the buyer is accepting the property in "as is" condition.
 - It is still wise to have a home inspection conducted. Therefore, the agent should write into the contract that the buyer will take the property in "as is" condition once he is satisfied with the condition as revealed by the home inspection.
 - It can take weeks to get a response from the lender. This is a problem if an offer expiration date is written.
 - Banks will not accept electronic signatures in short sales negotiations.
 - Banks might require proof of funds showing that the buyer has the ability to close.
- If any of the following occur, it is prudent to release the listing and not move forward:
 - Bankruptcy
 - The house is not available for sale while it is under the protection of the trustee of the bankruptcy court.
 - Judicial Foreclosure
 - The owner's court date for foreclosure has arrived, and there is not a signed letter authorizing a short sale with a closing date before the foreclosure date.
 - Notice of Auction of the property
 - The owner of the home no longer has legal ownership of the property.
- Banks are now trying to prevent the need for short sales because new legislation allows the refinancing of homes that are owned by sellers who have less than 20% down when Fannie Mae or Freddie Mac are involved.

Part 5 - Seller Consequences

- Tax Issues
 - The tax law, up until December of 2007, stated that "forgiven debt" was taxable as current income in the year the debt was forgiven. Many lenders sent 1099 forms at the end of the year.
 - On December 20, 2007, President Bush signed The Mortgage Forgiveness Debt Relief Act of 2007 to provide financial relief for sellers facing foreclosure or short sales. The bill gives a tax break to homeowners who have mortgage debt forgiven as part of a foreclosure

or renegotiation of a loan. No taxes would be owed on the value of any debt forgiven or written off.

- The exclusion of capital gain does apply so long as the seller has owned and occupied the property as his personal residence for 2 of the last 5 years.
- Credit Issues
- Just because the lender releases the lien after the short sale, it does not mean that the debt is forgiven or that the seller's credit will not be negatively affected. The following could occur:
 - The lien is released; however, the seller could be required to carry the remaining debt on a pre-payment plan.
 - The lien is released; however, the seller could be forced to liquidate other assets to pay the remaining balance.
 - The lien is released; however, the lender sues the seller on the note for deficiency.
 - The lien is released; however, the lender reports the amount of loss as a "charge-off" or "collection" to the credit bureau thereby causing the seller's credit to be negatively impacted. Even so, the credit report will show better with a short sale than with a foreclosure.
 - Often, the seller thinks that a short sale will solve all of his problems. In many cases, this is NOT true. However, if the seller has decent credit up to this point, the short sale will minimize the harm to his credit whereas the foreclosure will not.
 - The seller should be encouraged by the agent to sign a lease on a rental property before the credit is damaged by the short sale.

Short Sales Final Quiz

1. Is the seller's credit affected by a short sale?
 - a. Usually
 - b. Never
 - c. Only if the lender counters the buyer's offer
 - d. None of the above.

2. Who has most of the control in a short sale?
 - a. The agent
 - b. The buyer
 - c. The owner
 - d. The lender

3. Can working with short sales be advantageous for an agent?
 - a. No way. It's just a pain in the neck.
 - b. Absolutely. An agent who works short sales can provide a wonderful service for owners who are in trouble. When an agent provides a much needed service like this, he is likely to have referrals from those he helped.
 - c. No. They take too long.
 - d. None of the above

4. What is one downside to purchasing a short sale?
 - a. There are no downsides.
 - b. The prices on short sales are usually well above market value.
 - c. The buyer may be required to settle quickly
 - d. None of the above

5. A seller in the following situation might benefit from a short sale:

- a. He has paid off his mortgage
 - b. He has a lot of equity in his home
 - c. He can't make his payments, and he owes more than his house is worth
 - d. None of the above
6. The following alternatives to foreclosure should be considered by an owner in financial trouble:
- a. Consider a short sale
 - b. Moving into a smaller home and renting the larger, more expensive home
 - c. Asking the lender to modify the loan and extend the amortization
 - d. All of the above
7. What type of real estate climate contributes to a rash of short sales?
- a. Homes rapidly appreciating
 - b. A depreciating home market
 - c. A lot of existing mortgages with 100% financing
 - d. b and c
8. Going the short sale route instead of the foreclosure route will completely save the owner's credit.
- a. True
 - b. It will help but not completely save the owner's credit.
 - c. The owner's credit will be affected more by a short sale than a foreclosure
9. Why might an owner decide not to go the short sale route?
- a. To save the embarrassment
 - b. He finds the process completely overwhelming.
 - c. He cannot cope with the length of time a short sale might take.
 - d. All of the above
10. How might the listing agent minimize the effect of a short sale on neighborhood values?
- a. By putting a remark in the MLS after settlement or by checking a box stating that the transaction was a short sale
 - b. There's no way to minimize the effect a short sale will have on the neighborhood.
 - c. Short sales never affect property values.
 - d. None of the above
11. Why must a listing agent educate himself fully in short sales before attempting one?
- a. To minimize the chance of a lawsuit
 - b. To make the process go more smoothly
 - c. Both a and b
 - d. None of the above
12. Once a seller's net has been prepared, and it is determined that if the owner sells, he will be "upside down," the listing agent should
- a. Determine, along with the owner, if the owner must sell
 - b. List the house
 - c. Offer to give up his commission
 - d. None of the above
13. The first thing that the listing agent should do once it is determined that the seller is upside down and must sell is

- a. Have a frank discussion about short sales
 - b. Discuss staging with the owner
 - c. Explain to the owner that it will be impossible to sell the house
 - d. None of the above
14. Which of the following can be a potential problem in short sale negotiations?
- a. Lenders do not respond quickly.
 - b. Lenders would prefer foreclosure to short sale.
 - c. Lenders do not want to be involved in the negotiations.
 - d. None of the above
15. In a short sale situation, lenders often refuse to
- a. Help with down payment assistance
 - b. Make repairs
 - c. Accept electronic signatures
 - d. All of the above
16. Lenders sometimes drag their heels on accepting an offer
- a. Because they do not want the short sale to go through
 - b. Because they want to wait for another potentially better offer to come in
 - c. They don't like listing agents
 - d. None of the above
17. In a short sale situation, what kind of buyer do lenders like?
- a. Ones with a lot of cash
 - b. Ones who can be flexible on settlement date and willing to patiently wait out the process
 - c. Ones who have been pre-approved
 - d. All of the above

Name_____Date_____

5 HOUR FINANCING ISSUES IN TODAY'S MARKET FINAL QUIZ

Please circle the correct answer for each question.

Predatory Lending

1. A B C D
2. A B C D
3. A B C D
4. A B C D
5. A B C D
6. A B C D
7. A B C D
8. A B C D
9. A B C D
10. A B C D
11. A B C D
12. A B C D
13. A B C D
14. A B C D
15. A B C D
16. A B C D
17. A B C D

Mortgage Fraud

1. A B C D
2. A B C D
3. A B C D
4. A B C D
5. A B C D
6. A B C D
7. A B C D
8. A B C D
9. A B C D
10. A B C D
11. A B C D
12. A B C D
13. A B C D
14. A B C D

Name _____

Page 2

Short Sales

- 1. A B C D
- 2. A B C D
- 3. A B C D
- 4. A B C D
- 5. A B C D
- 6. A B C D
- 7. A B C D
- 8. A B C D
- 9. A B C D
- 10. A B C D
- 11. A B C D
- 12. A B C D
- 13. A B C D
- 14. A B C D
- 15. A B C D
- 16. A B C D
- 17. A B C D

Potomac Real Estate School Certification Sheet for Correspondence Course

Please fax to (703) 758-0044, scan and email to info@PotomacRESchool.com, or mail to Potomac Real Estate School, Box 494, Oakton, Virginia 22124

Print Name _____ **Course: 5 Hour Financing**

Billing Address _____ **Issues in Today's Market**

_____ (VREB Approval #58071)

RE License # _____ (10 digits)

Expires _____

Phone # _____

Email _____

Company Affiliation _____

Payment by Check

_____ I enclose a check payable to Potomac Real Estate School LLC in the amount of \$29.00

OR

Payment by Credit Card

_____ Please charge \$29.00 to my ___Visa___Master Card___American Express___Discover

OR

Card # _____ Expiration Date _____

Security Code _____ Signature _____

Did you find the material well organized?	Yes	No
Was the material well written?	Yes	No
Was the course material relevant?	Yes	No

Suggestions _____

How did you find us? Please circle

Internet Postcard Referred by _____ Email

Personal Note/Letter Ad VREB NVAR L&F

Other



Student Declaration: I hereby certify that I completed this continuing education course (5 Hour Financing Issues in Today's Market) on my own without assistance.

Signed _____

Date _____

Name (Print) _____

Notary Public Declaration: Taken, subscribed, and sworn before me this ____ day of _____, 20__

In the City/County/Town of _____

In the State/Commonwealth of _____

My commission expires ____/____/_____

Notary Public _____

Notary Signature Required

But Seal NOT Required