Tips for Home Buyers

5 Most Common Complaints of Short Sale & REO Buyers

Roughly forty percent of the homes for sale on today's market are short sales and foreclosures! Distressed properties are well known for their value (a reputation which is sometimes accurate, and sometimes not), but they also have a reputation for causing buyers to become distressed too.

Transactional snafus, last-minute surprises and long, drawn-out escrows that never close seem to be par for the course.

Instead of avoiding these properties altogether, get educated about the most common dramas that go down in these deals, and how you can avoid falling victim.

1. Run-on (and on, and on) escrows

When you're buying a home (or selling one, for that matter), time is absolutely of the essence. Buyers reasonably expect that the big time suck in real estate is in the house hunting process itself. It seems like once you find a home you want to buy and the seller agrees to your price and terms, things should move pretty quickly, right?

Not so much, when it comes to some distressed property sales. We've heard of the occasional, swiftly-moving escrow on an REO (real estate owned - by the bank), but for the most part, these transactions take anywhere from a few days to a few weeks longer than "regular" sales, because of the extra signatures, supervisor-level approvals and even investor involvement required to seal the deal. Banks don't have the same sense of urgency individual home sellers do, and it's not uncommon for the people who need to sign on the dotted line to be on vacation or scattered across the country, adding days or weeks worth of time to the escrow.

Short sales are also an entirely different animal when it comes to escrow timelines. While a standard sale from an individual seller to an individual buyer might take 45 days from contract to closing, a short sale can take anywhere from 45 days to 6 or 8 months after the seller has accepted the contract to get the deal closed.

Avoid the drama by:

Expecting your escrow to run long, and being pleasantly surprised if it doesn't. Expectation management is everything. Make sure you take these extended timelines into account when you're working with your mortgage broker on the issue of when to lock your interest rate, and how long your rate locks will last. You might even need to plan on and/or set aside an allowance for the cost of extending your low interest rate if rates are rising rapidly during the time you're waiting for the deal to be done.

2. Bank won't take a lowball offer

Banks owe their shareholders and investors a duty to get as much as they can for these properties. Just because you see it's on the market and listed as a short sale or a foreclosure doesn't mean they're going to give it to you for a fraction of its worth. The bank's goal is to get a purchase price as close as possible to the home's fair market value, as determined by the recent sales prices of similar, nearby homes, with some adjustments made for the property's condition. Fact is, many banks would rather see the listing agent reduce the price by a moderate amount, and wait to see what offers come in, than to accept an offer 30 percent below the asking price just because there are no other offers on the table.

Avoid the drama by:

Working with your agent to make a realistic offer, based on recent comparable sales in the neighborhood, not just on what you think you can get away with. You can waste a lot of time, spin a lot of wheels and lose out on a lot of properties making lowball offer after lowball offer on distressed homes. Sit down with your broker or agent, review the 'comps' and make a smart offer that reflects a good value for you, is within your budget and is not bizarrely out of the realm of the fair market value of the property.

3. Last minute postponements/cancellations

These transactions have an uncanny way of being delayed at the last minute - or never going through at all, through no fault of the prospective buyer. You signed docs yesterday, put your dog in the crate this morning and just hopped in the moving truck, only to get a text from your broker that the deal didn't close because the escrow company which was selected by the bank flubbed the checkboxes on a single sheet of paper (it happens). Or, you've been in contract (with the seller) on a short sale for four months, and the bank refuses the sale entirely because the seller refuses to kick even $1 of their own cash into the deal, despite having a flush savings account.

Avoid the drama by:

Staying as flexible as possible with your moving plans as long as possible. Best practice is to plan on some overlap between the time you can be in your last place and your scheduled move-in date. Also, if you're in contract on a short sale, you should take the point of view that you don't have a firm deal until you get the bank's approval of the transaction. Don't even think about starting to make moving plans or paying for home inspections and appraisals until you know the bank has given a green light to the deal and that the purchase price and terms they've approved work for both you and the seller.

4. The bank's black box

Make an offer on a normal home and you're likely to know what the outcome will be within a few hours or a few days, at the outside. If things take longer because the seller is out of town or some such, the listing agent tells you that, and you at least know what's going on.

Make an offer on a bank-owned property or a short sale? It could be days, but could also, easily, be weeks or months before you know what's going on. No amount of calling, pleading, prodding or nudging is likely to get you much information on how your offer or the seller's short sale application is being handled or what (if any) progress is being made. That "black box" into which your offer disappears at the bank level can be very frustrating.

Avoid the drama by:

Continuing your house hunt until you have an answer back. Maniacally pestering the listing agent for answers or harassing your buyer's broker into spending hours on hold with the bank is highly unlikely to get you any insight. (With that said, it does make sense for your agent to check in regularly - sometimes even daily - with a short sale or REO listing agent to stay updated on any developments with the property and to make sure your offer/transaction stays in the front of their mind.)

Most of the angst in these situations arises when a buyer feels they passed on properties that would have really worked for them when they pinned their hopes on a distressed home. You can only control your efforts and activities, not the bank's. Consult with your own broker or agent about staying proactive in viewing and even pursuing other properties until you have a firm "yes" from the bank on your short sale or REO offer. Until that time, and usually for a short time after you get the bank's approval, you have the right to back out of the transaction if you need to (make sure your broker briefs you on precisely when your right to rescind your offer or exercise contingencies - i.e., bail - will expire).

5. Double Standards

In a "regular" equity sale with no bank involvement, both buyer and seller are obligated to meet various timelines. Seller has to provide disclosures by X date, open the property to inspections - with utilities on - by Y, and close and move out by Z. REO and short sale buyers, on the other hand, are often dismayed to find that even though the bank might take weeks or months to sign or handle its deliverables, the bank will insist that the buyer show up, sign or send a check quick-like.

Avoid the drama by:

Chalking it up to the (admittedly irritating) way things are - the price you pay to buy from the bank. Realize that working with the bank on the bank's terms is unavoidable when you buy a distressed property. Then, go into the deal with realistic expectations - including the expectation that the bank will drag its feet, despite expecting you to keep every deadline - and you'll be less frustrated, and less likely to make poor decisions out of frustration.

Also, make sure you do respond in a timely manner to the bank's requests and your obligations under the contract. I've seen banks capitalize on buyer delays in returning signatures and removing contingencies to accept higher offers they received in the interim. Don't lose your home on a technicality because you assume that the bank's lackadaisical timelines apply to you as well.