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Demystifying Loan Modifications

There seems to be confusion and misinformation out there about loan modifications. After assisting clients daily with their lender-related issues (and witnessing firsthand the stress that the lenders create), nothing disgusts me more than to arrive home late each evening and watch a certain television personality read a teleprompter full of inaccuracies and ham-handed sales pitches to refer you to that television station's website. If that news personality put as much effort into giving Arizonans sound direction regarding loan modifications as that person does self-promoting at local charity events, the economic crisis in Arizona would have ended last year. You may then ask, "Why don't you change the channel?" The answer: the other news personalities read the same garbage. Additionally, I marvel at the law firms that have never previously practiced in the area of banking and finance, but now advertise their loan modification services.

Instead of writing a commentary on the demise of our local television personalities or berating my colleagues, I can be most helpful to the community by offering some guidelines about loan restructuring. Why am I or attorneys that practice in real estate or commercial transactions more qualified to offer advice, instead of the news anchors? Simply put, in the most prosperous economic times, attorneys represent developers and businesses that routinely seek modification and/or renegotiation of their loan terms. It has been a daily practice in the commercial real estate industry ever since commercial real estate existed. But with one residential real estate crash, every criminal attorney, personal injury attorney and local news personality is suddenly giving legal advice on loan modifications. Wonderful. Here are a few guidelines to assist you during this confusing time:

- 1) There really two (2) options available at this point: a) Forbearance – where you enter into an agreement with your lender, giving them some money now, and in return you do not have to make payments for usually up to a year; b) Loan Modification – you enter into a new loan agreement with your lender, whereby the loan terms are more manageable.
- 2) Do not use a real estate agent to negotiate your loan modification or forbearance. Why? For starters, it is an unauthorized practice of law and if caught, your realtor will hear from the Arizona Attorney General's Office

on the criminal indictment and the Arizona Department of Real Estate will almost immediately suspend their license.

As a more practical matter why would a lender be willing to negotiate with a realtor? What expertise or training does the realtor offer? Can the realtor read your existing loan documents – or more importantly – the proposed new loan documents and translate it into language you understand? And please do not overlook the reality that many realtors acted in collusion with loan officers to approve loans that borrowers could not handle, so that the realtor could take a large commission.

- 3) Do not use a mortgage broker or loan officer to negotiate a forbearance or loan modification. Why? How many mortgage brokers do you know that have sat there with you and translated your loan documents? Aside from, “Um - That’s just standard language,” they cannot tell you anything about the documents that you are required to sign. Mortgage brokers do not write the loan documents (the lender’s attorneys write them). Beyond that, you also risk the mortgage broker that you hired to assist you, acting in collusion with your lender just so “your” mortgage broker can earn a commission on the “refinancing.”

So What Should I Expect My Attorney to Do?

As stated above, attorneys have been negotiating forbearances and loan modifications for decades. Lenders will negotiate with attorneys for one reason: attorneys can sue lenders and that costs lenders money. Let me be more specific: Attorneys that threaten a lender with, “well my client will just file for bankruptcy,” have no experience in working with lenders. The teeth in a lawsuit was created by the lender when you entered into your loan agreements. The overwhelming majority of loan documents prepared during the “housing bubble” are subject to civil claims for predatory lending action, fraud, duress. But the single most compelling claim that will stop a lender in its tracks is the collusion among the loan office, title company and realtor.

Sounds too good to be true? Think about the last home you or your friends purchased. How many people out there had a lender referred to them by their realtor? In a previous newsletter, I wrote about how appraisers, lenders, escrow agents and realtors would work together to sell a home at inflated values. The appraiser would overvalue the home at the lender’s request; the lender would offer a larger loan; and the realtor would convince the buyer that they could afford their “dream home.” That how people got into this mess.

Does your lender want to risk a lawsuit (joining the appraiser, escrow agent and realtor) for fraud and collusion? When you think about it, **and assuming such a claim is legitimate**, a lender can either:

- a) Take a Five Thousand Dollar (\$5,000) payment from you and agree that you do not have to make payments on your loan for a year.
- b) Re-write your loan, stretching it into a forty (40) year mortgage, whereby the payments become consolidated and/or more manageable.
- c) Be named as a defendant in a lawsuit, where if found liable, they will be subject to punitive damages, and concurrently be investigated by the Arizona Department of Financial Institutions for possible criminal prosecution.

Lenders believe in counting money, not spending it. Simply defending a case like that costs a lender Twenty Five Thousand Dollars (\$25,000). To their credit, lenders are smart and realize it makes better business sense to enter into a forbearance agreement or loan modification. Either of those options guarantees that the lender makes money. The alternative guarantees that the lender loses money and may just be put out of business.

As an added bonus, if your realtor referred you to that lender, you probably have standing to request that your realtor return the commission you paid to them. If the lender/realtor required/referred you to a specific title company and/or appraiser, then they may be just a culpable and should be added as defendants in your civil complaint against the lender.

Sounds Great But What Is the Catch?

First and foremost, you often have to give your lender a lump-sum to receive a forbearance or loan modification. Too many people (the local media is to blame) are lead to believe that because of a new federal program or that lenders have lots of housing inventory, you can simply stop paying your mortgage; offer a sad story; and expect a change in your loan terms without offering something in return (again threatening bankruptcy is not offering something to your lender). I will say it again: Lenders are interested in making money and not losing money. If your attorney can viably show the lender that they stand to profit from a change in the loan arrangement, the lender will work with you. If your attorney can establish to the lender that the lender committed acts that subject it to a strong civil lawsuit that will cost the lender money, the lender will work with you.

Anything Else?

Regardless of what you hear on television or friends, you have to continue making payments on your loan until a new arrangement is reached. Contrary to popular belief, refusing to make payments in an effort to gain leverage destroys your credibility with your lender. I think back to my negotiations with commercial lending attorneys. They say it over and over, “Why should we offer your client new payment terms when the have made no effort to pay?” Even if you gain leverage by not making payments, as a precondition of your forbearance or loan modification, you may have to bring the back payments current and pay the lender’s legal fees.

Contrary to the loan modification commercials offered by the personal injury attorneys, sometimes it is best just to walk away. The best money that potential clients and client spend on an attorney is during that initial consultation. More often than not, attorneys that charge for an initial consultation actually read the documents that you bring them, and most importantly, inform you of your best options. I am always suspicious of attorneys that offer free consultations (and you should be too). Those meetings turn into high-pressure sales pitches, where the attorney tries to create a big case out of thin air.

Yes, there are other issues. Tax ramifications, junior lien holders, homeowners’ association assessments, etc. But it is my hope that instead of watching the news this evening, read this newsletter. It probably will not answer all your questions, or even solve your problems. But it will help you to understand the legitimate options available to you; why they exist; and what is involved in pursuing said options.

As for my friends in local television land, all I can say is: One of my favorite movies is “Anchorman.” I watch it once in awhile. I recite the funny quotes. I sometimes travel to San Diego. I even have an idea of what it takes to be a television personality. But none of that makes me Ron Burgundy (and it never will). Tell you what: stop trying to practice law by reading your self-serving garbage from the teleprompter. Bring back the story about the cute squirrel driving the little motorized boat in a swimming pool. Everyone enjoys seeing the little fellow.

In exchange for your diligent efforts to cease misleading your viewers that you comprehend anything about the housing crisis, I promise to you that I will never say to my clients: “You stay classy, Phoenix!!!”