

The 6 phases of a foreclosure

If you or someone you know is facing possible foreclosure, you should know what to expect.

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Many people have either gone through foreclosure, a process that allows a lender to recover the amount owed on a defaulted loan by selling or taking ownership of the property, or know someone who has.

RealtyTrac released its U.S. Foreclosure Market Report on April 15 for the first quarter of 2010. The report calculates foreclosure filings, including default notices, scheduled auctions and bank repossessions, and showed that 932,234 properties were involved in the first quarter. That was a 7% increase from the last quarter of 2009 and a 16% increase from the first quarter of 2009. An astonishing one in every 138 U.S. housing units received a foreclosure filing during the quarter. If you or a loved one are facing foreclosure, make sure you understand the process. While it varies from state to state, there are normally six phases of a foreclosure.

Phase 1: Payment default

A payment default occurs when a borrower has missed at least one mortgage payment. The lender will send a missed-payment notice indicating that it has not yet received that month's payment. Typically, mortgage payments are due on the first day of each month, and many lenders offer a grace period until the 15th. After that, the lender may charge a late-payment fee and send the missed payment notice.

After two payments are missed, the lender may send a "demand letter." This is more serious than a missed-payment notice; however, at this point the lender is probably still willing to work with the borrower to make arrangements for catching up on payments. The borrower would normally have to remit the late payments within 30 days of receiving the letter.

Phase 2: Notice of default (NOD)

A notice of default is sent after 90 days of missed payments. In some states, the notice is placed prominently on the home. At this point, the loan will be handed over to the lender's foreclosure department in the same county where the property is located. The borrower is informed that the notice will be recorded. The lender will typically give the borrower another 90 days to settle the payments and reinstate the loan. This is referred to as the reinstatement period.

Phase 3: Notice of trustee's sale

If the loan has not been brought up-to-date within the 90 days after the notice of default, a notice of trustee's sale will be recorded in the county where the property is located. The lender must also publish a notice in the local newspaper for three weeks indicating that the property will be available at public auction. All owners' names will be printed in the notice and in the newspaper, along with a legal description of the property, the property address and when and where the sale will take place.

Phase 4: Trustee's sale

The property is placed for public auction and will be awarded to the highest bidder who meets all of the necessary requirements. The lender, or firm representing the lender, will calculate an opening bid based on the value of the outstanding loan, any liens and unpaid taxes, and any costs associated with the sale. Once the highest bidder has been confirmed and the trustee's sale is completed, a "trustee's deed upon sale" will be provided to the winning bidder. The property is then owned by the purchaser, who is entitled to immediate possession.

Phase 5: Real-estate owned (REO)

If the property is not sold during the public auction, the lender will become the owner and will attempt to sell the property on its own, through a broker or with the assistance of an REO asset manager. These properties are often referred to as "bank-owned." The lender may remove some of the liens and other expenses in an attempt to make the property more attractive.

Phase 6: Eviction

The borrower can often stay in the home until it has been sold either through a public auction or later as an REO property. At this point, an eviction notice is sent demanding that any people vacate the premises immediately. Several days may be provided to allow the occupants sufficient time to remove any personal belongings, and then typically the local sheriff will visit the property and remove the people and any remaining belongings. Belongings may be placed in storage and retrieved later for a fee.

The bottom line

Throughout the foreclosure process, many lenders will attempt to make arrangements for the borrower to get caught up on the loan and avoid a foreclosure. The obvious problem is that when a borrower cannot meet one payment, it becomes increasingly difficult to catch up on multiple payments. If there is a chance that you can catch up on payments -- for instance, you just started a new job after a period of unemployment -- it is worth speaking with your lender. If a foreclosure is unavoidable, knowing what to expect throughout the process can help prepare you.