Short Sale

When a homeowner owes more on a property than it is currently worth and one of the above solutions do not apply to their situation, there is the option of pursuing a short sale. The short sale process will be covered extensively in the next section on short sales.

Definition of a Short Sale

A homeowner is 'short' when: When a borrower owes an amount on his property that when combined with closing costs and commission is higher than current market value.

A short sale occurs when:

A negotiation is entered into with the homeowner's mortgage company or companies to accept less than the full balance of the loan at closing. A buyer closes on the property and the property is 'sold short'.

What a Short Sale Is Not

It needs to be clear to You the homeowner; a short sale is a way to avoid foreclosure. It is not a 'get out of my mortgage free card'. For a short sale to be approved the seller has to either be in or be headed for foreclosure. This means that you have to have a valid financial hardship for why you can't pay the mortgage. A seller without a financial hardship that is upside down on their mortgage and wants to sell is not a potential short sale, they are a dissatisfy homeowner. Unfortunately this individual will either have to wait the market out, bring cash to closing or in the most extreme of cases let the property go into foreclosure.

Determine Initial Market Price

There are five factors, in order of importance, I consider when pricing a distressed property:

(1) Fair Market Value
(2) Time Left before Foreclosure or Pre-Foreclosure
(3) Days on Market
(4)Property Condition
(5)What is Owed on the Property

<u>Unfortunately the average agent </u>looks at a property and begins with the **5th item**

of importance on our list, determines what is owed, adds closing costs and commissions and sets the asking price of the property.

Fair Market Value
Do a full CMA paying special attention to what is and isn't selling and days on market. A complete CMA will be the basis for every price determination you make.

Time Left before Foreclosure or Pre-Foreclosure
How much longer do you have before you are in foreclosure or if you already are in the process how much longer do you have? The reason that time is so important is that timing could be the single most important factor in pricing the property. In this case you would need a contract immediately so you take fair market value, discount significantly and try to put a contract in front of the Lender.

Days on Market
How much time do you have left, you need to compare this to the average days on market to SELL and adjust expectations accordingly.

Property Condition
Next you assess what condition the property is in, what are the issues it has that will hinder a sale. It is important that you evaluate the property against other comparable properties, not against your personal opinion. Remember this is not a traditional listing; you simply want to determine if there is anything out of the ordinary in this particular property that will hinder a sale. If you determine there is then you adjust the pricing. The question to ask yourself is, 'what price would get a buyer interested in this property accounting for all it's issues?' Add your estimated amount to your calculation.

Amount Owed
The final step in considering where to price a property is to consider what the borrower owes. If you have the time, you may initially need to price the property at what is owed plus closing costs and commissions then make price reductions accordingly at least every two weeks. This is only advised in situations where the borrower has not missed a payment and the property is in good condition. If you simply do not have the time or the property is in inferior market condition price the property accordingly and get a contract to present to the bank.
FMV...Fair Market Value – Timing....

WHY WOULD A LENDER ACCEPT A SHORT SALE?

One of the most common misconceptions that a very high percentage of homeowners and agents have is that their lender is lying in wait ready to jump out and take their house. Nothing could be farther from the truth. Reality is lenders and financial institutions are in the finance business not in the real estate business and they do not want your potential clients' property. In fact a foreclosure has far reaching financial and regulatory consequences that most people are not aware of.

What is an Acceptable Hardship?

You must have a hardship that is preventing you from being able to pay the mortgage. Examples of acceptable financial hardships are:

1. Loss of Job
2. Business Failure
3. Damage to Property
4. Death of a Spouse
5. Death of family members
6. Severe Illness
7. Inheritance
8. Divorce
9. Mandatory Job Relocation
10.. Medical Bills
11. Military Service
12. Payment Increase or Mortgage Adjustment
13. Insurance or Tax Increase
14. Reduced Income
15.Separation
16.Too much debt
17.Incarceration

Mortgage Forgiveness Debt Relief Act of 2007

This act was originally introduced HR 3648 and was passed into law on December 20th 2007 when it was signed by the president. The Bill received an overwhelming amount of support in the House and was seen by many as a major step in the right direction. Prior to the passage of this law, for any debt that was forgiven in a short sale or a foreclosure the homeowner would receive a 1099 and would have to report this forgiven (or canceled) debt as income. This still holds true for those individuals who do not qualify for the exceptions of this act. From January 1, 2007 to January 1st, 2010 eliminates the phantom tax on debt cancellation in mortgage discharge.

- Debt must have been debt incurred to acquire a principal residence.
- Canceled debt up to $2,000,000 is eligible.
- Sets forth rules for determining the allowable amount of the exclusion for taxpayers with non-qualifying indebtedness and taxpayers who are insolvent.
- Debt from a second (non acquisition) mortgage or HELOC is not eligible.
- Canceled debt from investment properties and second homes is not eligible.

Deficiency Judgment

In some states the lender can obtain a deficiency judgment against a homeowner for any amount they are unable to recuperate through a foreclosure or short sale. This means that if your client has a mortgage for $200,000 and the bank forecloses and sells the property at auction for $125,000 they could obtain a deficiency judgment for $75,000.

This allows the bank to pursue collections against the homeowner for $75,000 and in some states garnish his wages. In most cases this does require an additional legal action against the homeowner to obtain a judgment. This is another reason that it is so important to exhaust every option a homeowner may have to avoid foreclosure. This does require a separate action to be filed in court causing the mortgage company to incur further expense. The mortgage company is also acutely aware of the borrower’s inability to pay so they often see further collection as fruitless.

REO Property

If a property goes through the foreclosure process, one of two things happen at the end:

It is either sold to the highest bidder at auction, or very often it is taken over by the bank as an owned asset. REO stands for Real Estate Owned. As mentioned earlier, the bank does not want to take over a homeowner's property however when the foreclosure time line runs out and the property does not sell at auction they have no other choice. At that point the property is handled by the banks REO or Owned Asset department. They will hire an agent (typically one they already have a relationship with) and there is not further opportunity with the homeowner.

The other major issue with REO property is that once a lender takes over a property and puts it back on the market, may times they will do so at highly discounted rates. In this case it will be the lender setting the market price for an area, not an agent. These properties will often be the lowest priced in a neighborhood.

For a Free Consultation please contact Jack Lara a Broker-Associate at Keller Williams Realty of Pensacola (850) 471-5000 or Email: JackLara@kw.com

*****Please Seek Professional Financial & Legal Advice*****