
October 24, 2010

Short Sales Resisted as Foreclosures Are Revived

By MICHAEL POWELL

PHOENIX — Bank of America and GMAC are firing up their formidable foreclosure machines again today, after a brief pause.

But hard-pressed homeowners like Lydia Sweetland are asking why lenders often balk at a less disruptive solution: short sales, which allow owners to sell deeply devalued homes for less than what remains on their mortgage.

Ms. Sweetland, 47, tried such a sale this summer out of desperation. She had lost her high-paying job and drained her once-flush retirement savings, and her bank, GMAC, wouldn't modify her mortgage. After seven months of being unable to pay her mortgage, she decided that a short sale would give her more time to move out of her Phoenix home and damage her credit rating less than a foreclosure.

She owes $206,000 and found a buyer who would pay $200,000. Last Friday, GMAC rejected that offer and said it would foreclose in seven days, even though, according to Ms. Sweetland's broker, the bank estimates it will make $19,000 less on a foreclosure than on a short sale.

"I guess I could salute and say, 'O.K., I'm walking, here's the keys,' " says Ms. Sweetland, as she sits in a plastic Adirondack chair on her patio. "But I need a little time, and I don't want to just leave the house vacant. I loved this neighborhood."

GMAC declined to be interviewed about Ms. Sweetland's case.

The halt in most foreclosures the last few weeks gave a hint of hope to homeowners like Ms. Sweetland, who found breathing room to pursue alternatives. Consumer advocates took the view that this might pressure banks to offer mortgage modifications on better terms and perhaps drive interest in short sales, which are rising sharply in many corners of the nation.

But some major lenders took a quick inventory of their foreclosure practices and insisted their processes were sound. They now seem intent on resuming foreclosures. And that could have a profound effect on many homeowners.

In Arizona, thousands of homeowners have turned to short sales to avoid foreclosures, and many end up running a daunting procedural gantlet. Several of the largest lenders have set up complicated and balky application systems.

Concerns about fraud are one of the reasons lenders are so careful about short sales. Sometimes well-off homeowners want to portray their finances as dire and cut their losses on a property. In other instances, distressed homeowners try to make a short sale to a relative, who would then sell it back to them (a practice that is illegal). A recent industry report estimates that short sale fraud occurs in at least 2 percent of sales and costs banks about $300 million annually.

Short sales are also hindered when homeowners fail to forward the proper papers, have tax liens or cannot find a buyer.

Because of such concerns, homeowners often are instructed that they must be delinquent and they must apply for a modification first, even if chances of approval are slim. The aversion to short sales also leads banks to take many months to process applications, and some lenders set unrealistically high sales prices — known as broker price opinions — and hire workers who say they are poorly trained.

As a result, quite a few homeowners seeking short sales — banks will not provide precise numbers — topple into foreclosure, sometimes, critics say, for reasons that are hard to understand. Ms. Sweetland and her broker say they are confounded by her foreclosure, because in Arizona's depressed real estate market, foreclosed homes often sit vacant for many months before banks are able to resell them.

"Banks are historically reluctant to do short sales, fearing that somehow the homeowner is getting an advantage on them," said Diane E. Thompson, of counsel to the National Consumer Law Center. "There's this irrational belief that if you foreclose and hold on to the property for six months, somehow prices will rebound."

Homeowners, advocates and realty agents offer particularly pointed criticism of Bank of America, the nation's largest servicer of mortgages, and a recipient of billions of dollars in federal bailout aid. Its holdings account for 31 percent of the pending foreclosures in Maricopa County, which includes Phoenix and Scottsdale, according to an analysis for The Arizona Republic.

The bank instructs real estate agents to use its computer program to evaluate short sales. But in three cases observed by The New York Times in collaboration with two real estate agents, the bank's system repeatedly asked for and lost the same information and generated inaccurate responses.

In half a dozen more cases examined by The New York Times, Bank of America rejected short sale offers, foreclosed and auctioned off houses at lower prices.

"When I hear that a client's mortgage is held by Bank of America, I just sigh. Our chances of getting an approval for them just went from 90 percent to 50-50," said Benjamin Toma, who has a family-run real estate agency in Phoenix.

Bank of America officials also declined interview requests. A Bank of America spokeswoman said in an e-mail that the bank had processed 61,000 short sales nationwide this year; she declined to provide numbers for Arizona or to discuss criticisms of the company's processing.

Fannie Mae, the mortgage finance company with federal backing, gives cash incentives to encourage servicers, who are affiliated with banks and who oversee great bundles of delinquent mortgages, to approve short sales.

But less obvious financial incentives can push toward a foreclosure rather than a short sale. Servicers can reap high fees from foreclosures. And lenders can try to collect on private mortgage insurance.

Some advocates and real estate agents also point to an April 2009 regulatory change in an obscure federal accounting law. The change, in effect, allowed banks to foreclose on a home without having to write down a loss until that home was sold. By contrast, if a bank agrees to a short sale, it must mark the loss immediately.

Short sales, to be sure, are no free ride for homeowners. They take a hit to their credit ratings, although for three to five years rather than seven after a foreclosure. An owner seeking a short sale must satisfy a laundry list of conditions, including making a detailed disclosure of income, tax and credit liens. And owners must prove that they have no connection to the buyer.

Still, bank decision-making, at least from a homeowner's perspective, often appears arbitrary. That is certainly the view of Nicholas Yannuzzi, who after 30 years in Arizona still talks with a Philadelphia rasp. Mr. Yannuzzi has owned five houses over time, without any financial problems. When his wife was diagnosed with bone cancer, he put 20 percent down and bought a ranch house in North Scottsdale so that she would not have to climb stairs.

In the last few years, his wife died, he lost his job and he used his retirement fund to pay his mortgage for five months. His bank, Wells Fargo, denied his mortgage modification request and then his request for a short sale.

The bank officer told him that Fannie Mae, which held the mortgage, would not take a discount. At the end of last week, he was waiting to be locked out of his home.

"I'm a proud man. I've worked since I was 20 years old," he said. "But I've run out of my 79 weeks of unemployment, so that's it."

He shrugged. "I try to keep in the frame of mind that a lot of people have it worse than me."

Back in Phoenix, Ms. Sweetland's real estate agent, Sherry Rampy, appeared to receive good news last week. GMAC re-examined her client's application and suggested it might be approved.

But the bank attached a condition: Ms. Sweetland must come up with $2,000 in closing costs or pay $100 a month for 50 months to the bank. Ms. Sweetland, however, is flat broke.

A late afternoon desert sun angles across her Pasadena neighborhood.

"After this, I'll never buy again," Ms. Sweetland says. "This is not the American dream. This is not my American dream."