

# REOs and Short Sales

>> GUIDE FOR BUYERS



The media loves to tout the idea that great bargains can be had purchasing bank owned homes, known in the real estate business as REO (real estate owned) properties, and how easy it is. While it is true you can get great bargains purchasing bank owned properties, it is not always easy. There are many things to watch out for that we have learned in our 30 plus years of experience in the San Mateo County real estate market.

## What is an REO?

An REO is categorized as a post-foreclosure sale. The home owner/borrower has defaulted on their loan and the bank (lender) has acquired ownership to the property as a result of the foreclosure process. Usually then, the bank lists the property with a real estate broker who is responsible to manage, market and solicit offers for the property through the typical channels, such as, MLS and real estate websites.

## Who is involved in an REO sale?

There are several parties involved in selling a bank owned property that are not involved in the traditional home purchase. The most critical is the asset manager who has been hired by the bank to dispose of the property profitably. The asset manager must justify the sale through various levels of bureaucracy which is almost always a challenge.

## Is buying an REO for beginners?

Purchasing an REO is not for beginners. The transaction is fraught with details and necessitates constant follow-up. Often it seems like the left hand doesn't know what the right hand is doing. Here are some tips:

1. Be polite and patient. Banks and their asset managers are swamped with sometimes thousands of properties in their portfolio they must manage and sell. Often they are understaffed and overworked. Remember they are human beings who can easily ignore your file if you disrespect them.
2. Use a Buyer's Agent. Work with an experienced real estate buyer's agent. Buying an REO requires a special set of skills, an intimate understanding of the real estate contract, attention to detail and persistent follow up...usually every 2-3 days.

3. Recognize the process. Banks have an operational manual, various levels of authority and supervision. Employees have strict job descriptions and rarely deviate from the rule book. Finally, they have to justify the net proceeds of every offer to an executive committee. If the numbers work, they will usually move forward. It is not at all emotional as it is for the traditional home owner.

4. Get a sales history. Almost every REO has been on the market in the past usually at a higher price and didn't sell. The longer a home has been on the market, the more shop worn it becomes.

5. Determine the comparable homes sold and pending. Ask your buyer's agent to prepare a market analysis of similar homes sold, pending sale and expired listings in the vicinity over the previous four months. Real estate markets are local and in constant flux. Defend your offer with facts.

6. Write a clean offer. Use contingencies wisely and well. Don't hold up on the weasel clauses like choosing the title company as they will sabotage your offer. Contingency periods should be short, specific and used only to protect yourself from serious deal killers.

7. Submit a genuine pre-approval letter. Be sure your lender, if you need one,

writes a strong commitment letter clearly demonstrating your credit worthiness.

8. Understand the local market demand. Be sure your buyer's agent asks the asset manager if other offers have been submitted and how many. Some markets, such as Sacramento, are tremendously active with multiple offers typically from investors seeing profit opportunity. The average number of days on market is an excellent indicator of market strength. An experienced, knowledgeable buyer's agent will help you understand the meaning of that number.
9. Follow the rules. Banks have prescribed procedures for selling their properties. Submit complete offer packages – never piecemeal – and use the forms they prefer. Failure to do so is a prescription for failure.

### Why are REOs better than short sales?

What is a short sale? A short sale is categorized as a pre-foreclosure sale. The seller can no longer make their loan payments and owes more on the property than it is currently worth. The seller places their home on the market looking to get an offer from a buyer they can present to the lender in hopes the lender will approve the sale, take a loss and let the seller walk away from the property without any further liability.

Buying an REO is generally a more business like, efficient transaction and takes far less time to complete with greater certainty.

A short sale is a case of a desperate seller. This means that emotions are involved and tension runs high. Plus, the lender must approve the sale and they generally are less likely to take below-market offers because the property is not technically on their books yet. So, more often than not, a buyer would be better advised to wait until the property is foreclosed on and becomes an REO.

There are other potential problems as well. First off, lenders are almost universally unwilling to assign the file to a loss mitigator until they have a fully executed sales contract signed and completely documented by both the buyer and seller, including a buyer's

pre-approval letter from a reputable direct lender.

Then several things must happen. The seller must demonstrate a genuine financial hardship. That is, show an inability to make loan payments. Examples of acceptable hardship are job loss, divorce, serious illness. Owning a home whose value has declined below the outstanding loan balance is not a hardship, it is a consequence of market fluctuation.

All throughout this process, the lender is the controlling force in the potential transaction. A lender will make a business decision based upon whether a short sale or a foreclosure will generate more dollars for them, so short sale homes may not be bargain priced or below market values. Lenders know what the property is really worth. They have fee appraisers and independent brokers available to determine the true value of the property. A buyer can expect to buy the property at market value.

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Given that fewer than 40% of the alleged short sales fail to close, and that most short sales can take between 3 – 8 months to actually close escrow, it is far more likely for a buyer to find a more suitable home in a shorter time for a better price.

From our perspective, it seems that buying an REO is a more business-like process which usually takes less time to close escrow as compared to the short sale

route. Short sales can often take 3 – 8 months to complete and there is the added difficulty of financially challenged home owners who are desperate for cash. REO properties, while market-priced, can produce greater net value and a smoother purchase.

### Bottom line, will an REO strategy work in San Mateo County?

The media has put a lot of emphasis on the spike in the number of foreclosed homes coming onto the national market, and while there has been an increase in San Mateo County as well, it is nowhere near the jump that other markets have seen.

Of the 1,878 single family homes currently for sale in the MLS, only 110 (5.6%) are bank-owned homes commonly known as REO and 321 (17.1%) are characterized as short sales. As San Mateo County has remained a moderately healthy market, we would expect the spring buying season to again heat up the market. This will mean that the best values will be sold quickly. So, while it can be a profitable strategy, it's not a sure way to a good deal.

**\*\*Insider tip:** It seems that a quirk in the accounting system used by banks opens the door for financial concessions, such as, credits for closing costs, prepaid HOA dues and assessments, seller paid charges and fees customarily paid by the buyer. So, the tactic is to offer the list price (or reasonably close to it) and offset the price with monetary concessions (give-backs) in the form of seller credits to the buyer.

If you would like an updated list of the REO and Short Sale (pre-foreclosure) properties for sale in Santa Clara or San Mateo County, visit [LivingWellinSanMateo.com](http://LivingWellinSanMateo.com) and click on the "Search for homes" tab. We'll also be happy to email this list to you. Simply send us an email at [info@LivingWellinSanMateo.com](mailto:info@LivingWellinSanMateo.com) and we'll get it over to you.

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The RayChel Realty Group has been coaching clients through real estate transactions in the Bay Area since 1978. Armed with some of the best trained agents in the area, The RayChel Realty Group has the experience necessary to successfully navigate even the most complex transactions, like REOs and short sales. Contact the team for more information about how they can help you buy your dream home or sell your current home and get started on your way to a new home today!

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