“BUYER'S GUIDE TO BUYING A BANK-OWNED OR FORECLOSURE PROPERTY”

In today's market, nearly four out of every five homes sold are bank-owned foreclosure properties. These are commonly referred to as Real Estate Owned (REO) properties

Buying an REO property is very different than a traditional buyer/seller transaction. The process is much more taxing and several more entities are involved in the REO transaction. This can create more time and challenges.

Many REO homebuyers, especially those buying a home for the first time or their first bank-owned property, get frustrated during the process.

Since the REO phenomenon started dominating sales, not coincidently, customer service scores in title, escrow, lending and real estate have plummeted.

Together with my team, I have developed this short, simplified guide to better help our clients understand the REO transaction process. We hope you will share this with your teams and buyers.

While this guide will not change the way the transaction occurs, it may help set more reasonable expectations upfront and eliminate some surprises.

Buying an REO is a great way to save money and get a fantastic deal. Just be prepared for the uniqueness of the process.

What is an REO or bank-owned property?

A property acquired in foreclosure and now owned by the bank that foreclosed on the property is called an REO or bank-owned property.

How did this property become an REO?

The last owner of this home was not able the mortgage payments. The mortgage note holder seized the property and evicted the owner. The bank attempted to auction the property and pay off the existing liens and mortgages. If that was not successful, the bank was then deeded the property by the Trustee. It is now an REO property.

How do banks sell REO properties?

The banks are not in the real estate holding business so they must sell these homes and turn them into cash. Because most foreclosed properties are not successful at auction, REO properties have flooded the market.

In any market, if there is oversupply, the property values depreciate. Because of the depreciated market, the banks are going to take, in most cases, a substantial loss on the property.

The banks have independent, professional real estate agents that assist them is marketing and selling their REO inventory. The banks also assign asset managers who work closely with these agents.

How do banks price their REO properties?

When a bank takes over a property, they conduct their own due diligence to get an accurate idea of the value of the home.

They hire a team of people to assess the current market value of the property through Real Estate Broker Price Opinions (BPO) and, in some cases, full property appraisals.

Based on these findings, they typically price the home within 10% of the current market value. There are always exceptions.

Banks are in business to make money. If they cannot make money, they need to minimize their losses. Banks are looking for a certain "net amount" on each particular property. This "net amount" is based on their research of the current market value minus costs associated with the property. They have priced the home sell quickly but as close to market price as possible.

Many buyers make the mistake of thinking the bank is desperate to get rid of the property. They believe they can submit a low-ball offer and expect to get an acceptance or at least a counter-offer. Think again! Low-ball offers (below 10% of list price) are not typically taken seriously. They may be a waste of your time and your agent's. Worse yet, you may be perceived as an illegitimate buyer. Banks own many homes in the same area, and they use many of the same agents, so this could adversely affect future offers you make on other properties owned by the same bank or listed with the same agents.

Be reasonable. Do your research with your agent and determine what the home is really worth. Make your offer according to the home's value, not to list price.

There are stories of buyers making tens of offers and not having a single one accepted. By making offers based on the home's true value and not what it's listed for, you can mostly avoid this challenge.

How do I find an REO property?

There are thousands of REO properties in our market. There is only one way to effectively research them all in a timely manner...hire a professional real estate agent. The seller, upon the successful completion of the transaction, typically pays for the buyer's agent commission. This will cost you nothing, but may save you tens of thousands.

Are REO properties damaged?

Some are. Many are not. It is important to inspect the home yourself before making an offer. Once you have viewed the property, consult with your lender about the damage the home has, if any.

It is equally important to have a professional home inspector inspect the property before you commit to purchasing it. Your real estate professional will refer you to a top quality home inspector. When the inspection is complete, your lender will likely want to review a copy of it. They do this to protect you and their loan collateral, your new home.

Many loan programs will require repairs to be completed before you close escrow. If you do not have the money to do this and the selling bank is not willing to make these repairs, you may need to find another home.

What does "As-Is" mean?

Nearly every bank-owned property today is sold "as is." You will have to sign a waiver that states you are willing to accept the home in the condition it's in with no further repair.

If a bank is marketing their home "as is", there is a possibility that the home needs repair and they are not willing to make them. Have your Real Estate Professional give you a thorough run down on what "as is" means to you during a transaction and once you have closed on the property. In addition, consult with your lender before making an offer on an "as is" home. Not all loan programs will allow you to buy a home that needs substantial repairs.

I am ready to buy an REO property, what do I need to do to get pre-qualified?

If you make an offer on a bank-owned property, they may require you to be pre-qualified with a home loan consultant from their own bank. They do this for two reasons; assurances and opportunities.

They want assurances that you are truly qualified to make an offer. While you may be pre-qualified by another lender, they will still want to review your credit, income and asset scenario in their own systems to make sure they are selling the home to a truly qualified buyer.

It is not negotiable in most cases and most banks will not consider your offer without a pre-qualification letter from their own institution.

This is legal for them to do this. However, you are not required to use this bank for your new mortgage loan; you just need to be pre-qualified through them. You can use whichever lender you choose for your actual purchase.

If you don't want to be pre-qualified through numerous lenders, you may want to reconsider making offers on bank-owned properties or ask your agent to narrow your search to banks without this requirement.

The banks also want to create a business relationship opportunity with you, as well as your agent.

Do not let this mandatory pre-qualification discourage you. This is truly in your best interest. Many times, the Home Loan Consultants from these banks have been authorized to offer steep discounts and other incentives if you proceed with a loan from their bank. It certainly doesn't hurt to have multiple lenders competing for your business.

In many cases, the bank is taking heavy losses on the property. If they can recapture the mortgage loan, at least it is not a complete loss. This creates an opportunity to parlay the great deal you got on the home with a great deal on your mortgage as well.

I am pre-qualified and ready to make an offer. What is next?

Your offer is submitted to the listing agent. The listing agent may have to submit to the Asset Manager, who works for the bank, and this is where the negotiation happens. It may take a few days for a response. Be patient. Do not bother writing in a short deadline for the seller to respond. They may not pay attention to it.

The bank will likely respond in the first 48 hours. Some banks take 3 - 5 business days. Once again, be patient. This is not your regular seller.

You will not get a response over the weekend or holidays. All offers submitted over the weekend will be presented the following business day.

As a rule of thumb, REO listing agents will tell you if you make an offer and do not hear back within five business days, the offer has been rejected. Do not wait around for the rejection or the counter. It may never come. Come back with a better offer or find another property.

What does bring my "highest and best offer" mean?

Because the homes are priced so well, it is very common for the bank to get multiple offers.

If the bank gets multiple offers, instead of making a counter proposal to you, they may go back to all of the potential buyers and ask for each buyer's highest and best offer.

This means come back with your best offer, as the bank will choose one at this point. In many cases, the bank will not return counter-offers after they have requested this.

If you are presented with this opportunity, it means you are in the running. You now have one more opportunity to increase the price or better the terms of your offer. You can choose to do nothing at this point but it may not get you anywhere.

Meet with your agent. Determine the true value of the home. Review your down payment, closing costs needs, and loan terms and then come back with your best shot.

I made a list price offer but they didn't respond. Why?

Many REO properties, especially those listed below market value receive multiple offers. Some houses sell above list price. The bank is like any other seller in the market. They can choose not to accept your offer if one comes in they think is better than yours.

If you offer list price and ask for your closing costs to be paid and another buyer offers list price and doesn't seek closing costs, the other buyer's offer is stronger.

How long will it take to complete my transaction and move into my property?

Traditionally, buyer and seller contracts are 30 days. However, this is not a traditional buyer/seller transaction. In today's REO property market, many buyers feel more comfortable with 45-day closings. Many banks have late fees of $100 or more per day past the contracted close of escrow date. These fees add up quickly so it is important to understand what problems can arise that may make you late.

What can make me late?

Aside from the regular loan process, which sometimes takes longer in today's stricter lending environment, there are many challenges unique to REO properties.

When the previous owner of your new home was foreclosed on and the bank took possession, a "Trustee's Deed" was issued in the bank's name. If this process is not executed properly, it may cause delays when the county is trying to record the deed into your name. There is little that you can do about this except wait until it is corrected. I have seen this issue take between one day to seven weeks to resolve.

If a Home Owner's Association (HOA) manages the community, your title company will request an HOA demand on the property. This demand will ensure that the bank pays any association fees and fines at close of escrow. If they are not paid at closing, they will transfer with the property into your name and will then be your responsibility.

It's pretty likely that there hasn't been an actual person living in this home in sometime. This means the home has not been kept. There may be a lot of fines (landscaping, upkeep, trash, etc.) levied from the HOA.

This can take time and be complicated but is necessary that it is done and done correctly. For more details, ask your escrow officer. It's their responsibility to get this resolved.

For the most part, if the close of escrow is delayed by problems that are out of your control, the bank should not penalize you. Just be sure to do your part in a timely manner, and you should be ok.

I am in escrow and we discovered a bunch of repairs that need to be made to the home...what do I do now?

Many people that have lost their homes to foreclosure have been struggling financially. This usually means the home has not been kept properly and is in need of repairs and general maintenance. Other homeowners, once they know they are losing their home, damage the property purposely.

When buying an REO property, you must be prepared to do some repairs. Banks may not agree to make these repairs. They may not pay for these repairs. This may require out-of-pocket expense for you.

They may be willing to help with some, but don't plan on it. Know what you are buying before you make your offer and be prepared to spend some money for repairs before you move in.

In most contracts, you can back out of the purchase if you find problems with the property or in loan qualifying in a certain time period. This is called the due-diligence period.

Make sure you know how long this due diligence period is when entering into a contract. Complete all inspections within that period so you can make an informed decision on whether or not to proceed with the purchase. It is important to respect these deadlines because they are strictly enforced.

Some repairs will be obvious when you visit the property. Others may be identified during the property inspection and the appraisal process. The inspector will identify repairs issues and may be able to give you a written estimate of the cost to repair the property. In some cases, an appraiser may also call for repairs to the property to bring it up to livable or safe condition.

Identify these issues quickly so you know what you are facing and have the opportunity to cancel if necessary. Again, this will help protect your deposit money.

You will want to be cautious buying a bank-owned property if you barely have enough money for the down payment and closing costs unless you have arranged for repairs with the seller.

I have signed my loan docs and I am still waiting for my keys. What is taking so long?

Just like you executed many documents at your loan signing, the seller has a stack of closing documents to sign as well. Remember, the seller of your home is a bank or some other financial institution. It may take the representative who is authorized to sign off on these documents days or even weeks to get around to it. Your trusted and skilled escrow officer will make sure to stay on this for you.

So, there you have it. Complicated? Yes. Frustrating? Sometimes. Time-consuming? Quite often.

At the end of the day, hopefully, you are getting a new home for you and/or your family at a much-discounted price so it will all be worth it.

The best tip we can give you is to remain positive and be patient. Expect the challenges. There will likely be some. Together with your professional real estate agent and experienced escrow officer, we will all do our very best to get you through it successfully.