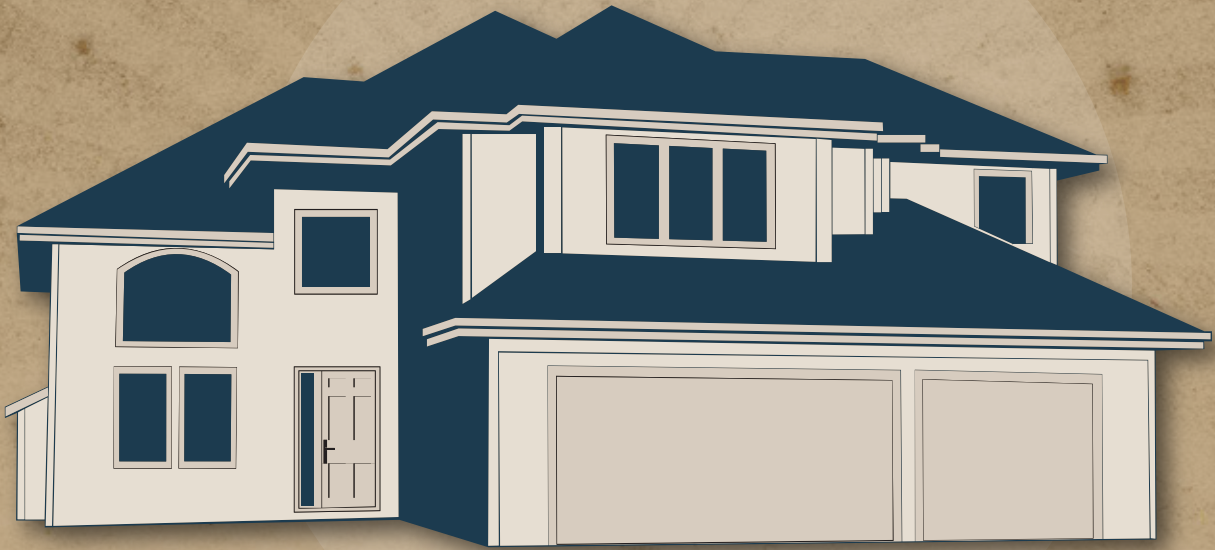


Understanding *Foreclosures & Short Sales*



A guide to buying with a VA Loan

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Introduction

The housing bubble has burst. Home prices and interest rates are hovering at record lows, and the market's few buyers all want to land the housing deal of a lifetime.

Foreclosures and short sale properties can offer some of the best deals to available buyers. But the process can be confusing, particularly for non-cash buyers.

The good news is that purchasing a distressed property with a VA loan is certainly possible. Knowledge, patience and persistence are key attributes for veterans and military families hoping to take advantage of rock-bottom home values and a glut of foreclosures nationwide.



Reasons to consider a distressed property ...

1. Price

Many foreclosure and short sale properties sell at big discounts, making them hot targets for cash-conscious buyers. Bank-owned foreclosures sold at an average discount of 36 percent in 2010, while short sale properties sold at an average discount of 15 percent, according to a RealtyTrac report.

Average Sales Price for U.S. Homes: Foreclosure vs. Traditional Sales

	Traditional Sales Price	Foreclosure Sales Price (includes both short sales and foreclosure sales)
Dec 2010	\$246,480	\$179,797
Jan 2011	\$231,946	\$162,779
Feb 2011	\$230,267	\$163,802
Mar 2011	\$228,396	\$161,964
Apr 2011	\$227,379	\$158,275
May 2011	\$231,434	\$159,193
June 2011	\$239,577	\$163,700
July 2011	\$243,251	\$164,485
Aug 2011	\$239,378	\$160,890
Sep 2011	\$235,475	\$164,313a
Oct 2011	\$230,879	\$164,379
Nov 2011	\$230,741	\$169,451

Source: RealtyTrac

Why are distressed properties so inexpensive?

Foreclosures and short sales slide to the bottom of the market for several reasons. Let's take a closer look at why it's easy to find a great deal on a distressed property.

"As is" condition

When a bank forecloses on a home, the previous owners are forced out. But foreclosure is a lengthy process, which gives the owners lots of time to get angry. Some owners take their frustration out on the home itself. Others may be facing a barrage of financial challenges and simply don't have the cash to maintain the home during the foreclosure process. It's typical for distressed properties to be in relatively poor condition and to be sold "as is," meaning that no improvements will be made by the current owner.

Owners want to sell NOW

Credit is tight and buyers are scarce. In a desperate attempt to grab those few buyers, owners of distressed properties frequently slash prices.

Fewer buyers available

When a homeowner is struggling to make payments, a fast sale is highly desirable. A quick short sale can help homeowners stave off foreclosure and its devastating effects. Properties that have already reached foreclosure and are under bank ownership also need to be unloaded as soon as possible. Banks are not designed to own and manage real estate, nor do they typically see any profit from foreclosure. After court fees, maintenance costs and the loss on a loan, lenders lose an estimated \$50,000 per foreclosure, according to a Joint Economic Committee of Congress report. Selling a property quickly helps lenders minimize this loss. Discounts help bring in buyers, so it's common to see comparatively low listing prices for distressed properties.



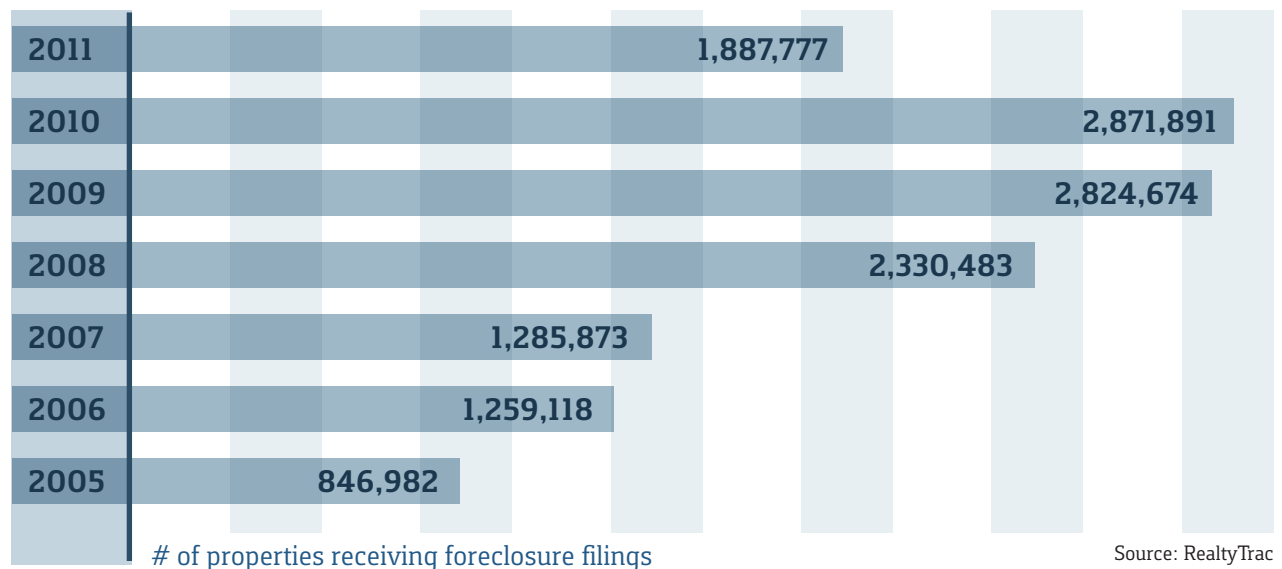
2. They're everywhere!

Distressed properties may be unavoidable in your home search. A RealtyTrac study found that one in every 69 U.S. housing units received at least one type of foreclosure filing during 2011. Foreclosure filings in 2011 actually reflected quite a slow-down from the 2010 record peak, due mainly to nationwide legal changes that have delayed final foreclosure proceedings. Industry experts anticipate a surge in foreclosure filings in 2012, as lenders satisfy the new legal requirements and begin pushing foreclosures through once again.

In some parts of the country, distressed properties constitute a clear majority of all residential sales. Nevada posted the largest percentage of distressed property sales in the second quarter of 2011, at a staggering 65 percent of total residential sales. Nationwide, 46 percent of homes sold in November 2011 were either short sales or foreclosure sales, according to a survey by Campbell/Inside Mortgage Finance.

U.S. Foreclosure Activity, 2005-2010

Total number of properties receiving foreclosure filings (default, foreclosure auction or bank repossessions)



3. Better chance of appreciation

A lower purchase price comes with a good shot at substantial appreciation. Buying a home at the bottom of the market gives buyers a great chance to reap future financial benefits.

2 Ways to Buy a Distressed Property with VA Financing

The easiest way to buy a distressed property is with cash. Sellers love the idea of a cash buyer who brings no lender restrictions or appraisal guidelines to the table. But not every service member can plop down \$50,000 to snatch up a foreclosure. VA loan borrowers can secure financing to snap up their own distressed properties, but the home must meet lender and VA guidelines. To purchase a distressed property, VA loan borrowers can pursue one of two channels: a short sale property or a bank-owned (REO) property.

1. Presale/short sale

A short sale can occur when a homeowner has missed mortgage payments and is in default. The bank has started foreclosure proceedings, but has not yet sold the home at public auction. During this limbo period known as pre-foreclosure, buyers can attempt to purchase the home from the current owner for less than what is owed on the home.

There's a catch to this process: All short sales have to be approved by the seller's lender. Lenders may decide that it makes more financial sense to foreclose on the home than to allow a short sale. Or the lender might agree to sell the home short of what is owed. Why would a lender agree to this?

Foreclosures are costly and time-consuming for lenders. A short sale cuts out legal and maintenance fees involved with foreclosure. If a home is undoubtedly headed toward foreclosure, lenders are usually willing to consider short sales as a cost-saving measure.

How to Buy a Short Sale

• Step 1: Find a property

The best way to find a short sale property is through a real estate agent. Agents can quickly sift through pre-foreclosure properties to find homes that meet your criteria. Short sale purchases can be challenging, so make sure that your agent has experience with distressed property sales. Your agent will need to negotiate with banks on your behalf, which is trickier than it sounds. Wading through layers of corporate gatekeepers to reach a decision-maker takes persistence and skill. Consult with an experienced agent for your best chance of success.

• Step 2: Make an offer

Remember that with a short sale, all offers have to be approved by the seller's lender. Your agent will help you create an attractive offer, which is first sent to the seller and the seller's agent. The seller's agent can preemptively accept or reject the offer. If an offer is accepted, it must then be sent to the lender for final approval.

• Step 3: Wait

There's a reason that short sales are nicknamed "long sales." After receiving an offer, lenders have to conduct an exhaustive review of the property, comparable sales and competing offers. According to Freddie Mac, this process can take weeks or months to complete. Patience is definitely a requirement for shoppers who pursue short sale properties.

2. Foreclosure/REO

Once a home has been foreclosed upon, it's offered for sale at public auction. Savvy buyers can pick up these homes at substantial discounts.

But VA loan borrowers usually can't buy properties at auction. Most foreclosure auctions require cash payment, eliminating buyers who need to borrow money for the purchase.

VA loan borrowers get their chance to buy after the auction is over and no one has bid enough to satisfy the lender. The property falls back into the lender's hands and is labeled an "REO," which is "real estate owned" by the bank. Financial institutions will either hire real estate agents or use internal staff to market and sell their REO properties.

How to Buy REOs

• Step 1: Find a property

Buyers should turn to real estate agents when hunting for any property. Agent assistance can be particularly valuable when searching for REOs.

Most agents can provide a comprehensive list of REOs in your area and price range. Agents can also quickly alert you to new foreclosure listings, which could be your best bet for scoring a great deal. Prospective buyers can also approach banks directly for a list of current REOs. Most large banks either maintain online REO databases or are willing to mail you a list of current REO properties. Even the VA acquires and offers REO properties. You can search the VA database at <http://va.equator.com>.

• Step 2: Make an offer

Lenders differ in the way they handle REO offers. Some lenders simply choose the best offer currently available. Others maintain a price threshold and offers below that price are discarded. Lenders who receive a flood of offers at once may ask buyers to resubmit their "best and final" offers to avoid tedious negotiations. Talk to your real estate agent about the best way to proceed.

• Step 3: Wait

Banks want to shuttle REO properties off their books as quickly as possible. Maintaining and marketing properties is costly business, so it's in a lender's best interest to sell fast. Compared to the weeks or months it can take to hear back on a short sale offer, REO offers usually get quick responses. Most lenders try to respond to REO offers within a week's time.

674 days:

Average time it took to resell a foreclosed property in the U.S. from the initial missed payment to the final foreclosure auction as of December 2011.

Source: LPS Applied Analytics

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Challenges of using a VA loan to purchase distressed properties

Buying any home can be complex. Adding poorly maintained homes and lender restrictions to the mix complicates the transaction even more. Before you approach the foreclosure market as a VA borrower, consider some of the challenges that may ahead.

Challenge 1: Home may not meet regulations

All homes purchased with a VA loan must undergo a VA appraisal, which in part ensures that homes measure up to the VA's Minimum Property Requirements (MPRs). MPRs are basic health and safety conditions that must be met for VA approval. Any conditions that violate the agency's MPRs will have to be repaired before the VA will allow the loan to close.

Many of these homes are not properly maintained and can't meet the property requirements. Traditional sellers are generally willing to make the improvements necessary to meet VA standards, but banks have other priorities. Banks want a quick, hassle-free sale, so they prefer to sell properties "as is."

TIPS:

• Choose homes in good condition

Don't set your sights on a fixer-upper in foreclosure. The VA appraisal will tear your homeowner dreams to shreds if you pursue a property in poor condition. Even though banks want to sell quickly, many won't make any repairs to their REOs. You may have more luck if your less-than-perfect home is a short sale property, as individual homeowners may be more willing to make needed improvements.

• Be realistic if you take a risk

Keep your expectations low if you've fallen in love with a wreck of a home. You can certainly ask a bank to perform necessary repairs, but be prepared for them to say no. Even if you're lucky enough to convince the bank to do repairs, they may not be immediate. Always have a back-up plan in case the sale falls through, and don't pursue foreclosures in poor condition if you're on a strict timeline.

A Snapshot of Some VA Minimum Property Requirements

- **Mechanical systems:** All of the home's major systems (heating, cooling, electrical) must be in safe working order.
- **Roof:** The home's roof must be free of any major defects.
- **Termites:** If the home is located in a termite-prone area, the VA will require a satisfactory pest inspection. If termites or other destructive insects are found, the home must be treated and re-evaluated.
- **Lead-based paint:** VA appraisers assume that paint problems (like chipping, cracking or peeling) at any property built before 1978 involve lead paint. Unless further tests can show acceptable lead levels, the surface has to either be repainted or reconstructed.



Challenge 2: Home's appraisal value may be too low

The VA appraiser will also calculate the value of the home you are considering. This value is extremely important in determining the success of your purchase, since a VA loan can't be issued for more than the appraised value. If the sales price is more than the appraisal value, you can either make up the difference in cash or ask the seller to lower the sales price.

\$190,000: Average sales price for REOs in move-in condition

\$99,000: Average sales price for damaged REOs

Source: Campbell/Inside Mortgage Finance, November 2011 Survey

The value of a distressed property can be tough to accurately assess. Appraisers generally use the sales of comparable properties to help calculate a home's value, so an excess of distressed property sales in the area could bring the value down.

Distressed homes that have not been properly maintained will also suffer during the appraisal. Imperfections such as leaky gutters, broken windows or badly damaged floors can send the appraised value plummeting. Once that appraised value sinks below the sales price, VA loan contenders are left with few options to complete the sale.

TIPS:

- **Ask your agent for a CMA before making an offer**

A good agent should have completed a Comparative Market Analysis (CMA) on the property before you made an offer. The CMA uses comparable sales and current listing prices to calculate a home's fair market value. The CMA is fairly similar to the appraisal and is a great way to establish value and flush out any problems that may arise during the upcoming appraisal.

- **Reconsideration of value**

If the appraised value comes in below the sales price, you can ask the VA for a reconsideration of value. The VA will be more likely to approve the request if the buyer can show that pertinent information was not used in the initial appraiser's report. It's important to know that a reconsideration of value is not a guarantee of a higher appraised value and may result in additional appraisal fees for the buyer.

- **Make up the difference in cash**

A buyer can choose to pay the gap between the appraised value and the sales price in cash. Obviously this is not an option (or a good idea) for all buyers. Paying above the appraised value may help you land a home but could be a poor use of your funds. Carefully assess how much a home is worth to you before casting out extra funds.

- **Don't buy in a neighborhood flooded with foreclosures**

An area rife with vacant homes and struggling homeowners can send home values into free fall. Seek neighborhood recommendations from your real estate agent, and focus your search on stable areas with well-maintained homes.



Challenge 3: Banks can be difficult to deal with

Buyers of distressed properties must get offer approval from the bank holding the property. Negotiating with a huge organization can be more difficult than working with one or two homeowners.

Although most banks now have entire departments devoted to REOs and short sales, getting a response from a bank can be tough. Considering that a large bank may be marketing thousands of REO properties on any given day, it's the patient buyer who ultimately lands a distressed property.

TIPS:

- **Make an attractive offer**

Many prospective buyers approach distressed property negotiations with the wrong attitude. The current market is tough for sellers, but that doesn't mean that any offer will be accepted. Banks don't like holding onto real estate, but they're not afraid to pass up a deal that doesn't make financial sense.

Low-ball offers and offers with tons of contingencies are frequently ignored by banks. This doesn't mean that you can't take a chance with a low offer. But realize that banks don't have time to negotiate with every person who wants to buy a cheap house. Your best bet for landing an REO home quickly is to make a fair offer with flexible terms. Do everything in your power to present yourself as a willing and qualified buyer, particularly when a property has multiple offers.

REO Offer Checklist

- **Include preapproval letter**

Banks want to be fairly certain that you'll qualify for financing before taking a chance on your offer. Send a preapproval letter with your offer.

Pullout: Get preapproved today with Veterans United. VeteransUnited.com or 800-884-5560.

- **Suggest a quick closing date**

Banks want to transfer ownership as soon as possible. Ask for a closing date within the next 30 days to get positive attention from the lender.

- **Make your offer contingent on a home inspection**

You want to be a trouble-free buyer, but don't agree to buy any home without a professional home inspection. Home inspections can reveal tons of costly problems that are invisible to the untrained eye. Move on if a bank refuses to permit the inspection or will only sell the home "as is".

- **Don't forget the VA appraisal**

When making an offer on an REO property, don't forget that the home will have to pass the VA appraisal. Any repairs needed to meet VA standards will have to be completed before the loan can close. Some banks are unwilling to do any repairs, while others are more flexible. If the bank refuses to complete any repairs, you'll either have to pay for the repairs yourself or walk away from the purchase. Figure in anticipated repair costs when making your initial offer.

- **Work with an experienced agent**

You don't want to give a newbie agent a trial run at the foreclosure market. Distressed property sales are quite different than traditional sales, with different tactical methods and title procedures. The best agents will have closed several recent foreclosure sales and have familiarity with the entire process.

- **Be a pest**

Getting a bank to respond to your individual offer takes special skill and lots of patience. Your agent will handle many of the negotiations, but don't hesitate to assert yourself. If you've made an offer on a distressed property, contact the bank's REO or short sale department and ask how offers are processed. Determine how long your wait should be, and don't hesitate to check back in if you aren't getting timely feedback. Sometimes the anxious bidder is able to urge the process along simply by making contact.

Conclusion

Today's real estate market is flooded with incredible deals for qualified buyers. Some of the market's best bargains can be found in distressed property listings, which sold at an average discount of 28 percent in 2010 (RealtyTrac).

Prospective buyers will have an even greater chance to purchase distressed properties in the coming months. Notices of default serve as the first stage of the foreclosure process and rose significantly in mid-2011. Many analysts predict that another wave of foreclosures will hit the market in 2012 as those properties in default are finally repossessed by lenders.

Completing a distressed property sale can certainly be difficult. Pursuing a foreclosure sale is not for those on a strict timeline or those who are easily frustrated. Buyers who can be flexible and persistent are the ultimate winners in the distressed property arena. These marathon shoppers are in prime position to secure great homes at rock-bottom prices.



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