



HAWAI'I LIFE
REAL ESTATE BROKERS

Foreclosure Facts & Opportunities ToolKit

Short Sale vs. Foreclosure - Top Ten Things to Know

Recently the national news has been filled with frequent reports about the housing market and the high percentage (between 30-40%) of the transactions that are coming from the distressed housing market. Distressed home sales refers to bank owned properties, aka REOs and short sales, where the property is being sold for less than the current owners owe to the lienholders or banks.

While both types of transactions are referred to as “distressed” let me highlight the top ten differences between an REO and a short sale. Remember, an REO is a property that is owned by the bank. REO stands for Real Estate Owned. A short sale is owned by the owner who is having to sell the home for less than the bank is owed. The short sale may be in the pre-foreclosure or foreclosure process but it is NOT OWNED BY THE BANK. You and your agent will need to be the judge as to which of these points have the most importance and value for you:

1. DISCLOSURE

When you see an REO listing in our MLS, it will be accompanied by the language AS-IS. There is no seller’s disclosure provided. It is incumbent upon the buyer and their agent to perform their own due diligence. In a Short Sale, most of the time there is a cooperative seller (not always) who will provide a true SRPDS (Seller’s Real Property Disclosure Statement) and share what the seller knows to be true about the property.

2. PROPERTY CONDITION

While this varies from property to property, in an REO the owner or their tenants have vacated the property or been evicted. Many times damage is done to the property during this transition or items are removed from the property. In a short sale the property can often be in very good condition but sometimes the homes are neglected as the short sale has either lost interest in maintaining the property or is venting their frustration at the bank by neglecting the property. In some REO properties if the damage is severe enough, the bank will approve some initial repairs to the property to get the home in more “sellable condition”.

3. RESPONSE TIME to AN OFFER

Most agents will tell you that the response time in purchasing an REO is quick and usually it is. Most banks or asset managers have the offers submitted in an online system and the decision maker usually responds within 48 to 72 hours. In a short sale, a buyer can wait one or many many months to get any response from the seller and seller’s agent. There are a multitude of reason’s for this but suffice it to say, REOs can be short in timeframe, short sales are usually not SHORT in time. However, when a short sale has matured, and the lienholder has determined the value, the response time in a short sale can be very rapid.



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4. MORTGAGE OR CASH?

There's an old saying, "Cash is King". I bet you've heard it before right. When it comes to buying an REO, it is true most of the time. I've had situations where my buyer had the highest offer, but the asset manager for the REO chose an offer more than 10% lower that was all cash. This is not always true when it comes to purchasing Fannie Mae or Freddie Mac REOs, but for the non GSE loans it is almost always true. Conversely, in a short sale, the agent generally submits only one offer at a time, and the loss mitigation department of the bank does not usually discriminate as to whether the offer is cash or mortgage. The lienholder simply wants assurances that the buyer is qualified, can prove they are qualified, and can indeed perform according to the contract and complete the purchase.

5. FINANCING INCENTIVES

When you see a Fannie Mae REO listed, you are likely to see language like Owner occupant offers will be reviewed by seller after 3 days on market. Investor Offers will be reviewed by seller after 15 DOM, as Fannie Mae First Look offers priority to owner occupant buyers during the first 15 DOM. This is a Fannie Mae HomePath property. Purchase this property for as little as 3% down! This property is approved for HomePath Mortgage Financing. These are incentives for owner occupants and loan incentives to make the Fannie Mae properties more attractive and more buyable. You will not currently find these options and incentives when purchasing a short sale. If you and your family decide that you want that Homepath loan with 3% down and where the bank may also pay up to 3.5% closing costs, you want a Fannie Mae REO.

6. ADDITIONAL CONTRACTUAL OBLIGATIONS

When you purchase an REO, once the bank accepts your price, the buyer will receive many contractual addenda from the selling bank stipulating the terms and conditions of the sale. Make sure you, your agent, and your attorney if you have one, read these so you understand the ramifications of the contracts you are entering into. In a short sale, the main document lenders provide that is significant is the "Arms Length Transaction Addendum" that states, usually under oath of Notary, that the parties to the transaction are not related. The ALTA also states that there is no relationship verbal, written or implied that the seller's are able to purchase or lease back said property.



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7. HIGHEST AND BEST

When a bank and their real estate agent list an REO, the price may sometimes be so aggressive(cheap) that the agent will receive multiple cash offers within the first 48 hours of releasing the listing. Often times in this scenario the buyer's agent and their buyers will receive a Highest and Best document. This document discloses that the bank has multiple offers and asking the buyer to provide their "highest and best" offer. As with most things real estate, it is wise to be unemotional about these very complicated and costly transactions. Don't say, "Ahh, I don't want to get involved in a bidding war!". Simply know that the bank, who is usually losing their shirt on the property, is seeking to get the highest market value on the property. Decide what that is for you and make that your highest and best offer, even if that means staying put on the same number you originally submitted. In a short sale, it is rare to receive a highest and best proposal, but it does occur from time to time.

8. PROPERTY ACCESS and INSPECTIONS

Access to an REO is usually quite easy. The home is generally vacant. In a short sale, the owner or their tenants may occupy the property and access can be more difficult or require more advanced scheduling and planning. When it comes time to performing inspections, the utilities will hopefully be on in either type of sale, but sometimes in an REO the utilities will be off and the buyer will need to arrange to get them turned on for their inspections.

9. TITLE AND ESCROW ISSUES

This can be complex because the fine legal science of property deeding and chain of titles is left to the experts and attorneys of escrow companies for the most part in the state of Hawaii. In an REO, some banks will list the property before having clear title. According to a class I took with Suzanne Nasser of Title Guaranty, often times the reassigning and securitizing of loans that was done extensively in 2004 thru 2007 resulted in many breaks in the chain of title. This can lead to a delay in the closing of an REO property. With a short sale, the property is generally still owned by the seller who is selling short. There can still be technical issues with trusts, or other liens on the property, like tax and IRS liens, that must be removed in order to sell the property. Rarely though are the break in the chain of title in a short sale.



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10. GETTING THE MOST BANG FOR YOUR BUCK

This is a tough one. Statistically, banks net 15-20% more on their defaulting borrowers property in a short sale than in an REO. Does that mean the REO's sell for 15% less? No, not at all. There are significant costs in legal fees, eviction fees, repair fees, and revenue loss for the bank in an REO. The home is often vacant for a long time even before listing. Additionally, many REO properties being sold AS-IS are in worse condition and require a lot more money invested by the buyer. Finally, the proof is in the pudding, or in the negotiation. A realtor is often involved in both REO and Short Sales to persuade the bank as to what the fair market value is. If you are buying a short sale and listing agent has an experienced team of agents and attorneys playing hardball with the banks, you may get the short sale at a comparable price to an REO, but without the added expenses of repairs after you close on the sale.

So there you have it. These are statistically where most of the great real estate deals are in our nation and in the Hawaiian islands. Whatever path you chose, make sure you work with an agent who understands each transaction type and who properly sets your expectations so you can be successful and not disappointed.