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Short sales: boon or burden?

Way to avoid foreclosure seen as last resort

by Nick Gosling

In real estate, a short sale occurs when the homeowner sells a property for less than the mortgage — and the lender agrees to forgive the difference.

Often, offering one's property as a short sale is a back-against-the-wall alternative to foreclosure, local real estate professionals say.

The upside to short sales is easy to see: foreclosure avoidance.

But the downsides are less obvious. Short sales can be hurtful to one's credit score, take a long time to transact and are somewhat unpredictable, Geraldine Asmus, a Realtor with Coldwell Banker in Palo Alto, said.

Eric Trailer, a partner with Absolute Mortgage Banking in Palo Alto, offers an example of a short sale when a buyer puts \$100,000 down on a \$500,000 piece of property, making up the difference through loans. Two years later, the buyer has to sell the property for \$350,000 because of financial hardships and the remaining \$50,000 has to come out of somebody's pocket: the bank's.

Of course there are repercussions to the homeowner as well.

"The negative impact to the homeowner is pretty severe if they are basically asking the bank to forgive debt," Trailer said. "A short sale, where debt is forgiven, has the same impact (on one's credit rating as) being 120 days late on a mortgage payment to the borrower."

The severe impact on a homeowner's credit score could mean he won't be eligible for a mortgage again in a few years, if not longer. In the case of a foreclosure, the homeowner would have to wait at least five years before he is eligible for a loan again.

"The biggest difference between a short sale and a foreclosure is in a short sale, the bank never takes ownership of the property," Trailer said. "(With a short sale) the bank only takes the property in a distress case, trying to sell it. There's less of a negative impact to the bank and the independent owner to settle on a short sale situation versus a foreclosure."

Trailer suggests pursuing a short sale or foreclosure only as a last resort.

"My advice to any client would be if there is a way to settle the debt that is short without having the bank absorb it, then that's usually best for the homeowner, mainly because it doesn't have a negative impact on their credit report," he added. "If the property is not the primary residence of the owner, that \$50,000 that's forgiven by the bank is also potentially taxable."

Trailer says he believes that short sale and foreclosure transactions are actually on the decline.

"The reason for that is because if you take a look at the pending home sales in debt and you take a look at the overall pool of buyers entering the market, it appears the demand (for property) is increasing every week," he said. "Certainly I see more short sales in the Bay Area but I think the trend is going from flat to declining. It seems like the median home prices are beginning to level and the demand for the property seems quite strong, which would push values in the other direction."

The recent launch of a new short-sale program in the Bay Area by Coldwell Banker is just one sign that Realtors believe short sales are on the rise. Geraldine Asmus is a graduate of the "Short Sale Trusted Advisor" program, designed to streamline the short-sale process of selling distressed homes and the first program of its kind developed by a residential brokerage firm in California.

Asmus defines a real estate short sale as "a transaction where nothing is certain but uncertainty."

A "short sale actually means 'the seller is short of money,'" she said in an e-mail. "However, the investor, bank or lender will tell you that the seller is still responsible for monthly mortgage payments, taxes and/or HOA fees, etc."

The owner institutes the short sale, she added, by first hiring a real estate agent to sell his or her home, then writing a letter to the bank stating that he or she is going into short sale status and then giving permission to the real estate agent to list the home for sale and negotiate any offers.

The risks of buying a short-sale property typically include a long waiting period to receive a decision and often a large number of buyers who are interested in the property.

"As usual, there can only be one winner," Asmus said. "At the end of six months, the buyer still has no home and starts all over again.

"In purchasing a home it's like anything in life: 'Pay me now or pay me later.' Everything has a price attached," she added.

As a result of the housing collapse more short sales are likely to be seen in the San Francisco Bay Area next year, Asmus said, though not as much in the Menlo Park, Mountain View and Palo Alto areas.

"(Those areas) are the home of Stanford and the dot-coms and the transfer of wealth is extremely high, which translates into staying power," she said.

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