



FORECLOSURE OR SHORT SALE

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Homeowners facing foreclosure often wonder whether a "short sale" is a better alternative. The answer depends on who's asking. Foreclosures and short sales affect different people differently, depending on their financial situations, priorities, goals, adversity towards risks, property conditions, market conditions, and many other considerations. To help you answer that question for yourself, here are some of the major factors to consider when choosing between foreclosure and short sale.

FACTORS	FORECLOSURE	SHORT SALE
DEFINITION	If you default on your loan, foreclosure is the legal process that your lender may use to sell your property to satisfy the debt you owe.	A short sale is a sales transaction where the seller's lender voluntarily agrees to receive a loan payoff for less than what's owed.
CREDIT	Foreclosure may have a greater negative impact on your FICO score as compared to a short sale with no deficiency balance, according to the FICO Banking Analytics Blog at http://bankinganalyticsblog.fico.com/2011/03/research-looks-at-how-mortgage-delinquencies-affect-scores.html . The magnitude of that impact depends on a consumer's starting FICO score and other credit characteristics. Aside from your FICO score, whether foreclosure or short sale is better for your overall credit-worthiness depends on what purpose you're using your credit, such as obtaining a mortgage loan, auto loan, credit card, apartment rental, or job application (see also right column).	A short sale with no deficiency balance may have a lesser negative impact on your FICO score as compared to foreclosure, according to the FICO Banking Analytics Blog at http://bankinganalyticsblog.fico.com/2011/03/research-looks-at-how-mortgage-delinquencies-affect-scores.html . Additionally, a short sale may be better than foreclosure for obtaining a new mortgage loan under current Fannie Mae guidelines at https://www.efannie.mae.com/sf/guides/ssg/annltrs/pdf/2010/sel_1008.pdf . According to Fannie Mae, only 2 years must lapse after a short sale for a borrower to show reestablished credit, whereas 7 years must lapse after foreclosure (or 3 years after foreclosure if the borrower has extenuating circumstance and shows he or she had no reasonable options other than to default on loan).
TAX	1. <u>Cancellation of Debt</u>: Foreclosure may give rise to taxable income to you for cancellation of debt, which is roughly calculated as your loan balance minus your property's fair market value at foreclosure. Certain exceptions may apply, such as bankruptcy, insolvency, forgiveness of a non-recourse loan through foreclosure, and a loan for purchasing or substantially improving your qualified principal residence. 2. <u>Capital Gains</u>: Foreclosure may also give rise to taxable income for capital gains, which is roughly calculated as your loan balance (or the property's fair market value) minus your original purchase price and major improvement costs. However, you generally do not have to pay taxes on capital gains up to \$250,000 (or \$500,000 for married couples filing joint returns) if you owned and used the property as your principal residence for at least 2 of the last 5 years.	1. <u>Cancellation of Debt</u>: As with foreclosure, a short sale may give rise to taxable income for cancellation of debt, but the calculation is different. For a short sale, the cancellation of debt income is roughly your loan balance minus the sales price. Certain exceptions may apply, such as bankruptcy, insolvency, and a loan for purchasing or substantially improving your qualified principal residence. 2. <u>Capital Gains</u>: As with foreclosure, a short sale may give rise to taxable income for capital gains, but the calculation is different. For a short sale, the capital gains calculation is roughly your selling price minus your original purchase price and major improvement costs. As with a foreclosure, you generally do not have to pay taxes on capital gains up to \$250,000 (or \$500,000 for married couples filing joint returns) if you owned and used the property as your principal residence for at least 2 of the last 5 years.

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FORECLOSURE OR SHORT SALE (Cont'd)

FACTORS	FORECLOSURE	SHORT SALE
PERSONAL LIABILITY	If your loan balance is more than the foreclosure sales price, you generally will not be personally liable for the difference under certain circumstances, such as if the lender forecloses non-judicially through a trustee's sale or if the lender forecloses on a purchase-money, owner-occupied loan for one-to-four residential units. Certain exceptions may apply, such as fraud, bad faith waste for intentional property damage, certain wiped-out junior liens, and FHA and VA loans.	If your loan balance is more than the sales price in a short sale for a property with one-to-four residential units, you generally will not be personally liable for the difference. Certain exceptions may apply, such as, without limitation, if you commit fraud or bad faith waste for intentional property damage (Cal. Code of Civ. Proc. section 580e).
POSSESSION	You generally have the right to stay in your home during the foreclosure process which takes a minimum of about 4 or 5 months. If you do not leave after a trustee's sale of the property, the new owner may negotiate a cash-for-keys agreement with you, commence the eviction proceedings by serving you a 3-day notice to vacate, or take some other action.	You generally have the right to stay in your home until you close escrow on a short sale transaction. You may, however, be able to negotiate with your buyer for a longer or shorter stay, subject to your lenders' consent.
PERSONAL CONCERNS	The foreclosure process takes little effort on your part, but the wait can be agonizing and stressful for certain people. Although non-judicial foreclosure takes a minimum of about 4 or 5 months, you generally cannot dictate how quickly the lender proceeds with each step of the foreclosure process. You may also feel uncomfortable with what you may perceive as the shame or stigma associated with foreclosure, such as when a notice of trustee's sale is posted on your property or the sheriff comes to escort you and your family out of the property.	Doing a short sale may involve a lot of time, effort, and paperwork on your part to list and market your home, get your lender's approval, and consummate the sale with your buyer. Yet, during this process, you generally do not know whether you will succeed in closing your short sale transaction. Despite the hard work and uncertainty, you may prefer a short sale because it allows you to take a proactive approach to finalizing this chapter of your life so you can move on to the next one as quickly as possible.
ASSISTANCE	To assist you, a foreclosure consultant as defined under Cal. Civ. Code § 2945.45 must be registered with the California Department of Justice and bonded for \$100,000. Real estate licensees are generally exempt from this requirement. To check whether someone is properly registered as a foreclosure consultant, call the California Attorney General's Office.	One big advantage of a short sale is you can hire a professional real estate agent to help you through what can otherwise be a complicated and difficult process. You may check whether someone is a duly licensed real estate agent in good standing with the California Department of Real Estate (DRE) at http://www2.dre.ca.gov/PublicASP/pplinfo.asp .



Contact a Professional for Your Real Estate Needs.