

THE SHORT SALE PROCESS

Overview

In the past, it was rare that a lender would accept a short sale. However, in recent years, due to the overwhelming market changes, lenders have become much more negotiable when it comes to these transactions. Furthermore, recent policy changes within many organizations and within the Federal government have made the chances of getting a short sale approved even higher.

A homeowner is “short” when they owe an amount on their property that, when combined with closing costs and commissions, is higher than the current market value. In a loan default situation (pre-foreclosure) a short sale occurs when a negotiation is entered into with the homeowner’s mortgage lender(s) to allow the property to be sold for less than the loan amount and/or accept less than (or “short”) the amount owed as payment in full. This sounds easy enough; however, this is an involved process that takes a lot of time and patience on the part of the homeowner, and good communications skills, professionalism and organization on the part of the real estate agent. As a Certified Distressed Property Expert® (CDPE), I am trained in assessing all foreclosure alternatives and pursuing the best solution for your own financial situation.

Expectations of the Homeowner/Borrower

A trained real estate agent can negotiate a short sale with a homeowner’s mortgage lender(s) if they meet the following three qualifications:

1. They must show that they have a valid hardship, such as divorce or death of a spouse, involuntary job loss, sudden loss of income, involuntary transfer of job, large unexpected expenses, business failure, illness, or natural disaster.
2. They must show that their monthly expenses are greater than their monthly income.
3. They must prove that their debts are greater than the value of their assets

A short sale has become a common occurrence in today’s market and requires the written approval of your existing mortgage lender(s). The homeowner should be aware that the lender is not required to participate in a short sale and there is no time limit for the lender’s approval or response. Each lender is different and has different requirements. As a Certified Distressed Property Expert® (CDPE), I have an understanding of the complex issues confronting the real estate industry, and the foreclosure avoidance options available to homeowners. Through comprehensive training and experience I can help you navigate through the unknowns and provide solutions for you in today’s market, specifically short sales.

The homeowner should be prepared to gather and organize their personal information, preferably ahead of time. Although each lender’s requirements differ slightly, this information normally includes the following:

1. Two years W-2’s or 1099’s
2. Two years Federal income tax returns
3. 90 days complete bank statements (all pages)
4. Last 30 days pay stubs
5. Hardship (SAD) letter, explaining the events that led to their current situation).
6. Financial statements depicting their current income and expenses
7. Personal P &L statement of their personal assets and liabilities.
- 8) Current Business P&L statement if they own a business.

The homeowner should make sure they provide every little bit of information required by the lender(s). When they omit something, either intentionally or unintentionally, it will, at the very least, delay the process.

The Assigned Agent's Preparation

The assigned agent presents a short-sale information package that explains the details of the short sale and structures an agreement in the event that the short sale is feasible. Included in this package is their own "BPO" or Comparable Market Analysis, cover letter, trends in the home's zip code, copy of the MLS, showing activity, and other related documents the lender might require. The agent contacts and works through the "Loss Mitigation Department" or other similar department name, and must demonstrate benefits to the lender of approving the short sale. These can include fewer legal costs, probably greater recovery of the loan amount, fewer non-performing loans, fewer repairs likely, and less negative impact on the neighborhood.

Lender and Investor Approval

Once the lender receives and reviews the Short Sale Package from the assigned agent, the lender orders a Broker Price Opinion (BPO) from a third party agent. If there is not a major difference between the assigned agent's BPO and the other agent's BPO, the lender will then review the closing costs and fees, going items by items through the HUD-1 Settlement Statement to make sure that the costs they are absorbing are acceptable.

If there is a subordinate or junior lien holder (2nd and/or 3rd loan), the primary lender will determine the amount of a symbolic sum to be distributed to this lien holder. It's almost always less than ten (10%) percent of the loan balance of the subordinate loan. It can be especially difficult to obtain a short-sale approval from a subordinate lien holder, and in some cases the short-sale falls through.

The package is then reviewed for approval by the investor. Most loans are owned by investors who have reserved the right to approve or disapprove the transaction, and the investor may want more than the lender has approved. There still may be one more player who could still pull the transaction out of the process. This would be the private mortgage insurance (PMI) company who still can insist on remuneration the form of cash or a promissory note from the borrower. This is not allowable under the Home Affordable Foreclosure Alternative (HAFA) program initiated by the Federal government.

If the investor approves the package, the lender forwards an approval letter to the seller, spelling out the terms and conditions that must be met for approval. After reviewing the lender's approval letter, the seller and the buyer must decide if they want to meet the terms and conditions and mutually proceed with the transaction. If the response is a positive one, the timelines set forth in the contract begin immediately, and the escrow process moves to close of escrow.

Even if a lender agrees to a short sale, the lender may not agree to forgive the debt entirely, particularly if it's not owner-occupied (investment property), and may require the seller to pay the difference as a personal obligation. Many lenders ask sellers to sign a promissory note for all or part of the difference between the process of the short sale and the debt obligation as a condition to a short sale.

Credit and Tax Consequences

A short sale could affect the seller's credit score, and may appear on the credit report as "Pre-foreclosure redemption", paid in full for less than full balance", or other similar term. The FICO score can be affected 80 to 100 points by a short sale, but up to 300 points by a foreclosure. Past-due payments prior to a short sale can often have a more negative impact on the seller's credit score than the short sale itself.

A short sale in which the debt is forgiven is a relief of debt, and may be treated as income for tax purposes. The Mortgage Forgiveness Debt Relief Act of 2007 created a three-year window for homeowners to pay no taxes on any debt forgiveness they receive; however, only cancelled debt used to buy, build or improve a principal residence, or refinance debt incurred for those purposes qualifies for this tax exemption under the Act. The IRS requires lenders to submit a FORM 1099C, stating the forgiven amount.