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Monday, April 21, 2003

# The Perfect Foreclosure Storm

*Hoosiers losing American dream at record rate*



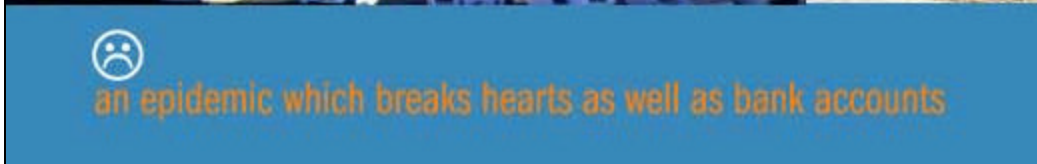
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Upper right, Mildred Wilkins, of Home Ownership Matters; on left, the Bayswater neighborhood (Eye photos by Ellen Jackson).



**Joe Saint: How's 'bout a Pacer-Piston Coach Swap**

**By Eileen Waldron**  
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The new beige vinyl-covered homes are wiping out the cornfields in astounding numbers. In the past two years, nearly 10 percent of new homes guaranteed by FHA in the entire country were built right here in the Indianapolis metropolitan area. Volume — in this high-risk sector — is just one of the reasons Indiana has the highest foreclosure rate in the county.

Obviously, Indiana's unprecedented job losses and economic turndown are also responsible. But the Indianapolis Eye has learned there are also other factors contributing to an estimated 3 out of 10 new homes ending up in sheriff's sales. Real estate agents, mortgage bankers and home inspectors are calling this an epidemic in the new-home sector, and one that breaks hearts as well as bank accounts.

"First, these newly built homes are marketed to the first-time homebuyer, who is not very sophisticated," said Mildred Wilkins, former real estate agent now turned housing activist. "Then there are special programs that allow them to pay nothing down — they're what I call the builder-banker brothers." Wilkins travels the state with a message many don't want to hear.

Wilkins is in the tough business of trying to help homeowners like Stephanie Hambrick, who could see her mortgage payment nearly double in two years. Wilkins said problems start when homebuyers like Hambrick don't realize exactly how much their payment will increase due to taxes and what is called a 2-1 buy down. Taxes are not assessed until the second year of occupancy and the 2-1 buy down results in the interest rate rising in the second year.

Others in the new-home industry agree some buyers are being set up for failure. "Mortgage lenders should not allow people to be qualified at a buy down rate. They should qualify people at the real rate along with the properly assessed taxes," said Aaron Starr, an FC Tucker agent specializing in foreclosures.

"The consumers I hear from say they didn't know that the payment would go up. I say to them, 'What do you mean you didn't know? You would have been told something.' Their response is, 'Well, they told me that my taxes would go up a little bit,'" said Wilkins.

### **Up, up, up and then shock**

Hambrick thought she was moving up when she bought her brand new home in Kensington Commons on the city's Eastside. Now she's desperately trying to sell it to avoid foreclosure.

A proud woman, she's trying to keep her spirits up. "I feel bad, but it was a learning experience," said Hambrick.

A look at Stephanie's paperwork, the many documents she signed during the home-buying process, points to how she could have misunderstand exactly how much her mortgage payment would rise.

In June of 2001, six months before she closed on the house, Hambrick signed what is called an estimated price quotation. It said her interest rate would be 4 7/8, and with only \$50 dollars a month set aside for taxes, she would pay \$816 a month. The cost of the house would be \$136,258.

"I kept saying over and over I had to keep my payment under \$1,000 dollars a month," said Hambrick.

At closing, the payment listed was more — \$839. But this was without accurate second-year property taxes and the effect of her 2-1 buy down. Both would make her payment go

well over \$ 1,000.

When the interest rate goes up due to the 2-1 buy down, her payment would be \$1,018 beginning in 2004 for the next 11 years. And her interest rate was not 4 7/8 but 6 7/8.

But there would be another expensive twist for Hambrick this year, according to Wilkins. In May, when her property taxes are finally assessed, the lender will want to recoup 12 months of taxes in six months. That could soon push her payment up to nearly \$1,300.

#### **Documents signed but what is escrow?**

Others in the industry confirm that many times new-home buyers are not getting correct information about how much their payment will go up. "If you ask salespeople, they'll tell you that they tell the buyer everything, but that's not the truth. The sales staff are young, they are trying to make a living, and they are paid on commission," said Aaron Starr, an FC Tucker foreclosure specialist.

But the trade association that represents builders disagrees. "I don't think that is a factor. We think it's the economy and high job loss in the state that are causing the problems," said Steve Lains, CEO of the Builders Association of Greater Indianapolis. As far as prevalence of defaults in the new-home sector, Lains says it is no greater than what occurs in existing homes.

And not all builders have the same practices, for the most part the companies building more expensive homes have better reputations and fewer defaults.



BAGI and the Metropolitan Board of Realtors will soon release a report about Indiana's high home foreclosure rate, which will point to the economy and job loss as the chief reasons for the high default rate.

That was indeed the other factor of the perfect foreclosure storm that happened to Stephanie Hambrick — she lost her job. A few months later she found another, but the damage was done. Through Wilkins, she contacted a realtor to put her house on the market.

#### **Then came the second shock**

She bought the home a little more than a year ago for \$135,000. Still almost brand new it appraised for \$112,000 and is now listed to move at \$106,000.

"How could a two-bedroom in that area originally appraise for \$135,000?" said Wilkins.

Home inspector Chris Schnepf told the Eye that trade magazines he reads are filled with letters from home appraisers complaining that lenders put pressure on them to "meet" a certain price, or else they won't use their services. "This results in inflated prices, especially in new-home developments," said Schnepf.

In a strongly worded letter written to Hambrick's current mortgage company, the realtor who is now trying to sell her home gave her opinion about why homes are in default in Hambrick's neighborhood:

"...(the builder) used a predatory marketing strategy of offering new buyers the option to construct a home with "Zero Dollars" as down payment. These buyers begin with zero or negative equity following their purchases. The purchase prices of these homes have been greatly inflated and after the real estate taxes are assessed on these properties, many

will find their payments have escalated beyond their ability to pay and more homeowners will lose their home to foreclosure.”



*Mike Troyan teaches classes about predatory lending for the Indiana Real Estate Commission*

“It would certainly make one question the original appraisal; was there a relationship between the lender and the builder? A number of them (new-home builders) have their own mortgage companies,” said Mike Troyan, a mortgage banker who teaches classes for Indiana Real Estate Commission.

#### **No free fireplace, really**

Troyan’s biggest beef with the new-home builders is what he hears from clients. “The builder will offer a free fireplace or some other option upgrade if they use their affiliated lender. I have personally had consumers apply for pre-approval (from my company). When they went to the builder, the builder tears up the pre-approval letter. They tell them, ‘If you don’t use our mortgage affiliate, we won’t pay your closing costs,’” said Troyan.

Troyan says this hurts the consumer because all those freebies get rolled into the price of the home anyway.

According to research done by Wilkins, the Bayswater subdivision in Indianapolis is a good example of home sticker shock. Foreclosures have doubled in two years with resale prices tumbling \$15,000 to \$40,000 dollars from the original purchase price.

Most homes in Bayswater, on the west side near 46th and High School Road, originally sold for \$95,000 to \$125,000. Two years later you can buy one of these homes for \$57,000. The trend is not limited to Marion County.

In Boone County at the I-65 Zionsville exit sits the sprawling Royal Run. Right at the edge of cornfields, four different builders have constructed more than 700 homes. In the past two years, seven homes were listed for foreclosure, most in the lower price bracket.

In many of these new-home communities, builders are still building new homes while empty foreclosed properties sit on the market with prices spiraling downward.

“Why would someone want to buy a home that’s two years old when they can have one built for them?” said Starr.

The foreclosure epidemic in new homes costs all of us.

When homes with government-backed loans like FHA go into foreclosure, they become the property of HUD — U.S. Department of Housing and Urban Development. HUD pays the mortgage company the balance of the mortgage. The builder is also free of financial ties, having sold the mortgage long ago to the mortgage company.

HUD then contracts with a private company — Golden Feather — to list the home. It often sells for thousands of dollars below what HUD paid the mortgage lender.

#### **Lenders don’t lend a hand**

To understand the next part of the perfect foreclosure storm Indiana is experiencing, you have to go back to the beginning, when a homebuyer first starts having trouble meeting mortgage payments.

In 2000, HUD released a clarification of a policy called loss mitigation. Simply put, the government wants lenders to work with homeowners so they will not have to go into foreclosure. The Eye has learned there is a pattern of ignoring the policy by lenders.

“The mentality within the mortgage lending community,” said Troyan, “says that if someone is more than 30 days late and they send in the payment, most times the lender will return that payment to the homeowner and ask for both payments. This is dehumanizing and the homeowner can never catch up and ends up losing the home.” Troyan calls this and other heavy-handed practices by lenders, “predatory servicing.”

If lenders followed HUD policy, a homeowner in financial trouble should be able to do the following:

- Postpone delinquent payments, putting them at the end of the mortgage.
- Refinance to get a lower interest rate and lower payments.
- Even something called a “partial claim” where the bank will give the homeowner money to pay back payments and get current, and the homeowner will pay HUD back later with no interest.

All this could be negotiated over a year, rather than the homebuyer rushing into foreclosure in a few months.

This in spite of the fact that HUD has a financial rewards policy to encourage lenders to do this and that the loss mitigation policy states “lenders are required to ... utilize loss mitigation whenever feasible to avoid foreclosure.”

“Consumers don’t even know loss mitigation exists; they are at the mercy of the lender,” said Troyan. He has now become extremely vocal about abuses in the lending industry, and he often hears from clients that lenders are demanding thousands of dollars in attorney fees first before they will work out an agreement with the homeowner. Another form of “predatory servicing,” according to Troyan.

“If the loss mitigation policy was followed by lenders, you would probably see the foreclosure rate decline by 50 percent in Indiana,” said Troyan, “We as mortgage lenders are in the position of finding ways to keep people in the homes, and not to kick them out. We all need to do a better job. “

John Hall, the HUD Field Office Director in Indianapolis, also says everyone in the home-buying industry needs to do a better job to lower Indiana’s high foreclosure rate. Hall had never heard of the lender practice of demanding attorney fees up front before entering into negotiations to forestall losing a home.

Fairly new on the job, Hall told the Eye this was a good education for him. For instance, he said he was amazed when he discovered that nearly 10 percent of the FHA loans for new homes are here in Central Indiana and that this fact could definitely be a contributing factor of why Indiana has the highest foreclosure rate in the country. “It costs all of us less if we are able keep people in their homes,” said Hall.

Like a tornado, the perfect foreclosure storm has hit Indiana hard. Record job losses and a problem economy have pulled the rug out for some in the new-home industry. What it exposes is less than truthful practices by builders, which results in setting up first-time homebuyers for failure. On top of that, lenders are ignoring HUD policy, which could keep the homebuyer from losing it all.

### **Related Links:**

[HUD's policy on how lenders should help homebuyers in trouble](#)  
[Home Ownership Matters](#)

## Reader Comments

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Posted: Tuesday, April 22, 2003

Article comment by: **Mildred Wilkins**

I thought the article and the photos were absolutely great. I especially liked the cover shot, the rising price on the house shot and the fact that you quoted me accurately. Thanks for a job well done. I will use this widely and have it posted to my site as well.  
mbw

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