<u>Foreclosure Implications for the Borrower under the USDA Rural Home Loan Program</u>

By Kassandra McQuillen

I recently had some clients come into my small town office with a serious and surprising problem. They had received a notice of Federal Debt in the amount of more than $130,000 for a home they owned and abandoned to foreclosure several years before. The U.S. Treasury was after them and they didn't understand why or what it meant.

My clients had purchased their first home in California in 2004 under the USDA Rural Home Loan Program. The mortgage broker had touted the program as a no money-down, easy to qualify for home loan program for first-time and low income home buyers. It sounded like a perfect fit for this family of five and they quickly found a brand new home that fit the bill. Wells Fargo loaned the money and the USDA guaranteed it under the Rural Home Loan Program. It seemed like a win-win situation.

Two years later the housing market crashed. Their home, which they borrowed $168,000 to purchase was now worth less than $60,000. The new neighborhood quickly emptied, lawns went brown, people abandoned their homes, moved on and allowed the banks to foreclose. My clients, after attempting to rent the home and discussing foreclosure options with several people, made the business decision to let the home go into foreclosure and purchase a new home in a better neighborhood for less than they owed on the first home. At the time my clients walked away from their home the principal balance on the mortgage was $160,000 and they claim they never heard from the bank about the foreclosure, its implications, or options to avoid it.

Wells Fargo went through the standard nonjudicial foreclosure procedures, eventually selling the home at a trustee's sale in 2009 for $65,000. Soon after the trustee's sale, Wells Fargo submitted a loss claim to the USDA in the amount of $112,000 (the difference in principal balance and sale price plus interest and costs associated with foreclosure sale, of which they were reimbursed $103,000 by the USDA under the Rural Home Loan program.

Imagine my clients' surprise in the summer of 2010, two years after they went into default on the loan to Wells Fargo, when they received a bill from the USDA for more than $100,000.

After some investigation, and having the U.S Treasury take their 2010 income tax return money, my clients learns just what the USDA Home Loan Program was all about in a time of financial crisis: a personal guarantee by the homeowner/borrower to the U.S. Government on their own loan. In the meantime, Wells Fargo was reimbursed the majority of its loss in an expeditious process that took less than six months. The only winner on such a loan in this time of upside down homes is the Lender.

Virtually the only way out of the USDA Home Loan personal guarantee is to prove negligence on the part of the Lender or to file bankruptcy or to negotiate repayment.

Lenders and mortgage brokers push the program to lower income families and first-time buyers as the "no money down, no mortgage insurance loan". There are websites out there pushing these loans, particularly since the program was expanded in 2009. (http://www.usdaloans.com/, http://www.usdaloanapproval.com/, http://www.usdahomeloanprogram.com/,) None of the websites I found touting the loans mention the fact that when the government pays the lender for a loss, the loss becomes the responsibility of the borrower.

My clients claim they were never told they would be responsible for the debt if the loan foreclosed. They also claim they never realized it could follow them or force them into bankruptcy. They claim the one paragraph acknowledgement and agreement to pay the USDA in the event of loss was something they never noticed and never had explained to them by the broker among the myriad of papers they signed in buying their first home. The mortgage broker, like so many in California, is no longer a broker and has disappeared along with his files on the matter. Had they known foreclosure meant a six-figure federal debt they never would have walked from the home.

There is something wrong with a federally guaranteed loan program that leads less-than qualified individuals into home ownership and barely manageable mortgages at the same time it doesn't insure the borrower is fully aware of the implications of participating in the program.

The lesson here: No matter how upside down your home is, if you have a USDA Rural Home Loan, do not allow it to go into default because you will not be able to walk away without filing bankruptcy.