BUREAU OF CONSUMER PROTECTION Consumer Facts

Protecting Wisconsin Consumers for 75 Years

Home equity scams

Home equity loans

A home equity loan is a loan for a fixed amount of money that is secured by your home. You repay the loan with equal monthly payments over a fixed term, just like your original mortgage. If you do not repay the loan as agreed, your lender can foreclose on your home.

The amount that you can borrow usually is limited to 85 percent of the equity in your home. The actual amount of the loan also depends on your income, credit history, and the market value of your home.

Ask all the lenders you interview to explain the loan plans available to you. If you do not understand any loan terms and conditions, ask questions. They could mean higher costs. Knowing just the amount of the monthly payment or the interest rate is not enough. The annual percentage rate (APR) for a home equity loan takes points and financing charges into consideration. Pay close attention to fees, including the application or loan processing fee, origination or underwriting fee, lender or funding fee, appraisal fee, document preparation and recording fees, and broker fees; these may be quoted as points, origination fees, or interest rate add-on. If points and other fees are added to your loan amount, you will pay more to finance them.

Before you sign, read the loan closing papers carefully. If the loan is not what you expected or wanted, do not sign. Either negotiate changes or walk away. You also generally have the right to cancel the deal for any reason – and without penalty – within three days after signing the loan papers.

Home equity lines of credit

A home equity line of credit – also known as a HELOC – is a revolving line of credit, much like a credit card. You can borrow as much as you need, any time you need it, by writing a check or using a credit card connected to the account. You may not exceed your credit limit. Because a HELOC is a line of credit, you make payments only on the amount you actually borrow, not the full amount available. HELOCs also may give you certain tax advantages unavailable with some kinds of loans. Talk to an accountant or tax adviser for details.

Like home equity loans, HELOCs require you to use your home as collateral for the loan. This may put your home at risk if your payment is late or you cannot make your payment at all. Loans with a large balloon payment – a lump sum usually due at the end of a loan – may lead you to borrow more money to pay off this debt, or they may put your home in jeopardy if you cannot qualify for refinancing. And, if you sell your home, most plans require you to pay off your credit line at the same time.

What safeguards are built into the loan?

One of the best protections you have is the Federal Truth in Lending Act. Under the law, lenders must tell you about the terms and costs of the loan plan when you get an application. Lenders must disclose the APR and payment terms and must tell you the charges to open or use the account, like an appraisal, a credit report, or attorneys' fees. Lenders also must tell you about any variable-rate feature and give you a brochure describing the general features of home equity plans.

The Truth in Lending Act also protects you from changes in the terms of the account (other than a variable-rate feature) before the plan is opened. If you decide not to enter into the plan because of a change in terms, all the fees you paid must be returned to you.

Once your home equity plan is opened, if you pay as agreed, the lender, generally, may not terminate your plan, accelerate payment of your outstanding balance, or change the terms of your account. The lender may halt credit advances on your account during any period in which interest rates exceed the maximum rate cap in your agreement, if your contract permits this practice.

Before you sign, read the loan closing papers carefully. Make sure to know all of the upfront closing costs, what are the continuing costs, repayment terms during the loan and what if any safeguards are built into the loan. If the HELOC is not what you expected or wanted, do not sign the loan. Either negotiate changes or walk away. And like a home equity loan, you also generally have the right to cancel the deal for any reason – and without penalty within three days after signing the loan papers.

The three-day cancellation rule

You have three days to reconsider a signed credit agreement and cancel the deal without penalty. You can cancel for any reason but only if you are using your principal residence – whether it is a house, condominium, mobile home, or house boat – as collateral, not a vacation or second home.

During this waiting period, activity related to the contract cannot take place. The lender may not deliver the money for the loan. If you are dealing with a home improvement loan, the contractor may not deliver any materials or start work.

If you decide to cancel, you must tell the lender in writing. You may not cancel by phone or in a face-to-face conversation with the lender. Your written notice must be mailed, filed electronically, or delivered, before midnight of the third business day. If mailed, it is recommended that you send the notice by certified mail.

Harmful home equity practices

You could lose your home and your money if you borrow from unscrupulous lenders who offer you a high-cost loan based on the equity you have in your home. Certain lenders target homeowners who are older or who have low incomes or credit problems – and then try to take advantage of them by using deceptive, unfair, or other unlawful practices. Be on the lookout for:

- **Loan flipping** The lender encourages you to repeatedly refinance the loan and often, to borrow more money. Each time you refinance, you pay additional fees and interest points. That increases your debt.

- **Insurance packing** The lender adds credit insurance, or other insurance products that you may not need to your loan.

- **Bait and switch** The lender offers one set of loan terms when you apply, then pressures you to accept higher charges when you sign to complete the transaction.

- **Equity stripping** The lender gives you a loan based on the equity in your home, not on your ability to repay. If you cannot make the payments, you could end up losing your home.

- **Non-traditional products** The lender may offer non-traditional products when you are shopping for a home equity loan.

  For example, lenders may offer loans in which the minimum payment does not cover the principal and interest due. This causes your loan balance, and eventually your monthly payments, to increase. Many of these loans have variable interest rates, which can raise your monthly payment more if the interest rate rises.

  Loans also may feature low monthly payments, but have a large lump-sum balloon payment at the end of the loan term. If you cannot make the balloon payment or refinance, you face foreclosure and the loss of your home.

- **Mortgage servicing abuses** The lender charges you improper fees, like late fees not allowed under the mortgage contract or the law, or fees for lender-placed insurance, even though you maintained insurance on your property. The lender does not provide you with accurate or complete account statements and payoff figures, which makes it almost impossible for you to determine how much you have paid or how much you owe. You may pay more than you owe.

- **The "home improvement loan"** A contractor calls or knocks on your door and offers to install a new roof or remodel your kitchen at a price that sounds reasonable. You tell him you are interested, but cannot afford it. He tells you it is no problem – he can arrange financing through a lender he knows. You agree to the project, and the contractor begins work. At some point after the contractor begins, you are asked to sign a lot of papers. The papers may be blank or the lender may rush you to sign before you have time to read what you have been given. The contractor threatens to leave the work on your house unfinished if you do not sign. You sign the papers. Only later, you realize that the papers you signed are a home equity loan. The interest rate, points and fees seem very high. To make matters worse, the work on your home is not done right or has not been completed, and the contractor, who may have been paid by the lender, has little interest in completing the work to your satisfaction.

- **Signing over your deed** If you are having trouble paying your mortgage and the lender has threatened to foreclose, another "lender" may contact you with an offer to help you find new financing. Before he can help you, he asks you to deed your property to him, claiming that it is a temporary measure to prevent foreclosure. Once the "lender" has the deed to your property, he may start to treat it as his own. He may borrow against it (for his benefit, not yours) or even sell it to someone else. Because you do not own the home any more, you will not get any money when the property is sold.

- **Loan modification** Be especially cautious if you are contacted by a foreclosure consultant who promises to help you arrange a loan modification. Many are scam artists who collect fees upfront but then do not provide the promised service. Ask the foreclosure consultant to explain their fees and provide you with a written contract. Do not pay any fees in advance for loan modification services. Wisconsin law prohibits a foreclosure consultant from collecting any fees for loan modification services until after the foreclosure consultant has fully performed each and every loan modification service they contracted to perform.

  The US Department of Housing and Urban Development (HUD) provides a listing of approved housing counselors on their website at: www.hud.gov.

Protecting yourself

You can protect yourself against losing your home to inappropriate lending practices. Here is how:

Do not:

- Agree to a home equity loan if you do not have enough income to make the monthly payments.

- Sign any document you have not read or any document that has blank spaces to be filled in after you sign.

- Let anyone pressure you into signing any document.

- Agree to a loan that includes insurance or extra products you do not want.

- Let the promise of extra cash or lower monthly payments get in the way of your good judgment about whether the cost you will pay for the loan is really worth it.

- Deed your property to anyone. First consult an attorney, a knowledgeable family member, or someone else you trust.

Do:

- Shop around. Negotiate with more than one lender. Do not be afraid to make lenders and brokers compete for your business by letting them know that you are shopping for the best deal.

- Ask specifically if insurance is required as a condition of the loan. If it is not, and a charge is included in your loan and you do not want the insurance, ask that the charge be removed from the loan documents. If you want the added security of insurance, shop around for the best rates.

- Keep careful records of what you have paid, including billing statements and canceled checks. Challenge any charge you think is inaccurate.

- Check contractor's references when it is time to have work done in your home. Get more than one estimate.

- Read all items carefully. If you need an explanation of any terms or conditions, talk to someone you can trust, such as a knowledgeable family member or an attorney. Consider all the costs of financing before you agree to a loan.

For more information

For more information or to file a complaint, visit or contact the:

Office of Consumer Affairs
Department of
Financial Institutions
PO Box 8041
345 W Washington Ave
Madison WI 53708-8041

Toll-free in WI:
(800) 452-3328

(608) 264-7969

WEBSITE:
www.wdfi.org

(Information taken from Federal Trade Commission "Home Equity Loans and Credit Lines" 08/12")