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PROHIBITED SHORT SALE TRANSACTIONS

By: M. Francesca Passeri

A short sale may be a homeowner's best option for a graceful exit from ownership of a property they can no longer afford to retain. A short sale occurs when the mortgage holder agrees accept less than full repayment of a loan in connection with the sale of a property. If the property is owner-occupied, the homeowner may qualify for the Home Affordable Foreclosure Alternative program (HAFA). HAFA requires the mortgage holder to accept the net proceeds from the sale as full satisfaction of the mortgage debt. Additionally, the Seller receives a $3,000 relocation allowance at closing.

A HAFA short sale is restricted to an arm's length transaction. This means that the short sale purchaser must be unrelated to the Seller by family, marriage or business relationship. The parties to the transaction, the real estate agents and the closing agent must sign an affidavit stating that there are no agreements or understandings between the Buyer and Seller that the Seller regain title or ownership of the property, nor will the Buyer or Seller receive funds or commissions from the sale except the Seller relocation expense. The affidavit also states that there are no agreements or offers relating to the sale or subsequent sale of the property that have not been disclosed and approved by the lender. Sometimes the short sale agreement prohibits the Buyer from re-selling the property for a period of ninety days following the closing. The short sale agreement may further restrict that the Seller from leasing the property back from the new owner.

Fannie Mae has a separate program which is designed to allow the owner to deed the property to the lender and rent it back at market rate for a period of up to twelve months. Lenders and servicers may impose their own restrictions and conditions on short sales not qualified under the HAFA program. If the parties violate the terms of a short sale agreement, the lender may choose to set aside the transaction and proceed with foreclosing on the property. The lender may also reserve the right to pursue the Seller for the balance of the mortgage remaining after the short sale that would have otherwise been forgiven. The violation of a short sale agreement may subject the parties to criminal prosecution for mortgage fraud. Sellers should also take care in arranging for the separate sale of fixtures or appliances in connection with a short sale. If the mortgage covers any of the personal property, or if the improvements are permanently affixed to the real estate, it is not advisable for the Buyer to pay additional consideration for these items outside of the transaction approved by the Seller's lender. For instance, if the Seller purchased the property with the appliances, those appliances are covered by the mortgage and should convey with the property without the payment of any additional consideration. Common examples of fixtures that would typically convey with the property are fences, pool equipment and enclosures, generators, storm shutters, sheds and light fixtures. The lender may seek additional financial compensation from a Seller who conveys the property after "stripping" fixtures and appliances, especially if the Buyer paid the Seller for these items outside of closing the short sale.