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## The short-sale buying guide for today's housing market



Here's a 10-step primer on short sales and the steps you will need to take to purchase one.

By Bobbi Dempsey of [Bankrate.com](http://Bankrate.com)

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Foreclosure is a fairly well-understood process, but as "short sale" signs sprout like weeds, you may wonder what they are all about.

When a lender agrees to accept a mortgage payoff amount that is less than what is owed in order to facilitate a sale of the property by a financially distressed owner, it's called a short sale. The lender forgives the remaining balance of the loan.

### Everyone loses — or wins

Short sales are a mixed bag for the buyer, the seller and the lender.

If you're a seller, a short sale is likely to damage your credit — but not as badly as a foreclosure. You'll also walk away from your home without a penny from the deal, making it difficult for you to find another place to live.

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The buyer gets the property at a reduced price, but the property in all likelihood has its share of problems — think fixer-upper — and will need to go through considerable red tape in order to make the deal happen.

The lender takes a financial loss, but perhaps not as large a loss as it might if it forecloses on the property.

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### What's your home worth?

Before you even start considering getting involved in a short sale, there are two situations in which an attempt at a short sale is almost certain to fail:

- No default on loan — Lenders almost never will accept short-sale offers or requests for short sales until the borrower is far behind in payments and a notice of default has been issued.
- Bankruptcy — If the seller has filed for bankruptcy, forget it. Few, if any, lenders will consider a short sale when the seller has filed for bankruptcy because negotiating a short sale is considered a collection activity and collection activities are prohibited in bankruptcies.

### Can it work for you?

Buying a home in a short sale can be a hassle, so why should you consider it? It boils down to the bottom line. You will get the property for a substantial discount. Since the lender is eager to continue to get paid the money it loaned out, it may also offer favorable financing terms.

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Since the sellers play an active role in the short-sale process, you will have their cooperation (and most likely won't need to evict them upon taking possession of the home). This is not always the case with a property that has gone through foreclosure.

Whether you've become aware of the distressed situation on a property through an agent, a "for sale by owner" ad or word-of-mouth, this is not a do-it-yourself project. A short sale is one real-estate deal where you really need to get help from an experienced agent or attorney. Not all real-estate agents know how to handle a short sale, so make sure you consult with one who can demonstrate special training or a good track record with short sales.

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### **Why lenders (might) agree**

It might seem counterintuitive for a lender to go along with a short sale. After all, a lender is legally entitled to pursue the full balance of the loan. When a homeowner falls behind on payments, the lender can (and often does) hold the borrower responsible for every penny owed.

And yet more and more lenders are willing to consider approving a short sale.

Lenders are painfully aware of just how bad the current foreclosure crisis is. They know the cold reality is that a large number of struggling borrowers will end up losing their homes, and so they often see the advisability in accepting the inevitable and trying to minimize their losses. Yet some lenders seem to remain in denial.

Foreclosure is an expensive and time-consuming process for a lender. By agreeing to a short sale, the lender wraps up this little mess quickly, and perhaps with less of a loss than it would have incurred with a foreclosure.

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Remember, after foreclosing, the lender owns the home and has to maintain it, insure it and pay taxes on it. So instead of receiving payments each month, the lender is now forking out money every month. Plus, short sales help the lender look good on paper — the property never gets listed as an actual foreclosure, which helps the lender's numbers. Lenders see it as the lesser of two evils — if the numbers make sense for them.

Here are the 10 steps to buying a short sale:

#### **1. Identify potential short sales**

Locate pre-foreclosures in your area. You can use an online database, search courthouse listings and legal ads or use an experienced real-estate agent as a buyer's agent. First, try to determine how much is owed on the house in relation to its approximate value. If it seems high, it's a good candidate because it indicates the seller might have trouble selling it for enough to satisfy the loan. Pass on those in which the owner has a lot of equity in the home — the lender likely will prefer to foreclose and resell closer to the market price.

#### **2. View the property**

Gauge its condition and estimate of how much it's going to take to repair or renovate. If it needs work, many "normal" buyers won't consider it, which is good for you.

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#### **3. Do your research**

What is the property worth? What's the profit potential? If you're an investor or even a homeowner planning to live in the home a short time, you'll want to profit from the deal.

#### **4. Find all liens and mortgages**

Ask the seller or his agent what liens are on the property, and which lender is the primary lien holder.

### 5. Figure out the financing

This is critical. You have to know how you're going to pay for the property. If you're a good credit risk, the existing lender may be willing to give you a loan. Since it already has a lot of your information in the short-sale paperwork, it may be able to expedite the loan application process. It's important to understand that in a short sale, you have to be able to move quickly. Once an agreement is worked out, it is common for the lender to require closing in as few as 20 days. This is too late to start shopping for a mortgage.

### 6. Contact the lender

You or your agent should speak with the loss mitigation department — or perhaps the resource recovery department — rather than the collection or customer service department, which is only interested in recouping past-due loan payments. Finding the decision-maker can be one of the biggest initial challenges. You will first need to have the homeowner complete and sign (notarization is usually required) an authorization letter, which gives the lender permission to discuss the mortgage situation with you.

**On our blog, 'Listed': [Zillow: No housing bottom before 2013](#)**

### 7. Complete the lender's short-sale application, if it has one

Many lenders have an application specifically for a short-sale request.

### 8. Assemble the proposal

The proposal generally consists of a package of materials including the application and authorization letter, plus:

**The purchase and sale contract**, signed by you and the seller, to buy the property for a specified price. The lender is not going to entertain tentative offers. You're not going to get the chance to ask the bank, "Would you take X number of dollars?" In most cases, this also means posting a sizable amount of money to demonstrate your desire and ability to go through with the transaction if it is accepted. If you can't make a sizable down payment, the lender would have no reason to believe you can do any better than the last owner. It's also very important to the buyer that the contract be contingent upon all lenders approving the short sale in writing.

**A hardship letter.** It's important to remember a lender will not even discuss a short sale until the homeowner has fallen behind on payments — usually 90 days. The lender must be convinced that taking a smaller loss now is better than a bigger loss later. To make that case, start with a letter written by the seller giving an overview of the seller's desperate situation. The lender must recognize the seller's inability to pay the loan — immediately and in the foreseeable future — and that the situation is irreversible. The seller should supply as much evidence and documentation as possible, such as divorce papers, evidence of job loss, delinquent accounts, utility shut-off notices, car repossession paperwork, last two years' tax returns, recent pay stubs and recent bank statements. If the lender thinks the seller has money or assets stashed away, it will never go along with a short sale.

**A statement of the property's value.** This can be an appraisal or a broker's price opinion. The lower the estimate of the property's current market value, the better it will be for you. You want to show the lender that the seller would not be able to get enough for the home via a normal sale to satisfy the loan. Compile a list of all the problems with the home that hurt the value and make it undesirable to the average buyer and tougher for the lender to resell. The longer a lender must hold onto a property, the more expensive it becomes. If the lender realizes the property will bring it nothing but headaches, it will be more likely to OK a short sale. Richard Geller, of [MortgageReliefFormula.com](#), who has participated in hundreds of short sales, says this part is critical. "Many short sales are turned down because the lender doesn't think the offer is high enough." He advises doing this before the lender does a valuation. "There are ethical and legitimate ways to get a low valuation, and if you show this to the lender to start with, your offer won't look so low." Geller adds that the offer to the lender can be below the amount of valuation: "The offer can be 85 percent in areas that are slow but not terribly distressed, and as low as 50 percent in really distressed areas."

**Detail the costs and liabilities.** You want to show the lender it would be much better off letting you take the property off its hands. If you can convince the lender that the home is a money pit, all the better. Take photos of any damage and get estimates of the repair costs. Note: This is also a good opportunity for you to take an honest look at the property and decide if you are willing and able to invest the time and money required to fix it up. Remember: A short sale is always an as-is sale. The lender is not going to pay for or otherwise be responsible for any repairs. But, for example, if the lender forecloses, there's a good chance it will be forced to make repairs just to get the house resold. That's one of the liabilities the lender may face.

**A settlement statement.** This statement, which can be prepared by a closing agent or real-estate lawyer, outlines the purchase price, the closing costs and any other costs or fees involved in the transfer of the property. It is often referred to as a net sheet, and the information can be entered onto a HUD-1 Settlement Statement to show the final, negative result at closing.

### 9. Negotiate

It's not uncommon for the lender to reject your offer or to come back with a counteroffer. As with any real-estate transaction, you should figure out beforehand what your absolute highest limit is, and don't be afraid to walk away if the lender won't meet your figure.

### 10. Seal the deal

Once you've reached an agreement that all three parties — you, the seller and the lender — are OK with, get everything in writing and officially recorded. Make sure the seller understands all of the terms of the deal. Next comes the closing and the property is yours.

### More important details

1. The entire process gets far more complicated — and success more uncertain — if more than one lender is involved. Second or junior lenders often are the ones absorbing most of the loss. If there is a second mortgage or a home equity line of credit, you'll need approval from all. In addition, you may find your mortgage loan was sold to another entity in a process called "securitization," and therefore you also need approval from that company.

Be sure to do a title search, and verify the lien position of the lender you plan to contact. Pursue short sales only with the primary lien holder. Making a deal with a junior lien holder is a waste of time, as you will still be on the hook to the primary lien holder for whatever is owed to it.

- 2. The Mortgage Forgiveness Debt Relief Act of 2007 gave short sellers a big tax break by changing the way the forgiven amount was viewed for tax purposes. Before passage of the act, that amount was considered as income for the borrower and was subject to tax. However, the new law removed that tax liability.
- 3. Time is of the essence. While you negotiate with the lender, the clock keeps ticking. Do everything you can to get the lender to move quickly. Many short sales fall apart because the lender moves too slowly and fails to complete the deal before the property goes to auction.
- 4. Some buyers have successfully negotiated with the lender to minimize the damage to the seller's credit rating. The lender has no obligation to agree to this, but if you can persuade it not to report this action as a black mark on the seller's record (and put this in writing as part of the deal), it will give the seller a big head start in rebuilding his financial life. Typically, the loan will show up on a credit report as "paid," but it will carry a notation that says something like "settled for less than originally owed." That is more favorable than a foreclosure, but still negative.

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Powerfade

Mar 8, 2012 3:53AM



### "Are you Nutso"

#### Now "splain this to me Lucy".

How is it that he worked full time, or even a good portion part time, as a lecturer when he was fully engaged into his political career?

As I stated, his resume' seems to overlap a lot, suggesting his motivation was not employment, but rather one of posturing for his political motives and ambitions.

*A lot of organizations place needs on their own, not so much for their employment, but rather to enhance their own credibility. Kind of like*

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Are YOU Nutso

Mar 7, 2012 10:58AM



powerfade.....



According to the University of Chicago, School of Law, President Obama worked at the university as a professor in the capacity of Lecturer and Senior Lecturer from 1992 until 2004, when he took office as a United States Senator. You also failed to mention that while attending Harvard, President Obama served as the Editor of the Harvard Law Review.

4 1

NoMoreMeltdowns

Mar 7, 2012 7:12AM



"Powerfade"

You must be joking! Are you so obsessed with your extreme right wing ideology that you need to go on a political rant in the comment section of an article about real estate short sales? You need to get life and don't get burn by the hot coffee or the political rants you are spewing out!

5 2

Powerfade

Mar 3, 2012 9:11AM



Dennis Elliott

*"This economy will keep getting better because we have someone in the white house that knows what it is like to work for a living."*

I just about spit out my coffee when I read this...LMAO!

For the record this person's, to whom you refer, only private work history is at a Baskin Robins in Hawaii employed as a clerk, in his youth, for a very short period, before he entered into the political arena. Yes, he had various sundry positions, but all were politically based and funded.

He attended mostly private schools that were quite expensive to attend and then traveled the world during his young adult life doing various things including spending an inordinate amount of time in Bali while being paid by

More

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Powerfade

Mar 3, 2012 9:10AM



*"The 29 year old law student made it clear in his initial interview with Miner that he was more interested in joining the firm to learn about Chicago politics than to practice law. During the four years Obama worked as a full time lawyer at the firm, he was involved in 30 cases and accrued 3,723 billable hours."*

That's less than 10% working hours for his four years. His so-called law practice occurred during this time from 1996 to 2004, with his law license becoming inactive in 2002 along with Michelle's.

It also should be noted that during this time 1995 he seriously begins political career. Most of his documentation dates and times overlap one another. Suggesting his "career" was more or less a front for his political ambitions. In other words when he "worked" was more or less a source of funding for his political activities.

More

2 6

Powerfade

Mar 3, 2012 6:05AM



RM59

*"The money that a smaller bank loaned out is the private owners money. and you want the government to come in and make them take a loss. That is like the government coming in and telling the company you work for to pay you less, just because someone else complained that you make too much."*

I believe obama tried this very thing awhile back. Didn't he try to make certain ceo's and other execs restrict their pay/bonuses?

Should it matter whether you work at big box store as a clerk or own the store or chain?

Government telling "private " business what they should pay is just another step in the wrong direction

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Someone

Feb 24, 2012 2:52AM



The article has way too many serious errors!

A Bankruptcy does not prevent a short sale. It just delays it. Once the Bankruptcy is discharged, the Short Sale can continue.

In almost all cases, the seller will be required by the lender to vacant the home by closing.

The lender does not forgive the remaining balance of the loan, unless they agree to do that as part of the sales contract.

Jim Weix

More

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Laurie Montijo

Feb 21, 2012 1:38AM



I dream of a time when we, human beings, get over the propensity to judge, provide black and white responses, and share information that others may benefit from. Clearly, as it often the case in life, the experiences each homeowner, potential homebuyer of short sale properties and successful purchasers of these types of properties have had a wide range of experiences. Several individuals posted serious challenges working with the bank(s) to obtain properties the bank is sitting on and in many cases, e.g., the person who offered the asking price, it simply makes no sense. What burns me is the individuals bagging on the people, families, extended families, people who purchased those homes with equity and had anywhere from sufficient to plenty of income to maintain their mortgage, taxes, insurance, take care of house repairs and or pay deductibles, through loss of work with 10% unemployment or were high performing, dedicated employees who became disabled and are attempting to pay that mortgage with 77% reduction in income, a home that had \$180 k equity (purchase price \$455 k -- loan \$28 0k) and are either have no equity to pay realtors commissions, escrow fees etc., or may possibly even be \$35 k underwater due to the extraordinary loss in value vs the principal reduction as the payments are made. If a short sale want good for you, then you are very blessed. However, it certainly does not invalidate their

More

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pghsold

Feb 18, 2012 6:12PM



I have been a Real Estate Broker for 35 years and my advice is to cut to the chase. Even if you see a really good distressed property, closely examine the complete area. If there are tons of other bargains, don't proceed. When they eventually sell, and the shadow market is completely exposed, you will really be underwater. The only thing more stupid is to pay cash. This goes for condos as well. You may be holding that property until the day you die, unless you find another sap who will pay cash. Even exercising the due diligence inspections can be a royal hassle; and remember, damage can occur after the due diligence and before settlement.

11 2

RM59

Feb 18, 2012 5:56PM



People that think the Government needs to step in and do something about this, remember, it is the banks money, and it is entirely up to them if they want to do a short sale. Not every bank took bailout money. Most small banks are privately owned and operated. The money that a smaller bank loaned out is the private owners money. and you want the government to come in and make them take a loss. That is like the government coming in and telling the company you work for to pay you less, just because someone else complained that you make too much.

5 0

RM59

Feb 18, 2012 5:41PM



DENNIS ELLIOTT: Can you send me \$100?

2 1

RM59

Feb 18, 2012 5:35PM



TOM C: they did. Go back and reread the article.

1 1

TomC

Feb 18, 2012 5:24PM



You didn't mention the tax ramifications on the debt forgiveness portion of the loan.

3 2

Da facts

Feb 18, 2012 5:08PM



Den Den,

Let's meet and I'll show you how to get a job and pay your bills. By the way... just get a job, ANY job, you over qualified looking for a way out? I wish I had your as\* in Farah.. I'd beat you!

Weak

1 1

Dennis Elliott

Feb 18, 2012 4:30PM



Once again there are morons posting. NOBODY asked to get fired, laidoff, or the comany go bust and put them out of work, you idiot! So stop putting this on some kind of bs entitlement program. Please? All of us are sick of hearing from your stupid mouth, think first, then speak or write. Stupid right leaning idiots. I never asked to be disabled, but guess what, i am. It happened to me while i was overseas defending your pathetic little life. So stop with that stupidity, please. I feel that it is unfortunate for the ones who have to sell, have to take a loss on what was so dear to them. This economy will keep getting better because we have someone in the white house that knows what it is like to work for a living. I for one, am sorry for all who lost, or is losing the home they bought on good faith, i wish there was something i could do. If i was a romney or one of those pathetically rich people, i would pay every ones mortgage for them. Money is just that, money. People are everything!

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nobabyboomers

Feb 18, 2012 3:48PM



We are living in a new era of the entitlement generation. Don't pay your mortgage, it is not your fault. It was that underhanded banker that loaned you the money to buy your home's fault. Don't pay your student loan, it is not your fault. It is that dum college you went to and got a two bit education's fault. Don't have a job, it is not your fault, and the government will give you 3 years of unemployment along with food stamps. Don't have health care, it is not your fault. The government will take care of you with free health care. We have created millions of people that think nothing is their fault and the government (Obama Administration) tells them this garbage. No wonder we are trillions and trillions in debt and there is no hope in sight.

47 19

Suffolk.County.New. York.Attorney.

Feb 18, 2012 1:27PM



Also, while some people may have gotten themselves in this mess in some way, I have found that is usually not the case. Who would have thought the economy would tank so bad, oil would skyrocket (client was an oil deliver person for decades until people cut back), other expenses would rise dramatically as housing prices plunged, etc.? Yes, not the best idea to borrow against the house for mahogany cabinets and a Hummer but I am talking about people who had no way to see this coming.

7 8

Suffolk.County.New. York.Attorney.

Feb 18, 2012 1:22PM



Get an attorney who not only knows the foreclosure defense business well but also has an extensive finance background. As people mentioned below, the lenders have some sort of a "system" where no one can make any reason out of it, not without legal help. Here in NY, in Suffolk



County, on Long Island, the foreclosure courts are very backed up due to the high volume. Attorneys who do this know how this should be handled. Additionally, the foreclosure court head conducts seminars for attorneys at the bar assn and there are numerous other programs. However, if people try to do this themselves, good luck. While waiting for the attorney for the lender, where there are so many foreclosure conferences we are all in big room, I again got to overhear lots of meetings between the lenders' attorneys and the h/o's attorneys. The little snot lawyers for the lenders were walking all over people and trying it on the foreclosure defense attorneys they did not recognize. I think if I had not thrown a couple of financial terms at him that he had no idea about, terms ANYONE doing this should know-heck I knew it on Wall St at my first job decades ago- that smirk might have sat on his face through the negotiations (went great-monthly pmt half and, as usual, I am still going for

More

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artsyone

Feb 18, 2012 12:39PM



There is NO SUCH thing..why they dont call it a long sale I have no idea....

We have tried 3 times on 3 different properties...after 3 plus months we gave up. We too have an above average credit rating..the banks are the ones who put this country in this mess..and they are the ones who control the short sales. We are done! Going to buy a mobile home until we can go after what we really want...

21 3

a4greymom

Feb 18, 2012 11:53AM



We are in the process of buying a short sale.

I will be writing my congressman and others about this process. The problem for me has been my lender. We have a 730 credit rating, have no real debt and have been told the following: Our credit score is too low to acquire the 3.5 or 4 percent money. We only qualify for the 5 percent only. IN order to qualify for the lower interest rate, our score must be 770 or higher. The lender is requiring that we have 2 years of taxes escrowed, for 2012 and 2013 and will continue to take out the escrow amount in the current new loan, which makes us 2 years ahead on our taxes. They are requiring that we have 2 years PMI insurance escrowed and again will take out the escrow amount in the current new loan. We are putting 20% down. Unfortunately, we will not be able to come up with the closing money due to the above required amounts which are absurd. We have complained and argued to no avail. They are making it impossible to acquire this home or any other short sale home. I don't want to hear anyone say that this is not the norm, we have talked to several short sale buyers that are going through the same thing. While I am against the

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