

Short Sale Activity Climbs During Last Year and Helps Avoid Foreclosures

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from the Atlanta Journal-Constitution HomeFinder

Last week we talked about the need for lenders in the Atlanta area to help stem the tide of vacant "bank-owned" homes in our neighborhoods. One step that lenders are taking more often is to accept a "short sale," or a discounted payoff on the sale of the house before it goes into the foreclosure process.

This week, we will answer some questions that are commonly asked when the subject of short sales is raised.

Q: How is a short sale different from a traditional foreclosure?

A: In a typical Georgia foreclosure, the lender notifies the borrower that payments on the loan are past due. The borrower is given a reasonable period of time to catch up or pay off the debt. Eventually, the lender forces the sale of the home at a public foreclosure auction. If no one else bids, the lender ends up owning the house. The bank will then try to sell the house for whatever it can get, often taking a significant loss in the overall transaction.

In a typical short sale, the borrower tries to sell the house before the foreclosure auction, and finds a buyer willing to offer a sum of cash to purchase the house "as is." Often, this offer is well below the amount owed to the lender, but may be accepted in order to avoid the likelihood of bank ownership of a vacant house. In many cases, the bank loses less by accepting a "short sale" than they would if they foreclosed and tried to sell in a tough market.

Q: So, what is the advantage of a short sale over a foreclosure?

A: In a traditional foreclosure, the bank is almost certain to end up owning a vacant house in poor condition. Then they will try to sell it in a depressed market. Because most lenders have a policy of making no repairs or improvements, the house deteriorates over time. The vacant house attracts crime and drugs, and serves as a deterrent to anyone who may be thinking about buying a home in that area.

In contrast, a short sale allows ownership of the house to be transferred directly from the original borrower to an investor who understands what it takes to get the house fixed up and rented. Investors know that time is money, and uniformly endeavor to complete their repairs quickly.

The short sale is advantageous because it 1) puts the house back into reasonable condition quickly so that it never hurts the community, and 2) avoids the typical 6 to 12 month period of vacancy and decline that these houses experience before they are sold.

Q: How many short sales are there when compared to foreclosures?

A: A recent study from the Comptroller of the Currency showed that lenders completed three times the number of short sales during the fourth quarter of 2008 as they did on the first quarter of that year. Even so, lenders completed six foreclosures for every short sale completed during the last quarter of 2008.

Q: Why don't lenders encourage more short sales?

A: Because they are unfamiliar with the benefits of selling now as opposed to selling later. In some cases, lenders genuinely hope to come out better by selling later, although typically that is not the case. In other situations, the lenders believe that the investors are driving too hard a bargain.

Q: Why is this topic important now in Atlanta?

A: Because there were over ten thousand homes advertised as going into foreclosure in the 13 county metro area for the month of April. This is a new record high, according to the experts at EquityDepot.net.

Unfortunately, the vast majority of these homes have no apparent equity, and most will likely end up as "toxic assets" sitting on the market and pulling down prices in the neighborhoods where they are located. The longer they sit empty, the sadder they look. In my opinion, these homes are preventing the beginning of a real estate recovery in the Atlanta area.

Q: Does the Housing Stabilization Initiative address the issue of foreclosures?

A: Yes, it seeks to prevent more foreclosures by encouraging lenders to refinance creditworthy borrowers and to modify loans of borrowers who are already in trouble. The goal is to keep borrowers in their homes if at all possible.

Q: Are short sales being encouraged by lenders as a way of avoiding foreclosures?

A: Lenders are slowly beginning to realize that they are often financially better off recovering a percentage of their original loan now rather than waiting a year or more to get that same percentage or even less.

Q: If these vacant homes become eyesores so quickly, why can't the lender do a better job of managing them?

A: In the real estate business, there is an old adage: Nothing good ever happens to an empty house. Lenders have never before experienced the need for large numbers of professional property managers, and often try to convince the real estate agents that they should maintain the houses.

Incidentally, code enforcement departments around the metro area are becoming less forgiving when neighbors complain about an abandoned house and find that the institutional owner has neglected it. I recently met a listing agent who was fined and held in contempt when her lender client failed to mow the lawn when needed.

Q: What can we do if there is a vacant "bank-owned" home in our neighborhood?

A: Establish ongoing contact between your neighborhood association and the lender's "property disposition" office. Insist that the house be maintained to community standards regardless of lender policy, and be prepared to work with local code officials to require ongoing maintenance until the house sells.

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