

# TALES FROM THE TRENCHES™

## BY BARRY C. MCGUIRE

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April, 2016

### “HELP, I CAN’T MAKE MY MORTGAGE PAYMENTS”

This is the fourth installment of our *Tales from the Trenches* series on mortgages and foreclosure. For a good overview of how foreclosures work and some comments on quit claims, look to our other Tales,

- ‘Mortgage Default’ <http://investorlawyer.ca/2015/05/25/mortgage-default/>, and
- ‘Quitclaims and Foreclosures’ <http://investorlawyer.ca/2015/06/23/quitclaim-foreclosure/#more-158486>
- ‘Mortgages & Related Security: How Are You Liable?’ <http://investorlawyer.ca/2014/02/06/mortgages-and-related-security-how-are-you-liable-handout>  
(Note: this is part 1 of a 9 part series)

Can’t make your mortgage payments? You are not alone, especially in Alberta.

The drop in oil prices from over \$100 per barrel to, at one point, less than \$30 a barrel has created economic disaster in Alberta. Energy and energy-related companies of all kinds, big and small, have been devastated. Capital spending has been slashed and layoffs are widespread as companies try to deal with how to survive in an environment where the sale price of a barrel of oil may be less than the cost to produce it. Job losses now exceed 65,000. For most workers, no job means no income unless you want to count Employment Insurance. Savings quickly disappear.

If you can’t make your mortgage payment, sooner or later your lender/bank will foreclose. Every province and state has their own particular rules around mortgages and foreclosure. Some of our discussion has general application but be sure to get your own local advice. This Tale is focused on Alberta.

### **Pre-Foreclosure: What To Do?**

Alright, if it looks like you won’t be able to make your mortgage payment, don’t panic! The best way to avoid foreclosure is to be proactive.

No matter what avenue(s) you take, it benefits you to check out possible solutions and to do that before you miss a payment. Let’s have our eyes wide open. A solution is always better. You don’t want to be foreclosed and lenders don’t want to foreclose. They would far rather have your payments than a lawsuit.

**As one foreclosure lawyer told me, “We want the dough, not the dirt.”**

Even though lenders don’t want to foreclose, after you miss a payment or two they will phone, and if you still can’t pay, they will write you letters demanding payment. Sooner or later, if you don’t catch up on your payments, the lender will send it to their legal counsel who will also write you a letter demanding payment.

If the mortgage is not caught up and all expenses of the lender paid, the lender’s legal counsel will start a foreclosure action by issuing a legal document known in Alberta as a ‘Statement of Claim.’

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So, if you know you are unlikely to meet your mortgage obligation, the first thing you should do is call your lender. It's painful, but you should do it.

### **Talk To Your Lender – Ignoring Them Doesn't Work**

Don't be embarrassed or ignore mail from your lender; that will just accelerate the foreclosure process. Take the lender's calls even though that can be an embarrassing, awkward conversation when the whole conversation is about, "when can you pay?"

It is especially awkward when you can't promise your lender any specific amount of money at any specific time. But, please be aware if you aren't paying, your lender will call. And, they keep notes of your conversations.

Depending on your situation, here are some options you or your lender might suggest. (N.B., it is strategically better and mentally more comfortable to discuss these options before you miss a payment.)

### **Can You Catch Up?**

As we said above, lenders don't want to foreclose. It's bad for you and bad for their business model. If you have a reasonable chance to catch up, your lender might agree to wait before taking legal action against you or they might suspend a foreclosure they have already started.

For instance, if the reason you can't pay is job loss but you have a new job starting in say, three months, your lender may not start a foreclosure action or put one on hold that has already been started. The more proof you can give your lender of the certainty and salary/income from your new job, the more likely they are to listen to your plan. No guarantees here because every lender is different.

### **Amend Your Mortgage**

All mortgages are amendable; some because you and the lender might negotiate amendments, some because your existing mortgage allows adjustments. For instance, a variable rate mortgage where your current interest rate generates higher than the required payment can be adjusted downward to lower your payment.

Or, if you took out a mortgage with a 20-year amortization period (being the number of years it would take you to pay off the mortgage), your lender might extend the amortization period to, say, 30 years. That would lower your monthly payments. As part of any reorganization, you could ask (some lenders may offer) to add your missed payments to the principal balance of your mortgage. That would spread out those missed payments over the balance of your mortgage.

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### **National Housing Act Mortgages**

If you made a down payment of less than 20% of the purchase price, you most likely have a loan made pursuant to the [National Housing Act \(NHA\)](#) where various insurance companies, the largest of them being [Canada Mortgage and Housing Corporation](#) (CMHC), insure lenders from any loss. If a lender forecloses on you and loses money, they make a claim to their insurance company, who pays them their loss.

Naturally enough, no NHA insurance company wants to pay a claim. They may have programs to assist you with some form of relief by way of forgiven missed payments or interest-only payments. Check your paperwork and if you find the name of any of the following three insurers, check with them further.

- [Guaranty Mortgage Insurance Company](#)
- [Genworth Financial Canada](#)
- Canada Mortgage and Housing Corporation

### **Get Creative**

If none of these more traditional approaches suit your particular circumstances, let's talk about non-traditional concepts that may have a chance to help you keep a property. Here are some options that non-creative, professional advisors may not suggest:

#### **Deal Sharing**

If your issue on your personal residence is that you can't make payments, how about a joint venture? With any decent amount of equity in your property, you can sell a percentage of ownership to a joint venture partner. Once you have funds from selling an interest, you can make up delinquent mortgage payments and perhaps give yourself a chance to get on your feet.

If foreclosure has already started, you will have to deal with the lender as part of paying those delinquent payments along with the lender's legal fees and any other costs, which when done will result in the foreclosure stopping. Yes, now you have a partner in your home, but that may be better than losing your home.

What about if you are an investor? If you just can't rent the property and because of personal circumstances can't make the mortgage payments, you might be able to find a joint venture partner who would put up some money to buy a portion of your equity, which you can then use to make the mortgage payments. However, without any equity and, for whatever reason, no tenants, you would have to make a very strong case for future prospects to have any joint venturer put up money to carry you through the tough times.

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### **What About Selling Your Property?**

This is the first and most obvious move in your chess game with the lender. Sell, pay real estate commission, pay the penalties on your mortgage, pay your legal fees, and just be done with the property. This only works if you actually have some equity in the property that can pay your costs of sale.

Or, you can try and sell the property yourself. Or, you can try to work with a reduced-commission realtor if you have confidence they can sell, since commission takes such a big chunk of your sale proceeds when you have a small amount of equity.

In a rapidly deteriorating market, one key success factor is listing at a price that will actually attract buyers and promote the sale. The object isn't to squeeze every last penny from the sale. The object is to actually sell! Many sellers make the mistake of listing their property at last week's or last month's price. As prices continue to drop, the sellers have to continually adjust their price downward, essentially chasing today's value but never quite getting there. Eventually sellers capitulate and sell at whatever number they can sell at, potentially reducing their sale proceeds substantially. Price your property to sell and take your beating. An actual sale is what this option is all about.

Along with an outright sale, you could look at selling to either another investor or to someone looking to move in. This option works in the proper circumstances, depending on a number of factors that include but are not limited to:

- today's property value in relation to your existing mortgage
- rentability
- cash flow generation potential
- suitability as personal residence

Sales techniques could be the [Lease Option more often described as a Rent To Own \(RTO\)](#). Or, you could sell by way of [Agreement for Sale](#). None of these techniques will likely be effective if your existing mortgage exceeds the value of the property by a substantial amount. But, I have seen deals put together where sellers with a mortgage principal \$20,000 more than the current value of the property actually contributed \$20,000 to the sale. They did not want their credit ruined by going to foreclosure.

### **The 'Negative Cash Flow' Option**

If your property is okay except for negative cash flow, then in these tougher economic times, you might consider carrying \$200, \$300, or even \$400 per month negative cash flow for a substantial period of time.

You can especially consider this option if the alternative is complete loss of the property and your substantial original investment along with ruination of your credit. If you bought a property for \$300,000 with 20% down, that is \$60,000. If you were negative cash flow \$300 per month for two years that is \$7,200.

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This is something to consider when you compare it against the loss of your \$60,000, bad credit, and a recognition of the fact that real estate markets are cyclical and our current downturn will certainly turn up sometime in the future. Obviously, the question is when?

### **Title-in-Lieu of Foreclosure (often called Deed-in-lieu in other jurisdictions)**

Some owners have used this process to stop a foreclosure quickly after it has started or to stop it from getting started. This process has you transferring the property back to the lender. You give the lender a transfer of land and sometimes a [quitclaim](#) and the lender stops the foreclosure.

Titles-in-lieu of foreclosure will probably ruin your credit to the same extent as a foreclosure would, so there isn't any real benefit there. Why would you do it? This method prevents or ends the foreclosure process quickly and may give you some room to negotiate with your lender. There are a number of situations where you should be able to negotiate.

In Alberta (but not in the rest of Canada) some mortgages are nonrecourse. Briefly, if you have a conventional mortgage (that is, a mortgage not insured by CMHC or other insurer) in your personal name, whether it is your personal residence or an investment property, all the lender can do is foreclose and take away the property. If the property is worth less than the mortgage, they can't come after the homeowner for the deficiency. You might be able to turn your nonrecourse mortgage into an advantage.

For example, I believe you have some room to negotiate if your property is substantially underwater and you have a non-recourse mortgage. Let's say that the mortgage principal is \$40,000 more than the current value of the property. The lender's legal bill for a very plain vanilla, no wrinkles foreclosure will be \$2500–\$5000. A smart lender will understand that if they foreclose they will lose \$42,500–\$45,000 being the sum of the deficiency and their legal costs. A smart lender would listen to your offer to pay the lender a portion of those uncollectible losses.

Remember, this is a negotiation. How much should you offer? Hard to say, this is a negotiation. For example, it might be a good deal for you if you paid the lender \$10,000 and agreed to transfer the title to the lender without a foreclosure with the further agreement by the lender not to make a credit report.

It might even be a good deal for the lender if they just got the property back without having to spend \$2500–\$5000 on their lawyer.

**Caution:** lenders often seem incapable of seeing what might be in their best interest. All they understand is their basic policy when the mortgage is in default, and they are often incapable of stepping outside the policy. For any of these negotiated settlements to work, you will have to move up the authority chain beyond your local branch or the lender's 800 number help desk.

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### **Foreclosure Already Started?**

For many homeowners and investors the above suggestions won't solve their problems. They are just in too deep with no real chance of ever catching up. Any attempt using the above suggestions would be only a temporary fix or delay. Really, unless you take other action there is just no reasonable hope to make up those back payments. The bank/lender will start a foreclosure action. The ultimate result of foreclosure is you lose your house and your credit is ruined for a lengthy period of time.

### **Once You Miss a Payment, Here's How a Typical Foreclosure Works**

1. At this point, if you decide not to make your first payments, the lender will almost assuredly start their usual 'missed a payment' routine. The routine varies from lender to lender, but usually includes a phone call or two from the branch or mortgage administration, a letter or two demanding payment and sometimes offering discussion, followed finally by a referral from the lender's mortgage administration to a foreclosure lawyer. This part of the procedure can take between two weeks (at its very shortest) and three months.
2. The foreclosure lawyer also probably writes a demand letter to you, the owner, indicating that they will commence action within a certain period of time if the mortgage is not brought into good standing. If you don't respond, the foreclosure action will be started by way of a document known as a Statement of Claim.

The lender will serve the document on you either personally or by substitutional service if they cannot locate you. There is then a waiting period before the lender can take the next step. This time is given to you to:

- File a Statement of Defense if you think you have a defense to the foreclosure (very unlikely),
  - File a Demand of Notice if you just want to keep getting advised of the lender's next steps in the court action or,
  - Perhaps you do nothing.
3. If you do nothing, the lender will get an appraisal of the property if they have not already done so and then make an official court application for a preliminary judge's order. At this court application, they will advise the judge of the status of the mortgage, how much it is in arrears, the value of the property according to the appraisal. They will ask the judge to set a time within which you have to pay, known as the 'redemption period.'

For owners living in the property as their personal residence with some equity, there is a minimum six-month redemption period (the time within which the owner gets to bring the mortgage back into good standing). For investors who have little or no equity in the property, it could be as little as a one-day redemption period.

4. At the end of the redemption period, the lender can ask for various types of order/relief. Typically, the judge orders the property listed for sale with a realtor on terms that the judge thinks are reasonable. If there

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are no offers, or if the lender is unhappy with the offers, then the property might get transferred into the lender's name.

Other than discussed above and if none of those solutions/improvements work for you, then your input into that typical foreclosure might be as follows.

When the lender's lawyer starts the foreclosure action by way of a legal document known as a 'Statement of Claim', you can:

1. Hire a lawyer and fight the foreclosure by issuing your own 'Statement of Defense.' There is usually no point to this because usually you have no defense to the lender's claim that your mortgage is in default.
2. Hire a lawyer or act for yourself in filing a 'Demand of Notice.' This requires the lender to provide you with notice of every step in the proceedings. There may be various points where you want to show up in court and have your say. Some of our clients just prefer that the lender's lawyer's numerous legal filings are served us here at [RMLO Law LLP](#), rather than having process servers constantly banging on their door. Plus, we can review what the lender is doing or asking for, which gives you a chance to go to court and have your say if you think you ought to or need to.
3. Do nothing. Many homeowners feel there isn't any point in hiring a lawyer or defending or even in getting a Demand of Notice. They either abandon the property with no further interaction or, some homeowners mail the keys back to the lender in a process called 'jingle mail' named after the jingling sound in the lender's mailroom from keys in envelopes.

***Caution:*** Be very careful if you think you don't have to worry because you have a nonrecourse mortgage. I can hear someone saying right now, *"Let the lender foreclose, all they can do is take the property. They won't be able to collect the \$50,000 that they will lose because my property is worth so much less than the principal on my mortgage."*

You have to be a little careful here. Yes, if your mortgage is a plain vanilla, non-recourse mortgage, you may not have anything to worry about. But, lenders aren't stupid. They understand about non-recourse mortgages in Alberta.

Lenders are constantly trying to get around the protection in s.40.1 of the [Law Of Property Act](#), and the way they do it is to try to turn those non-recourse, plain-vanilla mortgages into loans with an enforceable personal covenant. The lending trend has been way in the direction of other than plain-vanilla mortgages. Credit unions start out with a promissory note or other loan agreement secured by a mortgage. Other lenders use various kinds of loan agreements including lines of credit agreements, which are again secured by collateral mortgages. These are often described as HELOCs (home equity lines of credit). Scotiabank has their STEP (Scotia Total Equity Plan) mortgage.

STEP mortgages include a form of in-branch loan agreement with a collateral mortgage having a face value of 100% of the purchase price funded to a maximum of 80% of the purchase price.

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The theory is, as the value of the property increases, the lender can advance further funds without redoing their paperwork. Some STEP mortgages have the ability to tie loans to your VISA card. HSBC has their EPM (Equity Power Mortgage) being their form of mortgage, collateral to some form of loan agreement.

When these mortgages go bad, lenders sometimes take a run at you, the borrower. The lender says your mortgage is recourse and they should be able to collect any deficiency. So, we say again, if you don't know whether you have a nonrecourse mortgage, it is absolutely important to consult legal counsel and get an opinion.

### Lessons Learned:

1. The issues surrounding foreclosure are numerous and varied. Start educating yourself. At least read the blog posts referred to above.
2. Don't put your head in the sand. If trouble is on the horizon, deal with it. Way better to start figuring out your options long before the lender starts the foreclosure.
3. Be very careful about your supposed nonrecourse mortgage. There are lots of mortgage products and you might be in the recourse category with full responsibility.

### FORECLOSURE LOOMING? NON-RECOURSE MORTGAGE?

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