

## **FAQs – SHORT SALES IN OREGON (2013)**

By

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*The local and national real estate markets have been on the ropes for five years. The third quarter of 2007 was the statistical peak for housing prices in the Portland-Metro area. From that point forward, the real estate market went into a downward spiral from which it has never fully recovered.*

*However, the third quarter of 2012 was the first time since the third quarter of 2007 that home prices have actually increased over the prior year. Bend, Oregon is experiencing the same resurgence.*

*So for those homeowners still awash in negative equity, 2013 may be the last and best year to complete a short sale with a minimum of adverse consequences. This is especially true since this year we know that if a home is short sold [or foreclosed, or deeded back in lieu of foreclosure] the seller will not have to pay income tax on the cancelled debt.<sup>[1]</sup> We don't know if the forgiveness law will be extended into 2014. The extension for this year was not even announced until early January 2013, causing a lot of anxiety for homeowners who were unable to complete their short sales by December 31, 2012.*

*What follows are a series of FAQs based upon the latest information I have acquired while consulting with homeowners on their foreclosure avoidance options. ~ PCQ*

**1. What are short sales, exactly?** The sale of real property – residential or commercial – for a price that is insufficient to pay off the liens recorded against it. In order for the seller to be able to pass marketable title to the buyer, the holders of all recorded liens must consent to the short sale transaction. Whether the seller will have any personal obligation to repay the creditors any of the remaining debt due under the promissory note is a matter of negotiation that will have to be completed before the closing of the transaction.

**2. Short sales were not as prevalent in 2010 as they are today. What has taken lenders so long to figure out that short sales actually work to their benefit?** Statistically, it has been known for some time that if a property is foreclosed the extended carrying costs for property taxes, insurance, winterization, etc. – not to mention the lower resale price in foreclosure – returns much less money to them than had the property been sold in a short sale months earlier. Why it took the Big Banks so long to figure out the obvious is a bit of a mystery. My theory is that “*if you're a hammer, everything looks like a nail*” – that is, the only thing Big Banks knew how to do was to foreclose. So they doggedly continued to foreclose millions of homes, rather than learning to short sell them into the marketplace where they belonged. Once the Big Banks set up their short sale protocols, got them staffed and running, and realized that it actually worked, they got on board. The process can still be slow and frustrating, but it's much better than it was.

**3. What other choices do lenders have when a loan is in serious default?** Besides permitting the borrower/seller to short sell the home: (a) They can offer to modify a borrower's loan such that it becomes more affordable either in reduced payments, reduced interest rate, and/or reduced principal balance. The problem with the modification process is that it rarely succeeds; takes months or years;

frequently results in re-default; and overall is a disappointing and frustrating process for most borrowers. (b) They can offer to take a deed-in-lieu-of-foreclosure (“DIL”) from the defaulting borrower. However, banks are generally disinclined to consider this option unless and until the borrower has spent several months first trying in good faith to sell the home. And just like the short sale process, in order to do a DIL, the borrower must jump through the same hoops as a short sale, i.e. write a “hardship letter” and turn over all of their financial information. Furthermore, borrowers are not permitted to pursue a short sale *and* a DIL at the same time. (c) The lender can foreclose.

Although it will soon be “illegal” – whatever *in terrorem* effect that has on TBTF banks – currently, the Big Banks generally pursue foreclosure even while their defaulting borrowers are seeking a foreclosure avoidance alternative from the bank - a disgusting process known as “dual-tracking.”

**4. *Is it really the lender’s money that is being “shorted” in a short sale?*** Great question! Contrary to what many believe, it is generally not the original lender’s money that gets shorted. Or to put it a different way, the lender from whom you are seeking short sale consent does not “lose” any money as a result of a short sale. The reason is that most loans made during the easy money years, circa 2005 – 2007, were quickly sold into the [secondary mortgage market](#), either to [Fannie or Freddie](#), or to a “[private label](#)” buyer. Thus, the bank you’re discussing your short sale with today is likely just “servicing” the loan, i.e. collecting the payments, monitoring the tax and insurance reserves, and generally being responsible for what’s happening with the loan on a day-to-day basis – including foreclosing it. The bank that originated the loan, i.e. the one you actually borrowed funds from, received most of its money back when it sold the paper into the secondary market.

So, for example, when Countrywide made a loan in 2006, it quickly sold it into a huge trust called a “[REMIC](#)”, consisting of millions of dollars of other loans. Investors throughout the world bought “slices” of these loan pools. Countrywide – now Bank of America – appointed itself as the “servicer” of the trusts they created – guarantying it a nice stream of fees for the life of the trust. Due to cost-cutting, as well as the difficulty of servicing so many loans in default, today, many Big Banks have sold their servicing rights to large non-bank servicers, such as [Ocwen](#). [Note: The previous explanation deals only with the [first mortgage](#); oftentimes, originating lenders making second-position loans retained them in their own portfolio. Thus today, when a short sale involves two loans, there is a higher probability that the servicer of the second mortgage is also the owner – it which case it will likely take the loss on their own books. – PCQ]

**5. *So who really makes the final decision to consent to a short sale – the owner of the loan, i.e. the “investor,” or the servicer?*** Unless the Servicing Agreement provides otherwise, the “investor” in the secondary mortgage market, i.e. Fannie, Freddie, or the Trustee of the REMIC, makes the final decision. This applies equally to the consents for a loan modification or a DIL.

**6. *Does the seller/borrower really have any say in the short sale?*** I firmly believe the answer is “Yes.” It is here that a good short sale Realtor® is invaluable. My experience is that the following traits/skills are important to the ultimate success of a short sale: (a) Persistence; (b) Patience; (c) Courtesy; (d) Experience; (e) Knowledge about the short sale process – e.g. being familiar with the [Equator System](#) used by most of the Big Banks; (f) Never-say-die attitude. While there are a few monkey-wrenches that can be thrown into the process, most short sales do close. It just takes the skills of a good Realtor®.

**7. What if there are multiple short sale offers? How should they be handled?** This is ultimately up to the lender/servicer you're dealing with. Although it was different in 2009-2010, today I am seeing most lenders prefer to deal with only one short sale offer at a time. I do hear of some listing agents telling buyer agents that they are "not going to submit their offer to the bank because it already has an offer before it right now." If the listing agent's position is based on the bank's instruction, that's fine; but otherwise, I find this approach problematic.

**8. Is there ever a reason not to do a short sale?** Yes. For example, if the seller/borrower does not have a huge amount of negative equity, say \$30,000 to \$50,000, with the Portland and Bend markets showing signs of price resurgence, if the owner wants to keep the home and can cure any loan default, he/she may decide to wait it out, hoping to see some equity appreciation in the next 3+ years.

Another example may be that the borrower has already been served in foreclosure and several months have elapsed. The closer the borrower is to the foreclosure being final, the less incentive there is to try to short sell the property. However, there are actual and perceived differences between a short sale and a foreclosure, e.g. in credit and tax issues, and these must always be part of the analysis. I strongly recommend that when debating between a short sale and pending foreclosure, you need some expert help to evaluate these issues.

Lastly, in cases where the borrower's property will not escape the assessment of [income tax on the debt cancellation](#) arising from a short sale [e.g. *the property was used as a rental and not lived in by the borrower for two of the past five years*], if it is not too deeply awash in negative equity, it may be beneficial to ride things out, rather than suffering a "1099 event" from the short sale.

**9. What if my condo is involved in construction defect litigation? Will I be able to short sell it?** Surprisingly, the answer may be "Yes." I have seen investors, i.e. those purchasing properties for rental, buy condos that are currently involved in construction defect litigation. Investors are generally more sophisticated, and after crunching the numbers – which includes factoring in the anticipated cost of an upcoming assessment – they may agree to proceed. Remember, a potential renter is not going to be affected by such litigation in the same way as an owner-occupant who will be fearful of having to pay a large assessment in the future.

**10. Can I start a short sale while a foreclosure is pending?** Yes! And here's why: All of the Big Banks are foreclosing trust deeds judicially. They started doing this *en masse* in mid-2012. Wells Fargo had been doing judicial foreclosures months before that. Some of the smaller banks who carried the loans on their own books – i.e. they did not sell them into the secondary market - are still doing non-judicial foreclosures because there was no funny business in the handling of the paperwork after the loan closed.

So the rumors that there are fewer mortgage foreclosures today than 2012 could be an illusion attributable to the fact that it takes so much longer to tee up a judicial foreclosure. That is, the complaints are numerically coming out much slower, giving the erroneous appearance that there are fewer of them, when that may not be the case. This might be called the "Pig in a Python" effect, as the glut of paperwork slowly works its way through the courts' digestive tract.

A judicial foreclosure involves a massive amount of preparatory work and today it's not being handled by non-judicial foreclosure trustees. Rather, lawyers and paralegals are now up to their eyeballs in paperwork. Every person and entity appearing in the litigation report – i.e. the report issued by the title company telling the plaintiff bank/servicer who to name in the foreclosure – has to be tracked down and personally served. If they cannot be found, the lawyers have to secure court permission to pursue another form of service. *[In the "old days" of non-judicial foreclosures, service was accomplished by mailing and posting.]* Now, the banks' lawyers have to file a motion to obtain court permission at almost every step of the way. Invariably, they cannot complete the process fast enough, and pursuant to court rules, if too much time elapses, the attorneys have to secure court permission to continue with the foreclosure. And when they finally ask for a judgment, the bank/servicer must scour all of their records to find every last penny that was expended during the default stage and the foreclosure process, including the piling on of every fee and charge possible. All of this must be assembled and formatted in an understandable way so that it will pass court muster. Given the legacy of robo-signing, forged documents and bogus notarizations, you can be sure that bank attorneys are bending over backwards to make sure every "t" is crossed and "l" dotted, since it is their law license on the line if they ignore their client's hijinks.

Although I am not privy to the actual inner-workings of a foreclosure mill – it must be a paper chase of epic proportions - based upon what I've seen, I feel comfortable in believing that it would take a good six months for bank lawyers to get a foreclosure complaint filed and served - perhaps longer. After that, it can easily take 6 to 9 months to get the foreclosure judgment. Then there is a 30-day period to publish the fact that the property will be sold by the sheriff. And getting to the auction takes time, since the sheriffs in most large counties are now inundated with an unfamiliar process they had no involvement with during the many years of non-judicial sales by foreclosure trustees.

So from the date of filing to the date of sheriff's sale it can take nearly 12 months; plenty of time to complete a short sale. And based upon what I've heard from some bank lawyers, they are generally willing to dismiss a foreclosure at almost any point in the process – even well after the default judgment has been recorded – if the short sale closes.<sup>[2]</sup>

So it's never too late to try to do a short sale. If a delinquent borrower was served with a Big Bank<sup>[3]</sup> complaint in foreclosure, say on April 15, 2013, and the home was listed for short sale immediately thereafter, assuming it was priced right, the chances are good that the transaction would close before the end of 2013. The same cannot be said of the judicial foreclosure, which will not likely be on the sheriff's auction block until well into 2014.

**11. What is a HAFSA short sale?** This government program has been around since late 2009, and was touted as one that would "streamline" the short sale process. Initially, it was intended only for borrowers coming out of unsuccessful loan mods. That does not appear to be the case today. It has evolved over time, and appears to have perks other short sale programs don't have *[e.g. a \$3,000 relocation assistance payment to the seller/borrower]*. However, it is somewhat unclear who qualifies and who doesn't. Like so many other programs, the Big Bank Servicers seem to rely upon different criteria for who qualifies and who doesn't – and who gets the relocation assistance and who does not. Furthermore, since this program, like all government programs, *is voluntary*, banks are not required to participate, even though they are willing to consider a request for a short sale. The government link describing the program is [here](#). Just because a lender/servicer will not agree to do a "HAFSA short sale",

does not mean it will not consent to a regular one – and in my opinion, besides the \$3,000 relocation assistance, I don't see much difference between the two in terms of the final result.

**12. *I have heard of problems in short sales when there the borrower has mortgage insurance. Can you explain?*** I could, but have written so many posts about these uninvited interlopers that I will simply direct you to my rants, [here](#), [here](#), and [here](#).

**13. *Can I try to do a short sale and deed-in-lieu at the same time?*** My experience has been that you may not, metaphorically speaking, queue up in both lines at the same time. The reason is that the Big Bank Servicers cannot multi-task; they seem to have the institutional equivalent of [ADHD](#). If you want to do a short sale, you have to get in the "Short Sale Line." If you want to do a deed-in-lieu of foreclosure, there's another line for that. It's sort of like going to a movie at the Cineplex; if you wanted to see "[Reservoir Dogs](#)," you'd queue up behind that ticket window, and if you wanted something a little more sedate with less bloodletting, say, "[Love Story](#)," you'd queue behind that window.

Moreover, subject to limited exceptions, most lenders will not permit you to try to do a deed-in-lieu, until you've tried and failed to do a short sale. The reason is simple: They don't want the property any more than you do. They would rather someone, i.e. a short sale buyer, took it off their hands, thus assuming the duty to pay the taxes, insurance and maintenance. Big Banks are in the business of ~~larceny~~ lending, and not in the business of holding real property.

And just to remind its beleaguered borrowers who's boss, if you move out of the short sale line and into the deed-in-lieu line, the bank will act as if they never heard of you before, making you start from scratch in your new queue, filling out all of the old forms again, writing another hardship letter [as if it will be any different than the first one], and assigning a new bank negotiator.

**14. *What if the buyer wants me to give them some seller concessions, e.g. payment of closing costs or certain discretionary repairs?*** The answer generally is that since the bank<sup>[4]</sup> is taking the "financial haircut" by getting less of its loan repaid than was actually due, it will not voluntarily permit you, the seller, to offer up concessions that it will have to absorb out of the gross closing proceeds. There are cases where servicers will permit necessary concessions, since they know that any purchaser would demand them. For example, if a servicer refused to put on a new roof when everyone agrees it is absolutely necessary, and the short sale thereby fails, thus resulting in foreclosure, the bank would still have to pay for a new roof in order to sell the property.

**15. *What happens if the bank servicing my loan transfers the servicing to another entity while my short sale is in progress?*** Before answering, let me explain what a servicer is and does. In most cases, the servicer is not owner of the loan. The loan was likely sold into the secondary mortgage market shortly after it was made to you. The servicer is responsible for collecting and accounting for payments, monitoring the tax and insurance reserves, and generally being responsible for the handling of the paperwork on behalf of the owner [frequently called the "investor"] of the loan. Recently, many Big Banks, especially B of A, have sold the servicing rights to many of their nonperforming loans they were handling. In some cases, these sales are too large, non-bank servicers, such as [Ocwen Financial Corporation](#). This can throw a monkey-wrench into your short sale approval process, and it's likely you may have to start over, since one cannot assume that the new servicer has – or can find – all of your old

paperwork. However, since the owner of the loan hasn't changed, the outcome should be essentially the same regardless of who is currently servicing it.

**16. Why are some short sales more difficult than others?** There are several issues arising in short sales that can slow down or confuse the process. Here are some examples: Is there one loan or two on the property? If so, are they both owned or serviced by the same entity? If so, will the short sale proceeds pay off the first lender entirely? Will first lender contribute to the second lender? Is mortgage insurance involved? For a discussion as to the relevance of these issues, go to my post [here](#).

**17. Can I short sale my own home without using a Realtor®?** No. And why would you want to try? Your Realtor® knows what they are doing and you don't. Besides, it won't cost you anything, since the listing and selling commission comes out of the gross sale proceeds before the bank gets its money. By definition, the short seller brings no money to closing.

When a seller tries to sell their own home without a real estate agent, the process is called a "FSBO" or "For Sale By Owner." Banks insist that all short sale properties be listed with a neutral [i.e. unrelated] real estate agent. *[I say "neutral" to include almost any financial or personal relationship. If there is a pre-existing relationship between the seller and his or her agent, it should be disclosed to the bank negotiator up front. Putting it into the Sale Agreement itself will go a long way in establishing disclosure. - PCQ]*

The reason for insisting upon Realtors® is simple: The banks want to make sure that the property gets as much exposure as possible as quickly as possible, and that means getting it posted on the local multiple listing service ["MLS"]. FSBOs cannot display their property in the MLS.

**18. What if the property I want to short sell is currently rented?** This can be a problem on many levels. First, under Oregon law, landlords may not have access to the property without first giving advance 24-hour notice. *[Although the notice doesn't have to be in writing, other forms of notice, such as a phone call, or even email, can create a risk that receipt may be denied.]* This pretty much kills the idea of putting a lockbox on the property for buyer agents to have unlimited access anytime with their clients. And although the landlord and tenant may enter into a written agreement for less than 24-hour notice, it must be supported by separate consideration, i.e. a reduction in rent or other form of compensation, and cannot be included in the original rental agreement; it must be a separate agreement. And if the property is on a fixed term lease, the short sale buyer would have to honor the lease for the remainder of the term. For investor clients, this may be an advantage rather than a drawback. Lastly, month-to-month tenants may not be very willing to fully cooperate, since it could mean they will lose their home to a new purchaser. For these reasons, before listing the property, it may be best to terminate the rental agreement if it is a month-to-month tenancy. In Oregon you may issue a no-cause 30-day written termination notice for a periodic tenancy. If it is a fixed term lease, the landlord's only option is to see if the tenant will vacate early, perhaps by an offer of free or reduced rent for a short period of time.

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[1] This assumes they lived in the home two of the last five years and used the loan proceeds to build, buy, or substantially improve the residence. ***Caveat - This post is intended to be informational only and not tax advice. Please verify this information with a tax consultant who is familiar with your particular situation!***

[2] The bank attorneys will not dismiss until there is a confirmed closing, after which time they will record the judgment of dismissal, thus clearing the title for the short sale buyer.

[3] Smaller banks move much faster, and my comments regarding slowness in the judicial foreclosure process are limited to foreclosures by B of A, Wells Fargo, Chase, Citi, Morgan Stanley, and large non-bank servicers such as Ocwen.

[4] Actually, in most cases it isn't really the bank or servicer who is taking the financial hit – rather, it's the "investor" i.e. the party who bought the loan shortly after it was made. This could be Fannie Mae, Freddie Mac, or some private label investment trust.

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