ACCELERATION – THE KEY TO FORECLOSURE

By Bruce J. Bergman

Any properly drawn mortgage will contain a clause giving an **option** to the lender to declare due the entire balance of principal and interest on the loan upon the happening of certain events. The most obvious and common default triggering this right is the failure of the borrower to make the payments. (There are, of course, other defaults, such as failure to keep the premises insured or neglect to pay taxes, among others. But these are less frequently encountered and are generally treated by courts as less severe, raising legal issues not necessary for this article.)

When a borrower does not pay, the lender has two basic choices. At the expiration of the grace period (usually fifteen days, but it can be more or less), he may begin collection procedures, or he can accelerate. While there are very good reasons why acceleration might be in order at this point, most lenders follow the usual custom of giving the borrower further opportunities to submit the past due payments. An installment one month late usually precipitates one type of letter. Two months' worth of arrears elicits a sterner warning. At the end of three months, most lenders will, and should, accelerate.

This acceleration — the declaring of the entire balance due — is the essential method of controlling the collection-foreclosure process. It is critical because it gives to the lender enormous leverage and allows him to deal from a position of strength, on **his** terms and at **his** pace. To appreciate this sweeping statement, look at it this way. Until you accelerate, the borrower is free to pay his arrears, at his leisure and convenience. You **must** accept a valid tender of those arrears, even if months or even years late. On the other hand, once there has been acceleration, arrears can be rejected without any reason. You may then insist — if you choose — upon full payment of the **entire** mortgage.

Of course, a lender may not wish to extract that full payment. But having the power to do so has a considerable salutary effect on the future of that loan. In addition to establishing control over the situation, which we will review in further detail, there are two major reasons explaining why the acceleration is so vital.

First, suppose the not uncommon circumstance of the chronic defaulter. Month after month, year after year, you have chased him for the payments and you no longer want the time, expense and problem this borrower represents. But he and his problems are yours for the life of the loan — in the absence of acceleration. As noted, before you accelerate, the borrower is free to tender his arrears at any time and you are constrained to accept, even if you prefer not to. However, once you have accelerated the balance, you need not accept those arrears. You may instead require full satisfaction of the mortgage.

Second, suppose this particular loan is at an interest rate well below the current market return. No matter how tardy the borrower has been, until you have validly accelerated, the loan will continue to yield that deficient rate of return. But once you **have** accelerated, you are free to foreclose, thus eliminating this unwanted loan, or, alternately, to insist that the borrower enter into a modification of the mortgage whereby the interest rate is increased to an appropriate percentage rate. While the borrower may object, he has no choice. Should he decline to agree, he suffers foreclosure or the obligation to pay the loan in full. Again, **there** is the leverage.

There is still another corollary benefit to this concept of acceleration. Assume the unfortunate but not so uncommon case where the mortgage documents neglect to provide recompense for legal fees. In most jurisdictions, no matter how extensive and expensive your collection efforts have been, you cannot compel the borrower to pay you for it. Similarly, if the foreclosure goes to a conclusion, the legal bill presented by counsel must be paid by the lender. But after acceleration, and assuming you wish to accept a reinstatement, as a condition of that, you may correctly demand return of legal fees incurred. The borrower may deem this unfair — even outrageous — but the lender is simply not obligated to reinstate after acceleration.

To clarify the point further, let's examine a typical amalgam of frequently encountered circumstances.

Here is the example. Borrower Smith owes his $750 monthly mortgage payment on January 1. For some reason, he fails to remit the check on the due date. The mortgage contains the usual grace period of fifteen days, after which the lender has the right to accelerate.

The sixteenth day passes and still Smith does not pay. He has now obligated himself to pay a late charge — usually two percent. The lender makes some phone calls and sends Smith a letter attempting to collect the one-month arrears. Smith promises to send his check, but neglects to do so.

It is now February and the lender is continuing its requests. Smith finally sends his January and February payments, but submits them on condition that the lender release some escrow monies it was in fact justly retaining. The lender refuses to accede to the condition and returns the checks. It is now late March. With two percent late charges accruing, Smith owes three months' payments, plus late charges of $45, for a total of $2,295.

Smith relents, withdraws his condition and mails a check for $2,200, the three months' mortgage arrears. The lender rejects the $2,200 as insufficient because late charges were not included

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and returns Smith's check. By this time the lender has concluded that this mortgage is no longer worthy of the staff time necessary to effect collection, so it exercises its right of acceleration and sends a letter to Smith declaring the entire principal balance immediately due and payable.

Upon receipt of the acceleration letter, Smith mails his check for the full \$2,295. The lender rejects and returns the checks, informing him that the file has been turned over to counsel to start a foreclosure action. Based upon these facts, Smith's lawyer tells him he can't lose the case and puts in an answer.

Who wins? The lender does. Given the recited events, the lender is entirely correct in proceeding with the foreclosure and will be successful. This is why.

- When a borrower "promises" to pay his obligation — and whoever refuses to pay — he has done nothing. A promise or offer is not the equivalent of an actual tender. (At the time of the "promises" the lender could have chosen to accelerate.)
- A tender submitted conditionally is not valid. It must be unconditional. (Again, the lender could have ended the problem at that time with acceleration.)
- A tender of less than the full amount validly due is not considered a tender.
- A borrower may avoid acceleration if he tenders all arrears in full prior to acceleration. In our example, full payment of arrears came **after** acceleration and was therefore properly rejected.

While not every case contains each of these events, the point should be clear. Some reasonably significant number of borrowers, for a wide variety of reasons, either cannot or will not make their payments. There must come a time when a lender recognizes that the borrower's promises and efforts are either insincere or that the wherewithal to pay simply does not exist. When that time arrives, collection efforts will probably prove fruitless. Then it is time to accelerate. When you do, the borrower is much more likely to realize that the lender "means business". A demonstration of strength, it is suggested, is a better way to bring a conclusion than mere gracious equivocating.

To carry the idea a step further, all during the collection process, interest and arrears are continuing to accrue. In the meanwhile, the property itself may be deteriorating and there is a good chance that the security for the loan is thus in jeopardy. Time may then be the lender's enemy. Until acceleration, there is no progress. Upon acceleration, the foreclosure can proceed.

Suppose then the first step is begun, preparing the summons and complaint, and in most states, a document called a lis pendens. The borrower is now awakened to the threat of eventual loss of the property. He promises to reinstate and pay the legal fees incurred. The lender is prepared to accept such reinstatement. You could then wait for the check **or,** proceed to the next step in the action if the promised check does not arrive. If payment is forthcoming, the problem is over and the lender has incurred no loss. If the check does not arrive, you proceed to the next plateau in the case (in many states a referee's computation of the sum due.)

That the borrower has not sent the check is of little moment. The lender is that much closer to the foreclosure sale. If **now** the borrower finally pays, he is obligated also for the additional legal fees in having carried the action further. Again, the lender loses nothing — all of which was precipitated by judicious use of acceleration.

Then the question is, how to accomplish this acceleration? Although some mortgage acceleration clauses are self-executing, that is highly unusual and clearly the exception. Rather, these provisions provide in essence that upon the happening of some occurrence, the lender has the right, or option, to make a declaration that the entire sum secured by the mortgage is immediately due and payable. The exercise of that election is something which must be manifested.

There are two ways to do it. One is to send a letter setting forth the acceleration. The other choice is to demonstrate the acceleration by actually filing the legal papers, i.e., the summons and complaint (and in some states the notice of pendency) with the court. While either method works, it is obviously easier and faster to use the correspondence method.

If the letter route is chosen, there are two further points to be made. The lender can prepare the letter himself — the most rapid way to obtain the leverage provided by acceleration — or to have his counsel do it. The first way is preferable, so long as the letter is properly drafted. The time involved in conveying the file to the attorney mitigates in favor of recommending that the lender attend to it.

Regardless of who prepares the correspondence, its content is essential. It must be an absolutely clear, unequivocal declaration that the lender has chosen to demand due the entire balance of principal and interest. For example, it would not be effective to demand payment of arrears within ten days, failing in which the lender intends to call the balance or foreclose. That is merely a statement of a future intention and will not suffice.

There is one final item to be considered. The terms of the mortgage will control the right to accelerate. Some mortgages will not permit acceleration unless and until a borrower has been given some period of notice to cure a default. Only when the notice period has expired with the default uncured may there be an election to accelerate. Moreover, the mortgage may address the mode of transmission of the letter. Although not common, it might require any notices to be sent by certified mail, in which event, of course, the lender must comply. In most instances, the means of transmittal is regular mail. If such is the case, a recommended procedure is to send the letter by **both** certified mail return receipt requested and regular mail. The certified letter may bring proof of receipt which can be helpful in litigation. For the clever borrower who will refuse a certified letter, the regular mail will nevertheless have been received.

No discussion of acceleration will be fully complete without an examination of all the applicable case law in every state, which is certainly beyond the purpose of this article. But the concept is

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clear. The astute lender can do himself a great service by sage employment of the power offered by use of acceleration provisions.

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MARKETING SECONDS

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sion to borrow money, especially the amount of money involved in a second mortgage, is a very major decision for our customers. Having to wait a week, two weeks, even four weeks or more, just to get a "yes" or "no" is not just inconvenient — it's agonizing. At Beneficial, we rely on local, fast decision making, not on committees remote from the point of sale. We pride ourselves on being able to get the commitment to the customer in 48 hours. And I cannot tell you how many customers have told us that this speed is the main reason they first did business with Beneficial.

Second, service means simplicity. There's simply no need for the incredible hassles that some lenders put their applicants through. It doesn't produce any additional protection or profit for lender; all it does is turn off the borrowers. Even if they get their loan, they have no inclination to come back the next time they need one of your products. We try to keep things as simple, relaxed and friendly as possible. This approach was effective even in the less hurried years gone by. Today, in this rush-rush era of two workers and two mortgages in the American household, this no-hassle borrowing is very important in our recipé for repeat business.

Finally, service means ongoing care. We have a company maxim: Marketing goes beyond the point of sale. The office that strikes the deal is also the office that handles delivery and future servicing as well. Our managers stay in touch with the consumers who buy our seconds. If a problem has arisen with a customer, we want to know about it before it gets out of hand, at a time when we may be able to help get their finances back on track.

The point is, every time our managers renew a contract with their outstanding customers, they are simultaneously strengthening the relationship and probing for changing circumstances that could make possible the sale of new products to the same person. In many ways, this is the cornerstone of the concept that ongoing care and service are the best forms of marketing.