

The steps of buying a bank-owned property are very different than what you may have experienced in a typical property sale. The following is an overview of the variations and what you, as an REO buyer, should expect of the process.

Buying a Bank-Owned Property (REO)

Buying a bank-owned property may be an opportunity to buy a home for less money, and with some sweat equity, owning a home that you might otherwise not be able to afford. Many investors are reaping the benefits of the increased foreclosure rate, buying REOs and either flipping them, or using them as rental properties. We believe it is important that the buyer of REOs recognize that the process, the parties involved, and the governing documents are considerably different than what you may have experienced with a typical retail sale. We recommend that buyers of REO properties work with real estate agents experienced in the REO process. By understanding the process, the REO buyer will have adjusted expectations thereby reducing the involved stress, and greatly increasing your odds of completing a successful transaction.

What is an REO?

REO stands for Real Estate Owned. What this means is that a previous homeowner defaulted on his mortgage, the bank ultimately took possession of the home and now has the home listed for sale in an effort to liquidate the loss. This process is frequently managed by a company or subsidiary of the mortgage company whose sole purpose is to minimize the loss.

How are REO Purchases Different?

The sale of an REO property is much different than a typical retail sale. In the case of an REO sale, the seller calls all the shots. Frequently, terms normally included in the normal Offer to Purchase will be deleted. In all cases, the terms dictated by the REO seller will supersede the buyers' offer.

Typically, an REO is sold in "as-is" condition. The buyer should consider the value of the property with "what you see is what your get" mentality. The buyers' formula should be:

(A) Sales Price + (B) Anticipated Expense of Repairs/Upgrades = (C)
Desired Value Home

Many people have the misunderstanding that the sales price of REO homes reflects a home in first-rate condition, and that offers should be drastically low to compensate for the “scratch and dent” condition of typical REOs. The reality is that prior to listing the home for sale, sellers have already had several appraisals and at least two different Broker Price Opinions establishing its current value in its current condition.

Understanding the REO Process

The Listing Agent (REO Broker) is simply a conduit between the Buyer’s agent and the Seller. The Listing Agent does not have any power to say what the terms are, and has little or no negotiating power or influence.

The Seller will not normally negotiate after they accept your offer. All terms should be negotiated prior to acceptance to minimize problems during escrow.

Does “as is” mean that inspections are not allowed? No. Typically, the buyer has the option when making the offer to indicate if they intend to have inspections done. Though the Seller does not have an obligation to entertain any repair request, the buyer will typically be allowed to perform an inspection within a specified period of time (typically 10 days). If the buyer finds something wrong, they have the right to cancel the contract and receive their deposit back if they do so within this inspection contingency period. Seller will not pay for any inspections. Some Sellers (not all) will provide utilities for inspections. Inasmuch as buyers need to de-winterize a home to perform inspections, the Seller may require the buyer to re-winterize the property.

Will the Seller pay and arrange for termite inspections? No. If a termite inspection is a lender requirement, then you should expect to order and pay for that inspection. The same goes for any other lender required inspections. If the property shows evidence of infestation, your lender may have a stipulation that it be corrected prior to closing. Be aware that you will be responsible for paying for the correction, not the bank. We suggest that the termite inspection be done well within your contingency period to determine your obligations.

Can the Buyer cancel if they find something wrong? The buyer has the right to cancel the contract and receive their deposit back *if they do so within their contractual time.*

Pre-Approval and/or Proof of Funds are required. The loan process should be started prior to making the offer. A pre-approval letter from your lender, or a proof of funds statement from your banker are typically required to even present the offer to the Seller. In many cases, the Seller may require that their mortgage lending affiliate must interview and pre-approve the buyer (even though it is still

the buyer's decision where they will get their loan). Make sure your real estate agent checks with the REO broker for any special requirement prior to making an offer.

FHA / VA Financing. FHA/VA offers present obvious problems when associated with "as-is" property sales. It is rare that a bank will accept an FHA or VA offer; and often time will accept the offer only with the understanding that the buyer will be responsible for any lender required inspections. An option you may want to discuss with your mortgage lender is a 203K FHA loan, a loan which includes money to renovate the property

Is there information regarding the history of the property available? No. Neither the Seller nor the REO Agent has any information from the previous owner of the property. This is why REO transactions are exempt from the property disclosure form typically involved in the real estate transaction.

How soon will the Seller respond? The REO Agent has no control over the bank's decision-making process. On rare occasions they will respond within 48 hours, however, more than likely, they will respond in 3 to 5 days.

Multiple Offers. Frequently, the bank does not accept any offers for the first several days the property is on the market. For a desirable property, this may result in multiple offers being submitted at once. When there are multiple offers, the bank will typically counter with "highest and best". To the buyer, this means to come back with the most you are willing to offer. The bank will choose which buyer's offer to accept, or which buyer to continue negotiating with.

How will Sellers Respond? The Seller will communicate acceptance to the REO Agent, and the immediate acceptance will typically be verbal (or communicated by email). In the short term, you will receive a Seller's Counter Offer, which outlines the acceptance of the basic terms as discussed, along with variations and details of the Seller's acceptance. It is very important to read and understand this document prior to acceptance; remember, the Seller's Counter Offer supersedes the original Offer to purchase. These are forms generated by the bank's Asset Manager or the outsource company (and often come to the Listing Agent as an email attachment).

So the Acceptance is a Verbal Agreement? Once you are informed that your offer is accepted, it is. REO departments and Asset Managers give the "ok" and then go to their managers for signatures. We realize this is an unusual business practice to agree to offers orally, but the banks have their own way of doing business, and are in the driver's seat of the transaction.

Time Frames? Generally you will have 30 – 45 days from mutual acceptance (even if verbal) to close the transaction. The closing date on the Seller's Counteroffer supersedes the closing date in the Offer to Purchase. It is important

that Buyers have a clear understanding from their mortgage lenders regarding the ability to meet the closing deadlines. Given the current market conditions, it has been our experience that loan underwriting is taking longer. Read the Bank Addendum carefully—*there is often a per diem late fee assessed for tardy closings.*

Will the Seller accept Contingent Sales? No. If the bank accepts a buyers offer and then finds out that the buyer really does need to sell a home in order to purchase (and you haven't disclosed that), the sale will be immediately cancelled and the buyer will lose their earnest money deposit.

In Summary

With foreclosure on the rise across the nation, purchasing REO properties may offer an opportunity for investors and home buyers to buy and own a property resulting in a significant savings from buying in the typical retail market. The processes involved in purchasing an REO home are unique, and best managed under the direction of real estate agents who have experience in the REO field. As REO Agents representing Bank Sellers, our team includes agents who have the expertise to work with REO buyers. If you have any questions regarding the process, we invite you to call us at (336) 553-0444.