Acquiring Bank Owned Foreclosures

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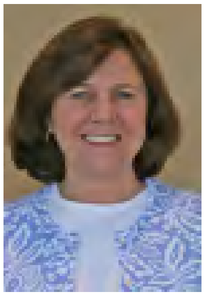

When a homeowner loses their house to foreclosure, there is a public auction. If no one bids high enough to pay the lender the amount of the first mortgage, the lender takes the property back. A deed is filed in the bank's name and the home is vacated. The home is now known as "real estate owned" or REO.

In some cases the bank held this property in its portfolio and is the full owner but most of the time the banks are the servicer of the loan and they own the property on behalf of the entity that purchased the mortgage in the secondary mortgage market. The bank transfers management of the property to its REO department. All banks treat REO's in their own manner but there are some common elements. Most banks want to sell these properties to make back their loss. Since they are not set up to actively market, manage, and show the properties, they will assign the homes to large real estate brokers who are responsible for listing, selling and even maintaining the properties.

Most banks have a website where these homes can be viewed. The contact for interested purchasers is the realtor who has the listing. If properties do not sell in a given timeframe, 90 days for example, they will take it off the market and put it into a bulk portfolio to market to investors. Realtors are obligated to present all offers to the banks. The banks usually do not counter back with anything less than the offering price. This can be frustrating for nonprofits or investors who want to acquire the properties. The investors know that the selling amount is higher than the actual market value. For a time, the banks do not want to show the considerable losses in the properties by selling short, so they stick to their offering price. But frequently they will decide to sell off the property more rapidly and will entertain lower offers.

The following points are a guide to further navigating the process of acquiring REO properties.

1. Identification of Properties. Where do you find REO's?

- **a.** Multiple Listing Service. Find a good realtor to identify listings.
- **b.** Bank REO websites. View the various lenders websites to see what is listed.
  Example: ***www.bankofamerica.reo.com***

c. Florida Housing Coalition Assistance. The Coalition is working with lenders to identify properties that are within the affordable range. It may be possible to consider bulk portfolios before they are listed with realtors.

2. Consider your list. You now have a list of potential properties- start with about ten or twenty.

a. Physically visit the homes. Take a contractor to examine the condition of the building and grounds. Try to get access to the inside- if you cannot get inside, cross it off the list. If the area is somewhere your buyers won't want to live, cross it off the list.

b. Get real prices from the contractor for all of the items that need to be repaired, completed or replaced- many times homes will have been vandalized, neglected, or robbed. Check carefully for mold and the condition of the septic system. If mold is present, you may want to walk away. During vacancy, septic systems can become damaged by tree roots so check this carefully.

c. Consider other costs to carry the property, including liability insurance, taxes, financing costs, legal costs, your labor costs to view the property and work up the analysis. Consider your development fee that will compensate your organization for this activity. You are providing a construction supervisor and coordinating all of the work for this house.

d. Liability Insurance. A major pitfall is the cost to provide insurance while the nonprofit owns the home- this can be costly. Work with your insurers to find a reasonable policy.

e. Permits. Check with the building department to make sure there is a final certificate of occupancy on the home. This is essential!

f. Check other public records for liens. You will be getting title insurance but it's a good idea to see what is lurking with the title.

g. Gather warranty information on systems- AC, structure, appliances. If this is a new home abandoned by the builder, many times there are warranties in place. If the builder is local, contact the company.

h. Many times there will be no appliances and the AC will have been stolen.

i. There will be other due diligence items to go further with just before you make an offer (ie, another visit inside).

3. Negotiate a Purchase Price. Once you know how much money you need to put in for rehab, closing costs, insurance, financial costs, you will know what you can offer. Go in low. They may counter back with exactly what they have it listed for. They may not even respond to you. Keep trying and be persistent with your offer. Let the seller know of damage or deterioration that detracts from the value that should be reduced from the price. Make your offer with a traditional FAR-BAR purchase contract. You will need to have a 30 day closing. A typical deposit is $2,500. You are buying the home AS IS. Leave a 3 day acceptance period from your deposit date to clear. Try to get inside again during the 3 day period to make sure everything is still as you thought.

4. Closing Pitfalls. You now have an offer made with a cash earnest deposit with people you may not even know. They may be in a large city in another state or even in a foreign country. This is an unnerving time. You are dealing with a title company and bank you don't know. You place calls and no one answers. That is why you need to be very careful about who you are dealing with. Try to have a solid contact person that is reliable.

5. Hard Money Stage. When you have your buyer qualified, you purchase the home. You are waiting for the title policy- the seller should be paying for this. Foreclosure is supposed to clear off the title but you need to be ready to review for the odd lien that survived foreclosure. This is where you need an equity line to draw from- this will be further covered in the financial items. Your nonprofit will own the home for a short period of time before you resell it to the homeowner. Normally nonprofits are advised not to speculate and purchase properties before they have buyers. This is not that market. You should do everything you can to be confident you have willing and able buyers. You should not enter a contract with your buyer until you hold title to the property. There are other ways to do it, but this is a simple framework. This allows you to add on all of your carrying costs and development fee before selling to the end user. Of course you need to ensure the purchase price remains affordable and competitive with the current market.

6. Appraisals. If you are using the NSP program you will be required to have an appraisal that is less than 60 days old. Your buyer will also need to get an appraisal prior to purchase. You are buying based on what works for you and your buyer. Be aware that the appraisal value may be less than your costs. If this is the case, the financing will need to have non-secured funding for a portion of the cost.

Members of Polk County, City of Lakeland and Keystone Challenge Fund staff discuss NSP strategies and challenges with Stan Fitterman and Gladys Schneider.

7. Once you hold title you should turn on the power. This will enable other systems to be further inspected that you could not when it was an REO. Yes this sounds risky, but there will not be power on in the homes when you first inspect them. That is why you need a good contractor to examine everything as carefully as possible.

8. Your buyer. By this time, your buyer should have visited the home. You are selling them the home not as someone else's discard, but as a new home they can be proud of. These are the steps they need to have completed.

- **a.** Income qualified
- **b.** Homebuyer training
- **c.** They visited the home and want to buy it
- **d.** Qualified for their mortgage
- **e.** Subsidies applied for and approved - per program requirements

9. Are you selling the home AS IS? No! You are selling a new or used home that is in good working order. You can purchase a homeowner warranty (HOW) for about $375 to cover the big items- trusses, structure, etc. This provides comfort and security for the buyer. If you bought new appliances, you will have those warranties in place. Along with the HOW warranty and the appliances warranty, you should also provide a blanket one year warranty to cover other items not covered by the other warranties. A good business practice would be to have a $2,000 reserve from the purchase proceeds that will be there for any repairs that are needed in the first year. (HOW - NAHB Homebuyer Warranty- $375)

10. All legal matters of the home- permits, code liens, assessments, other liens- have been cleared up. You are selling the home with clear title.

11. Financing. As a nonprofit, you need capital to make the initial purchase of the home. Many SHIP programs discourage such speculation and they are set up to reimburse nonprofits after they have purchased land or homes. In this case, there is a need for a revolving line of credit with little or no interest that non-profits can use to purchase the home. The line of credit would be repaid with each sale to the end user. There is and will be debate about having a pool of funding for this purpose. Various requirements could be placed on such a pool. One would be a resale requirement that homes are to remain affordable. Another suggestion would limit the number of units that could be outstanding before more funds could be drawn down. This would ensure that the fund revolves.

12. Know your numbers. Your organization has a mission and it has a fiduciary responsibility. This is a new business line for many. It is essential that adequate analysis be done up front to determine what the carrying costs are for acquiring and rehabilitating homes. A suitable developer fee is appropriate and can be used to cover these costs and keep the organization afloat. Remember, just because something is inexpensive, doesn't mean it's a good deal.

13. This is a summary of what you need to Acquire Bank Owned Foreclosures:

- **a.** Your Team- elements include: homebuyer outreach, home inspector, contractor, construction supervisor, supportive county or city SHIP policies and funding, a cooperative permanent lender, a title company you can trust, good legal counsel to assist with FAR BAR contracts. Plus you need basic organizational capacity- leadership, financial systems, staffing.
- **b.** You must understand how to inspect a home and determine its rehabilitation needs. This includes codes, costs and carrying out the work. If projected costs make the deal infeasible, be ready to walk away.

c. Multiple or Volume approach. You need to gear up to be able to work on several homes at a time. Doing them one at a time will not be efficient.

d. Line of Credit- you need some type of below market rate funding that is easy to draw down. Federal funds for foreclosure acquisition are approved and will be available in many areas. A faster closing date may get a better price.

e. Ready buyers with subsidy. This means income eligible, counseling completed and a demonstrated desire to buy the home.

f. Sensible appraisals- the first mortgage needs to be based on an appraisal that reflects the replacement cost of the unit, not the unstable market conditions we have become accustomed to.

14. Timeframe. Here is an idea of the timing for this activity:

Search for Properties	Price Evaluation and Negotiation	Closing with Seller	Preparing Buyer and Rehab of House	Closing with Buyer
60-90 days	60 days	30 days	45 days	45 days

The Florida Housing Coalition Work

The Florida Housing Coalition is providing workshop training and on-site technical assistance on the Neighborhood Stabilization Program thanks to funding support provided by the Bank of America Foundation. The Coalition has provided on-site strategic planning for Jacksonville, Tampa, Hillsborough, Polk County-Lakeland, Ft. Myers-Lee County, Palm Beach County Community Land Trust Collaborative, Orlando, and Miami-Dade. Two workshops were held in October both of which were over-subscribed due to high demand for this training. The Coalition is currently discussing the possibility of providing additional technical assistance through the Florida Department of Community Affairs for those communities whose NSP funding will come from that department.

The 48 entitlement communities receiving direct allocations from HUD face a tight deadline to complete a substantial amendment to their Consolidated Plans detailing their intentions to expend over $450 million in Housing and Economic Recovery Act funds. After a fifteen day public participation requirement the plans are due to Jacksonville HUD by December 1. If plans are approved, funding could be available as early as January 15, 2009. The Florida Department of Community Affairs statewide plan for its portion of the HERA dollars, just over $91 million, is under the same timeframe although communities wishing to participate will submit their proposals directly to DCA. DCA has already held two workshops seeking input for the state plan. DCA will administer that portion of the NSP for entitlement and non-entitlement communities that did not meet threshold allocation formulas over $2 million. Based on foreclosure risk data, the DCA plan will allocate funding to these communities.

In its strategic planning sessions with targeted areas, the Coalition has outlined the issues and opportunities presented by the NSP program, including eligible activities, target areas, and data needs. A basic question revolves around who will administer the program and conduct the actual purchases. Some are persuaded the local government can secure the best discounts for the acquisitions and some are delegating to nonprofit partners. Others are considering the use of purchase assistance allowing the homebuyers to locate and negotiate a purchase for bank owned properties. Perhaps the most feasible for most is the delegation to sub-recipients, or those nonprofit partners who possess the capacity for transitioning their business line to that of acquisition-rehabilitation. The underlying question for all of the homeownership options is the availability of buyers in the current market and their access to financing for permanent mortgages.

Since a minimum of 25 percent of the NSP funds must be reserved for households below 50 percent of the area median income, most communities are providing rental and supportive housing strategies. There will be program income and resale obligations which have been discussed at the Coalition's workshops and strategic planning sessions. Since the maximum income level for the program is 120 percent of the area median, there is an opportunity for mixed income in both the ownership and rental strategies. This will also allow for targeting in areas that may not be the typical CDBG blighted areas, but newer single family subdivisions that have a high rate of sub-prime lending and risk of foreclosure. There were many questions and discussions about the available data and its sources. Communities are tasked by HUD to select areas that have

Gladys Schneider provides on-site NSP strategic planning assistance to the Lee County Coalition of Affordable Housing Providers.

the greatest risk and incidence of foreclosure so that the program funds will be most effective in stabilizing these neighborhoods with occupied homes and an infusion of construction dollars.

The Coalition is working with communities and workshop participants to sort through the issues and opportunities presented by the NSP program. The Coalition will be focusing primarily on implementation of the strategies through building the capacity of nonprofit partners who are sub-recipients of the funding. This is where strategic planning is essential to ensure that the homes proposed for acquisition are inspected and evaluated for not only current market appraised value, but also the condition of the home, location, and the ability of buyers to meet stronger credit requirements to qualify for a mortgage. It is evident that many of the homes will need to be rented prior to sale. Both acquisition-rehab and scattered site rental property management are new business lines for most of Florida's nonprofits. The Coalition will emphasize the retooling of skill sets to be able to not only navigate the purchase, but to rehabilitate the homes, and sell or lease them while preparing to manage them for an indefinite period.

At no time has housing had a national spotlight such as this and it is the responsibility of the Coalition and all its members to implement the Neighborhood Stabilization Program successfully to help bring economic life back to shuttered and overgrown home sites and their surrounding environment. All funds must be obligated by June 30, 2010. For technical assistance, contact the Florida Housing Coalition at 850-878-4219 or email info@flhousing.org. Visit our website at ***www.flhousing.org*** and click on the NSP link to view current information on the program.

Bank of America Foundation Sponsors FHC Foreclosure Recovery Work

The Florida Housing Coalition has held workshops, strategic planning meetings and site visits across Florida. Under the Catalyst program a workshop was held in Sarasota focusing on developing strategies under the SHIP program for recovering foreclosure affected houses for use in affordable housing programs. Two Bank of America sponsored workshops were held, in Ft. Myers and Plantation, on neighborhood stabilization through the acquisition of foreclosed properties. Strategic planning meetings were held in Jacksonville, Tampa, Hillsborough County, Polk County/Lakeland, Lee County-Ft. Myers, Orlando, Palm Beach County, and Miami-Dade.

The strategic planning meetings have been attended by local governments who are HUD NSP grantees, partnering nonprofit organizations and lenders. The workshops and planning meetings have emphasized the implementation of the NSP program from targeting, to acquisition strategies, rehabilitation, land banking, community land trusts, and working with the buyer or renter of the properties. The Coalition has clarified many elements of the NSP program and provided examples of funding the strategies and rehabilitation budgets. The overall intent has been to ensure that local governments and their partnering nonprofit organizations have the capacity for unique acquisition opportunities, conducting rehabilitation on pre-owned homes, and managing scattered site rental housing. The Coalition is available for on-site strategic planning meetings. Contact us to discuss this opportunity further.