NATIONAL ASSOCIATION OF EXCLUSIVE BUYER AGENTS

A National Association of Exclusive Buyer Agents Home Buyer Report

Short Sales Are A Long Shot For America's Home Buyers!

51 Critical Things Buyers Need To Understand About Short Sales

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Short sales have become commonplace in the American housing market. Many real estate buyers do not understand all that goes into processing a short sale transaction. This report will describe many of the buying complications that home purchasers have had to go through to buy a short sale home.

Note that this report does not constitute legal advice. Consult a local real estate attorney for answers to specific legal questions.

Definition:

The term short sale is defined by the Nolo Legal Dictionary as "A sale of a house in which the proceeds fall short of what the owner still owes on the mortgage." This means that the lender must agree to take less than the amount that is owed on the mortgage to release their lien on the home. If the lender thinks they will lose less money by letting the home go into foreclosure or by pressuring the homeowner to continue to make payments, then they will not authorize a short sale.

The Seller's Preparation:

To better understand the short sale purchase process, it is helpful to review what a home seller typically does to prepare for a short sale. A seller will need to get the help of a title company and a real estate professional. Sometimes a short sale negotiator or attorney will also be involved. Lenders typically want to see the property listed with a realtor and typically will not approve a short sale without having a purchase offer in hand from a buyer. Also, a seller's lender often will not consider a short sale unless the seller has been delinquent on their mortgage payment.

A seller will need to write and gather the following additional documents to provide to the lender:

1. A history of the listing, including asking price changes and information on any other offers that have been received.
2. A current printout from the Multiple Listing System.
3. An appraisal, Competitive Market Analysis (CMA) or a Broker's Price Opinion (BPO).
4. A letter detailing the seller's hardship in making payments on the home.
5. A budget detailing the seller's income and expenses.
6. Two years of the seller's tax returns.
7. The most recent two months of the seller's bank statements.
8. The most recent two months of the seller's pay stubs.
9. A copy of the seller's listing contract with their real estate brokerage.
10. A release that allows the lender to discuss the transaction with the real estate professionals involved.
11. A history of their mortgage delinquency, including all correspondence they have had from the lender.

These items are often referred to as a “hardship package” and they need to be updated and transmitted to the seller’s lender once a purchase contract is in hand. These days most lenders have “short sale packages” already prepared to help homeowners get started.

Once these steps are taken the real challenge begins: that is waiting to see if the seller’s lender responds to the offer. Often a lender will feel very little motivation to even respond to a short sale proposal. Since some lenders get hundreds of short sale proposals each week, they often do not have the time to carefully consider any individual transaction.

On The Buying Side:

On the buying side, a short sale starts just like a regular home purchase. Often a home is advertised without disclosing that it is a short sale. This is like advertising a home that is not really for sale at all because, at this point in the vast majority of cases, the seller does not have the ability to sell the home at the advertised price.

At some point, a buyer sees the property. Once they find out it is a short sale they may decide they still are interested in it enough to want to make an offer. The negotiating process is a little different with a short sale in that the seller will not be taking any funds from the sale, so they may not care that much the amount of the short sale offer. It is really up to the lender to decide if they want to proceed with an offer.

In many cases, the lender does not respond in a timely manner, and if the buyer actually needs to move into a home on any kind of schedule, the buyer will withdraw their offer. Our members report that nationally about one in four short sale purchase agreements actually moves through to completion. Obviously that ratio will be different in each local market. A short sale usually saves the lender from the additional losses that come with a foreclosure. It also saves the seller from the extended financial entanglements of a foreclosure and it can provide a buyer with a nice home for a fair price.

When our Association decided to publish a report helpful to home buyers, our committee decided to identify the ten most critical factors that home buyers need to be informed about related to short sales. However, when we surveyed our members, we determined that there where many more than ten factors that buyers should know. This report is the result of that survey.

51 Critical Things Buyers Need to Understand about Short Sales:

1. Most short sale contracts do not close. The numbers are improving, but our members are still seeing that the majority of short sale purchase contracts do not get to closing. Our members estimate that about 50% of homes listed as short sales eventually sell as short sales. The balance usually ends up in foreclosure or loan renegotiation.
2. Short sales usually take a long time to close and the timing is unpredictable. Again, the numbers are improving, but it is still not uncommon for a short sale transaction to take five or six months to get from purchase contract to closing. This often includes transactions where the listing agent initially feels the transaction should close in two to three months.
3. There are many aspects to a short sale transaction that are completely out of a buyer’s control. Even if there are potential legal remedies to a seller’s default on purchase contract terms, the fact that they are in financial trouble can make it impractical to enforce purchase contract terms in court.

4. Many lenders will not discuss a short sale with a seller without a purchase contract from a buyer in place. This means buyers often spend time looking and negotiating on short sales without any confidence a home is actually going to be available at the asking price, or if it is going to be available to purchase at all.
5. Short sales are often listed at a ridiculously low price. Because lenders will not discuss a short sale with a seller until a contract is in place, many listing agents will list a home for a very low price to get a purchase contract. They do this knowing that the seller's lender is not likely to actually accept it, but at least it will get the process started. Listing agents who do this justify it because even though it may be wasting the time of dozens of different home buyers, it is potentially in the best interest of their client, the seller.
6. A seller will often agree to any offer, even an offer that has no chance of being accepted by their lender. Because they will not receive any proceeds from a sale, a seller will often agree to any offer, even if they know there is little chance their bank will approve it, just so they can begin negotiations with their lender.
7. Often buyers who think they are willing to wait for a lender to approve a short sale get tired and walk away from the transaction. Sometimes these listings later show up as a "Price Previously Approved" short sale in the local Multiple Listing System.
8. Even if a price has been approved previously by the seller's lender, there is still no guarantee it will not take months to close or that it will close at all. Having a previous approval does show a potential for a shorter transaction, but remember the seller's lender is not obligated to approve a new transaction at the same price and terms they approved for a previous transaction.
9. The seller may not be sufficiently motivated to do their own paperwork. Once a purchase agreement is obtained, the listing agent or short sale negotiator needs to transmit the contract along with an up-to-date hardship package to the seller's lender. Getting that hardship information requires the seller's participation and we have seen many situations where the seller delays the process at this point.
10. There are many additional risks involved in a short sale transaction. Along with losing time, buyers often lose appraisal fees, lender application fees, inspection fees and legal fees. There is often even additional risk with the earnest money deposit.
11. A foreclosure sale can take place at any time and kill the transaction, even after there is a short sale approval from the seller's lender. The vast majority of the time an approval from the seller's lender is not fully binding on the lender. Sometimes the approval is not even in writing. This is quite different from buying a home from a private owner. Usually things work out when a seller's lender approves a transaction, but short sale contract provisions also usually give that lender a path to back away from the transaction.
12. The seller's lender's rules can change during the process, killing the process or resetting the time-line. Since short sales take a long time, it is not uncommon for the lender's policies to change during the process. These changes have negatively impacted many short sale buyers.
13. Since the seller's lender is not the seller, they are not bound by the terms of the real estate purchase contract. Many buyers are not clear on this. The homeowner is not the final decision-maker, the seller's lender is, even though the lender usually has very little knowledge of the actual home or the local market.
14. During the negotiations, the seller and the seller's lender may come to terms on a loan modification. Often, if the seller can get a loan modification, they can stay in the home, so this side negotiation can totally derail a purchase transaction. Usualy neither the buyer nor the real estate agents have any knowledge of this negotiation going on until it is too late.
15. Sometimes when the seller's lender approves a purchase agreement, they do not provide adequate time to do inspections. An alternative approach is to do inspections before the lender

approves, but then you lose the money you spent on those inspections if the transaction is not approved.

16. Your Earnest Money Deposit may be at additional risk if the home goes into foreclosure. In many areas, a brokerage must have a seller's agreement to return a buyer's earnest money deposit. Home sellers are often frustrated to the point of being uncooperative in signing anything if they are losing their home to foreclosure, especially if they had previously had a short sale approved. Our members have had situations where a seller's lender approves a short sale then decides to foreclose and the sellers take out their frustrations on the buyer by not releasing claim to the earnest money deposit. The deposits usually end up being returned, but not without additional legal expense and frustration for the buyer.

17. The extended timing of short sales can often cause contract deadlines to expire at uncomfortable times during a transaction. Buyers should be extra vigilant in watching contract dates and contingency provisions, since these can bind the buyer to the transaction.

18. Unpaid Home Owner Association (HOA) fees can kill a transaction. Unpaid Home Owner's Association Dues, utility payments, back taxes etc. can all derail a short sale transaction. Normally, somebody has to pay them to clear the title. What can make it worse is that sometimes these costs cannot be calculated until just before closing.

19. Having a short sale negotiator does not guarantee success. A new industry has started with companies who claim to specialize in short sale negotiation. Unfortunately, these are often national companies who are not familiar with local real estate practices. Also, there is really no accreditation process for these companies so, without prior experience with one, it is difficult to know if they are even likely to help the process. Additionally, a short sale negotiation company still cannot guarantee a successful transaction.

20. Repairs may be required at the buyer's expense. If the home has major defects, safety issues, or has problems that violate the local building code, the buyer's lender may require such items to be repaired prior to closing. For obvious reasons, it is unlikely the seller or the seller's lender will pay for or make the improvements. In order to be able to close, a buyer may be tempted to complete the repairs. Again, the buyer's investment for such improvements is at risk if the deal does not go through.

21. The seller's lender normally will want two or three third-party opinions on a property's value, any one of which can upset a transaction. A valuation on the property can take the form of a formal appraisal or an informal broker price opinion (BPO). A valuation coming back to the seller's lender that is higher than your contract price can kill your transaction. Additionally, sometimes banks ask for new sets of valuations during the negotiation process. Since short sales often take such an extended time to close, the valuation is sometimes a moving target.

22. The seller's lender may not be aware of the condition of the home. A listing agent may not forward your documentation showing the poor condition of the property to the bank. Third-party opinions about the property's value are often not detailed enough to show the mold in the basement, or that the windows or roof need replacement. Many people who provide banks with BPOs are not experienced enough to adjust for such factors. Additionally, some of the valuations are just done as drive-by reviews, so they are sometimes quite inaccurate.

23. The seller's lender may choose to foreclose at a greater loss than a short sale. Because of favorable bank bail-out terms, sometimes a lender stands to make more money, even if they sell the home at a loss through foreclosure, because they will be reimbursed for a portion of their losses by taxpayers. This sometimes explains financial decisions a lender may make that seem to be totally illogical.

24. The seller may have more than one lender involved. There may be more than one lender that needs to approve the short sale. Piggy-back purchase loans were very popular during the days of rapidly rising values. These loans had a large first loan and a smaller second loan, often from

different lenders. The second mortgage lender stands to lose everything if the home moves to foreclosure, so they typically accept a smaller percentage of their original loan than the first mortgage lender, but they still need to agree with the amount.

25. There may also be mortgage insurance companies and investors who need to approve the short sale, in addition to the actual seller's lender. Each one of these entities can have an impact on the transaction.

26. You may never actually communicate to a person with authority to make a decision on the transaction. This is also true for the seller and the real estate agents. The actual decision makers at the seller's lender are usually totally isolated.

27. The listing brokerage's loyalties are sometimes confusing. In a short sale, the seller's lender has the authority to make decisions, but the listing brokerage has a legal obligation to represent the seller, not the seller's lender. This can lead to situations where the listing agent and seller will give preference to a lower price offer if the other terms of the offer seem to make it more likely to be acceptable to the seller's lender.

28. A listing agent is not required to submit all offers to the seller's lender. A listing agent is typically required by law to present an offer to the seller, but there is no legal requirement to present an offer to the seller's lender. A listing agent will typically only send a signed contract to the seller's lender, but once that is done, they may submit no other offers or, worse, offers so that the first contract seems good to the lender, or sometimes all other offers.

29. If later offers are stronger than the first buyer's offer, the seller's lender my reject or renegotiate the previous agreement. Usually, once a decision has been made by the seller's lender, they will stick with it. However, since the short sale documents often do not obligate the lender to complete your transaction, they sometimes will change direction, especially if they feel they can recoup more of their loan through a different buyer.

30. An incompetent, unprofessional or untrained listing agent can make the transaction impossible. Because of the large percentage of short sale transactions and the high turnover rate in the real estate business, it is not uncommon to be involved with a listing agent's first or second short sale transaction. Buyers obviously can not choose the listing agent, but if things seem to be getting off track, your agent can contact the listing broker to try to keep things rolling.

31. The seller may just be listing the home as a short sale to try to delay a lender's inevitable foreclosure. Sometimes a home will be listed, but the seller makes it very difficult to actually show the home. This may be because the seller is not really motivated to sell, but is convinced that by listing it as a short sale, their lender will postpone the foreclosure proceedings. This can be an incredible waste of a buyer's time. We have witnessed numerous situations where a showing is scheduled and, when the buyers and their agent arrive, the seller is actually inside the home, but will not come to the door to let the buyers and their agent into the home. This seems to be more common now than it has been in the past.

32. The seller may get started with a short sale transaction but lose motivation and refuse to complete it. The seller's emotional state can have a significant impact on the process. There sometimes is little benefit to them for selling, since they will not receive any funds from the sale and their credit is usually already damaged.

33. The seller's lender may require ridiculous terms in their short sale addendum. Some lenders are adding absurd requirements to their short sale forms. These have included provisions to make the real estate agents and brokerages parties to the contract, changing the terms of both the purchase agreement and the brokers' agreements, imposing duties on brokers that are in conflict with each broker's duty to their own client, and even requiring brokers to make representations and/or agree to things over which they have no knowledge or control. In some cases these addenda may even violate state license law.

34. The seller's lender may have multiple decision makers and negotiators involved over the course

of the transaction. Because of the extended timeframe of short sales and the difficulty of processing a large number of transactions, the short sale department of the seller's lender may be inconsistent in their decision making.

35. The seller's lender may be very slow to respond to inquiries and contract modifications. As an example, a lender approved a short sale subject to a $10,000 price increase based on their appraisal. The purchasers were willing to move forward with the transaction if they could see the appraisal. The lender took three weeks to respond to the simple request.
36. The seller's lenders often lose documents that they have been supplied to them. Keeping track of documents and resending documents is crucial to the success of the transaction. Our members have been involved in purchases where the seller's lender has lost documents as many as four different times in one transaction.
37. Cooperation from the closing authority is also critical. The closing authority (a title company in most states) is often called on to prepare draft closing statements early in the transaction so the seller's lender can get a clear understanding of how much money they will be losing if they approve a short sale. If the seller chooses a slow or unresponsive closing authority, the transaction can be needlessly delayed.
38. The costs to close often change while you wait for the seller's lender's response. A draft closing statement supplied to the seller's lender may be accurate when it is prepared and presented to the seller's lender, but by the time someone at the lender makes a decision on the transaction, the numbers might have changed dramatically, typically because the homeowner is not making mortgage payments. When this new number gets back to the seller's lender, they may decide not to move forward. This gets particularly complicated when there is a second mortgage, because now there are two different moving targets.
39. A seller may be trying to have a friend or relative buy the home for them at a short sale price. Sometimes a homeowner who owes more on a home than it is worth will try to cheat the lender by having a friend or relative repurchase the home under a different name at the current market value. This is mortgage fraud and an outside buyer could waste a lot of time on a transaction that will never close.
40. A seller may ask you to pay them money outside of closing. This again is typically mortgage fraud. The seller's bank is losing a lot of money on a short sale. They feel it is not fair for the seller to make anything on the transaction.
41. The seller's lender may want to renegotiate the commission being offered in the listing to the real estate brokerages. This is illogical considering short sales are typically a lot more work than regular real estate transactions, but it is worth the effort to discuss this possibility with buyer's agents beforehand when considering the purchase of a short sale.
42. A property may not be a short sale when it is listed, but may turn into one by the time it sells. This is potentially one of the most frustrating aspects of short sales. A seller and listing agent may calculate that a seller has enough equity and assets to pay off a mortgage when a home comes on the market, but by the time an acceptable purchase contract is actually negotiated, the seller may not have the funds to pay off their lender. Thus, a conventional private-party transaction becomes a complicated and time-consuming short sale.
43. The seller's lender may not be willing to pay any of a buyer's closing costs. This is typically a concern with Veterans Administration loans and, fortunately, is becoming less of a problem, but there have been times when a buyer's lender requires some closing costs be covered by the seller. In a short sale, the seller does not have any money so this obligation flows to the seller's lender. Sometimes the seller's lender will have policies that do not allow payment of any closing costs for the buyer. The result is often tremendous frustration for qualified military veteran home buyers.
44. The seller may reach an agreement with their lender and then change their mind when the final

numbers become clear. If the seller has an additional financial setback during the short sale process, they may back out of the transaction or want to renegotiate. One of our members had this happen on a short sale purchase recently and, when the seller started to back out of the transaction, the second mortgage lender agreed to take a smaller payoff so the seller again became comfortable and completed the transaction. Unfortunately, this delayed the transaction by about two additional weeks.

45. If the sellers are going through other major life changes during a short sale, things can get even worse. Sometimes a seller will declare bankruptcy or file for divorce during a short sale process. We have even run into situations where a seller has passed away and the seller's estate is trying to negotiate a short sale with the lender on the home. Generally, these situations make the process even more difficult and time-consuming.
46. Negotiating personal property is often impossible. Personal property like refrigerators, stoves, washers, dryers and lawn equipment are often included in normal home purchase negotiations. However, with short sales, since the personal property is not part of the transaction with the bank, most home sellers will not include it in a purchase contract. They may as well give it away. Home sellers will normally want to take the personal property with them to their next home, or sell it locally so they receive some value for the items. So if you are buying a home and you need appliances, it is often impossible to get them included with the home in a short sale.
47. Short sale homes often have significant deferred maintenance. If a seller has the kind of financial hardship that will convince their lender to agree to a short sale, they often do not have the funds to do necessary maintenance on a home. It is critical for buyers to look critically at the home with an experienced buyer agent before starting negotiation and to have a competent and thorough home inspection once there is a purchase agreement in place.
48. You have less protection with respect to a home's condition at the pre-closing walk-through. Since the home seller is not receiving any financial benefit from closing on the home, they are often less motivated to actually clean the home and leave it in proper condition at closing.
49. The seller's lender may not allow a utility escrow. Often, for a property on city water and sewer service, there is a chance that the final water bill is not paid to the date of closing. It is common for the listing office or closing authority to escrow or hold on to a few hundred dollars of the seller's money to make sure the final water bill is paid. The seller's lender in a short sale may not allow that at closing, so the buyer has additional risk if the bill can not be paid at closing.
50. The seller's lender may have a specific allowable contribution to closing cost made based on an earlier estimate. Normally the exact closing costs can not be calculated until a few days before closing. Often, short sale lenders will put limits on their costs based on approximations made months earlier. Sometimes it comes down to the buyer making up for the difference or not being able to close on the home after waiting for months.
51. A deficiency judgment could complicate the seller's position. Some states allow a seller's lender to come after the seller after closing a short sale for the amount still owed the lender. The chance of this happening or the last minute refusal of the seller's lender to promise not to come after the seller for the deficiency has sometimes derailed an almost complete short sale transaction.

Strategies to Survive and Benefit from Short Sales:

1. Think seriously before you consider looking at short sale homes. If you have a short timeframe for buying or you need a predictable purchase process, short sales are probably not for you.
2. Work with a competent and loyal agent on the buying end. This can make a huge difference

if you decide to consider purchasing a short sale. You need someone who will be honest and help you objectively evaluate the risk vs. the potential reward of purchasing a short sale. A short sale home may not be worth waiting two to six months for just to save a few percent off market value. When considering agents, an Exclusive Buyer's Agent is usually the best choice, if one is available.

3. Consider contract provisions that will allow you to escape the transaction if the seller's lender is too slow or unresponsive.
4. Limit your earnest money deposit and/or have contract terms that require the release of the deposit back to you without the seller's approval if the home goes into foreclosure.
5. Have your contract contingency timing start when the seller's lender approves of the transaction.
6. Take the time to thoroughly look at the home before you start negotiating on a short sale.

Again, note that this report does not constitute legal advice. Consult an independent local real estate attorney for answers to specific legal questions. Additionally, some lenders are making efforts to improve and streamline the short sale process and the federal government is considering new laws to force banks to speed their processes. Talk to local home buying experts to learn the current processes in your area.

If you are considering buying a home and are interested in expert advice and counsel, there are Exclusive Buyer's Agents in virtually all major markets, including Hawaii, Mexico and the Virgin Islands. To find an Exclusive Buyer's Agent to speak to about your home buying needs, visit naeba.org or call 800-986-2322.

We hope this brief report will help to make your home buying process more pleasant and profitable.

Good luck with your efforts!

Jon Boyd & Ben Clark
Past Presidents of The National Association of Exclusive Buyer Agents (naeba.org)

The National Association of Exclusive Buyer Agents was founded in 1995 to help consumers become educated home buyers. NAEBA is a nonprofit organization whose purpose is to be the "champions of real estate buyers' rights and representation." NAEBA has over 500 members worldwide. Starting in the mid-1990s, savvy buyers wanted the benefits of a real estate representative working for their interests exclusively. They turned to EBAs, Exclusive Buyer Agents, to do the job. NAEBA is an industry group dedicated to supporting EBAs in serving clients to the best of their ability. NAEBA offers industry standard certifications, ongoing education, client referral service, technology and information sharing. The NAEBA Code of Ethics pledges undivided loyalty to real estate buyers only. More information about NAEBA can be found at naeba.org.