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Short sale basics

A home buyer looking for a bargain can try picking up a house via a short sale, but the process can require nerves of steel.

By **DAVID P. WILLIS** • BUSINESS WRITER • April 25, 2010

So you're thinking about buying a house where the owners are financially underwater and unable to afford their mortgage, a transaction **known as a short sale**.

Make sure you have lots of patience.

It took three months for the bank to approve Joe and Lindsay Thein's offer for a four-bedroom home in Hazlet. (In a typical real estate transaction, an approval can come as quickly as 24 hours.) They closed on their first home a month later.

"It was very stressful," said Lindsay Thein, 27. "We were basically in limbo the whole time. We didn't find out until I would say a couple of weeks before we closed that we had gotten the house. We just continued to look for houses while our offer was in."

So-called short sales can lead to bargains, making them attractive to buyers. The Theins purchased their home, listed at \$400,000, for \$355,000. It was originally priced at \$500,000.

Since the start of the recession, many homeowners, stuck with houses they purchased at higher prices during the housing bubble, have found themselves with properties that have lost value.

In essence, these homeowners find their house is worth less than their mortgage balance, and would command a lesser price than they paid. "If you are underwater on the home, to sell it you have to make up the difference between the selling price and the (mortgage) principal," said economist Joel Naroff, president of Naroff Economic Advisors.

Unable to do so, sellers resort to a short sale, a lengthy, difficult sales process that in the end allows them to walk away without paying the full balance. The other option: foreclosure.

Short sales have complicated the already battered housing market and in some areas have weighed down home prices.

Let's take a look at short sales in New Jersey. The effects have been limited in the state, said Jeffrey Otteau, president of the Otteau Valuation Group in East Brunswick.

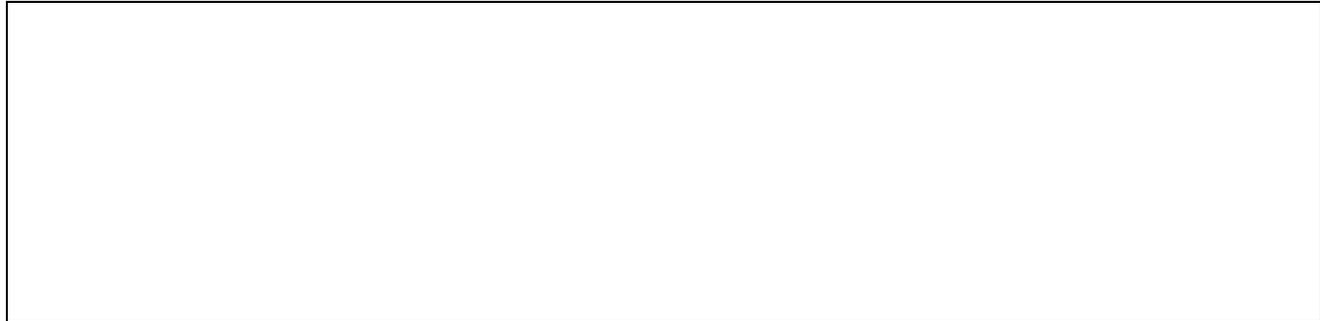
In 2009, 5 percent of home sales in New Jersey were properties in distress, mostly short sales, Otteau said. That's up from 3 percent in 2008, and 1 percent in years prior.

In areas further removed from the state's northern job centers, including Ocean County, as well as urban areas, short sales were a greater part of the mix. In those places, "higher concentrations of short sales are infectious and create downward pressure on home prices," Otteau said.

The effect of short sales in higher-income markets and those closer to jobs centers is "nonexistent" and has had a minimal effect on waterfront or waterview vacation houses, Otteau said.

While the state's economy has lifted itself out of a

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recession, short sales are not over. With mortgage delinquency rates at about 10 percent, homes in short-sale situations represent about 15 percent of the unsold inventory in the market, Otteau said. "There is a large number of these that have not yet been digested by the housing market."

The time it takes to complete a short sale is among the challenges cited by real estate agents.

Depending on the complexity and state of paperwork submitted by the seller, a purchase can take three or four months to as long as a year to complete, said Mary Chin-Greninger, sales associate at Coldwell Banker Residential Brokerage in Howell.

Why so long? "The bank that's holding the mortgage on the property really controls the whole tempo of the process," said Walter La Cicero, a real estate attorney in Lavallette. "If (the buyers have) some time constraints -- they're looking to get kids in the school district or something like that -- then it might not be the best move for them."

Sellers have to submit hardship letters detailing their financial conditions and why their bank, or the holder of their mortgage, should give them a break. The bank then would approve or deny the deal.

"Everything is submitted and now everyone is sitting on their hands, anxiously waiting," said Anton G. Auth, senior mortgage development officer at Sovereign Bank in Brick. "It can be quick or it can take forever."

There can be further complications, such as a home equity loan, second mortgage or other liens on the property. Each one matters and each can cause delays.

"It necessitates the need to get permission from the debtors who have liens on the property," said Bob Levenson, broker sales representative at Weichert Realtors in Rumson.

In today's environment, mortgages may be owned by several investors, he added.

It creates a lot of paperwork for the bank, which must verify the seller's dire financial condition before it accepts a lower amount. "I'm not sure that they were prepared for the massive influx of the

numbers that we're seeing," La Cicero said.

"Initially when we first saw this influx of short sales, the banks were just flatly rejecting the offers and then you had to go back to square one," the lawyer said. "Now they are actually countering to speed the process."

For banks, the options are short sale or foreclosure. But the foreclosure process is typically more expensive and the bank is forced to take on the costs of owning and marketing a property as well as increased legal fees, La Cicero said. "They will take almost any reasonable offer in order to not have to do that."

But short sales can fail. A buyer's offer that is too low can sink a deal.

"Let's say the house is listed at \$250,000. They want to throw something to the bank at \$180,190," said agent Susan Geiger, a sales associate at Coldwell Banker in Holmdel. "The bank comes back and totally rejects it altogether. You can't offer too low."

New rules put into place by the U.S. Treasury Department hope to address the delays and other problems with the short-sales process, said Jeff Lischer, managing director for regulatory policy at the National Association of Realtors.

The regulations, which took effect on April 5, give \$3,000 to borrowers for relocation assistance and \$1,500 to mortgage servicers to cover costs. They

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also call for standard processes, uniform documents and deadlines. Borrowers would also receive pre-approved short-sale terms before listing the property, including the minimum acceptable net proceeds and closing costs.

But it will be months before it is known whether the changes are successful and how many are being helped, Lischer said.

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A foreclosed house is shown in East Palo Alto, Calif. Banks prefer short sales to foreclosures, because they're cheaper, but buying a short-sale home can be a lesson in endurance. (AP PHOTO)

Long on patience

Buying a house that is a short sale -- where the price is less than the owner's mortgage balance -- can take up to five months. New changes by the Treasury Department to the Home Affordable Foreclosure Alternatives Program, which took effect April 5 and runs to Dec. 31, 2012, are designed to grease the process.

The changes:

- Gives \$3,000 to help a distressed borrower relocate.
- Allows borrowers to receive pre-approved short sale terms before listing the property.
- Uses a standard process, uniform documents, timelines and deadlines.
- Provides \$1,500 to loan servicers, such as banks, to cover administrative and processing costs.

Source: National Association of Realtors

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