Don DeRosa's

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The Short Sale: A Win-Win-Win-Win-Win Proposition

The mortgage crisis is real. It's affecting millions of families, either directly through foreclosure, or indirectly through lost jobs and other "collateral damage." As a result, a surprising phrase is finding its way into more and more MLS listings: *"This is a short sale."*

Even the most timid, "by the numbers" realtors are finally beginning to experiment in creative financing tools that we investors have been using for years. The result? Benefits all around: to lenders, sellers, realtors, and of course, to us as investors. Short sales can even help neighborhoods. If you're not doing short sales, you'd better hop on that train!

Let's review the concept of short selling for just a minute, and then I'll tell you why it's such a great way to buy houses.

Simply put, in a short sale the buyer of a property offers the bank less money than it's owed to settle the account. Let's say the seller owes $100,000 on a first mortgage, and $35,000 on a second mortgage, but the house is only worth $135,000. The seller's equity is zero, right? But what if you can get the second bank to take $10,000 instead of $35,000? Then, the cost of the house is only $110,000, giving you instant equity of $25,000.

In the past, if an owner had too little equity, most investors would pass on the deal, figuring they couldn't make any money on it. There was, of course, money to be made all along from many of these properties. It was just a matter of creating equity by negotiating a lower payoff amount with the lender.

Normally, investors work with the holders of second mortgages, because the primary lenders don't have as much incentive to negotiate. But in this market, banks may even be willing to negotiate a short sale for a loan in first position.

Why on earth would a bank agree to take less than what it's owed? Simple: Because something is better than nothing.

Have you ever had a garage sale? You get up at 4 a.m. and spend two hours setting up tables and carrying all your stuff outside by the armful. You mark prices on every little knick-knack while you fight off the "early bird" vultures. At 9:00 a.m. sharp, you start selling. All day long, you take money. You negotiate like crazy.

Over the course of the day, though, your goal changes drastically. At 9.a.m., your goal was to make as much money as possible to pay for little Betsy's first year at Harvard. At 9 a.m., that lime-green planter you inherited from your Aunt Mildred was a rare and valuable antique easily worth the marked price of $45. By the end of the day, the only thing you care about is getting rid of what hasn't yet sold. In fact, you'll just about pay someone else to take it, because there's no way you're going to carry it back inside. And as for that hideous green flower pot from your cheapskate aunt, even the local charities don't want it. You'll take a buck – no, fifty cents. Hey, let the kid go to community college. Heck, she'll never get into Harvard with those grades, anyway. Take my pot. Please.

Aunt Mildred's ugly old flower pot has become . . . A Problem to be Solved.

What's this got to do with short sales? The banks in this country are going to add up to a million ugly old flower pots this year to their inventories. Luckily, it turns out that you know how to paint and sell flower pots. Get the picture? The lenders want out of these houses. Some of them are so desperate they'll even consider short-selling loans in first position.

The great thing about short sales is that they present a win-win-win-win-win solution for coping with the mortgage crisis. What do I mean by that? I mean that everyone benefits: the banks, sellers, investors, realtors, and even whole communities. Here's how:

The banks benefit because every time they short sell, they unload a problem. Bank officers don't want to babysit empty houses all day. They don't want to file foreclosure paperwork. They want to invest and make money. They want to cut their losses and go back to what they were doing before they were distracted by the housing bubble. As an investor, your job is to give them a way to do that. True, we negotiate a price as low as possible, but the banks are sophisticated and know what they're doing. For them, it's 5 p.m. on the last day of the garage sale, and that ugly green pot is still sitting there.

Sellers benefit, too. Notice that I haven't once mentioned what a great thing this mortgage crisis is for investors. Foreclosure is tragic thing, and I get no joy out of watching hundreds of thousands of families lose their homes. Yes, a lot of homeowners are at fault for taking on homes they couldn't afford. Guess what: I've messed up, too.

For many sellers who have adjustable rate mortgages, equity lines of credit, or second mortgages, there are only three options: foreclosure, handing the house back to the bank, or a short-sale. If I ever had to make that choice, I'd take a short sale all day long, even though right now I might be taxed on the amount of the forgiven debt (the rules on this vary depending on the seller's situation).

Investors, of course, benefit from short sales. In any market, the short sale offers a way to create equity where none existed. That, in turn, expands your pool of possible investment properties dramatically, especially in a depressed market like this one.

Realtors are big winners, too. A realtor who learns the ins and outs of short sales can list a house at the true market price, instead of having to list at an over-inflated price to cover the loans. Houses with inflated prices don't sell or even get any traffic, and houses that sell don't pay any commission. All they do is sit there. Short sales let realtors price to sell, which puts a lot more money in their pockets.

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Finally, *the community* benefits. Why would a community benefit from investors doing short sales? Well, short sales allow you to buy, renovate, and sell properties at reasonable, marketable prices. Without short sales, and with credit as tight as it is right now, many houses won't sell. Investors won't want them, and many families won't be able to get loans to buy them.

A house that doesn't sell eventually winds up abandoned. Abandonment drives down property values even further, leading to more houses that don't sell, and more vacant houses. Short sales can help correct market imbalances. And that's a win for everyone.

If you haven't tried short sales before, now is the time. If you don't learn how to do short sales now, you'll soon find yourself at a serious competitive disadvantage as more and more debt-heavy properties wind up on the market. After all, *somebody* is going to buy Aunt Mildred's ugly green flower pot and sell it at a profit. Why shouldn't it be you?

Don DeRosa *was recognized as one of the nation's top 21 real estate investors in the New York Times bestseller The Millionaire Real Estate Investor. Don, who is a full-time investor, trainer, and mentor, can be contacted at don@donderosa.com.*

Synopsis: As realtors and banks cope with an ever increasing inventory of homes, more and more conventional realtors are learning how to do short sales. Short sales help sellers, investors, realtors, and even the neighborhood by preventing foreclosure. Investors would be wise to get on the bandwagon to learn how to negotiate and manage these important transactions.