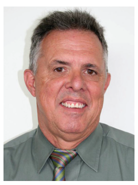
Strategic defaults: Giving your home back to the lender can be a mistake, even if problems seem overwhelming

By Mark Samuelson



In the summer hit movie 'Larry Crowne,' star/director Tom Hanks gets a pink slip from his employer, takes a college economics course, and then gives his house back to the bank – yielding a satisfying moment as he dumps the paperwork on his unsuspecting loan rep. However, real-life choices involving 'strategic default' – willingly handing a mortgage back to the lender -- aren't so simple, says a Denver expert on foreclosures and short sales.

"I can understand why a lot of people end up wanting to do it," says Daniel M. Hilty, Realtor with The Denver 100, a Certified Distressed Property Expert and REO Specialist. "But it's often the fear factor that's driving the decision rather than a balanced assessment of the options available to the borrower."

Hilty, who blogs to a growing audience at DMHHomes.com, says homeowners with loans in default often tell him, "they're (the bank) the ones that sold me this mortgage in the first place." However, mortgagees who face numerous problems – loss of a job, divorce, credit card debt – may have as many as a dozen options to avoid a foreclosure. "In 99 percent of cases," he adds, "a foreclosure ends up being a mistake."

"A lot of people have the impression that the bank can't come after you for a deficiency judgment after you're foreclosed," Hilty adds. "That is absolutely false." In a short sale, a packaged offer at a price below the loan value, banks typically recover 15 to 20 percent more than after foreclosure, meaning a large difference in the balance sheet that governs a creditor's future recourse. "To date, clients I've represented have not had a past lien holder search for a deficiency judgment against them."

Hilty adds that unless a full release is obtained from all lien holders, potential for a deficiency judgment exists. There is no time period that would stop a past lien holder to bring the deficiency judgment now or in the future. The Mortgage Forgiveness Debt Relief Act signed into law in 2007 contains some protections for sellers, through the end of 2012.

Hilty, who did his first two short sales in 2001, ranks as one of the market's most experienced agents in distressed properties, when banks were reticent to accept even a small loss on a loan. Now lenders have a good idea of what foreclosures really cost them, Hilty says, and are anxious to find ways to reduce losses. However, short sales, despite being better performers for lenders than foreclosures are, have been perceived by real estate agents and the public as taking too long to process.

In actuality, his own recent short sale packages have averaged around 30 to 45 days for bank approval. "Banks tend to look at these situations depending on how they're packaged," Hilty says. Primary responsibility for that goes to the agent, who must anticipate the current appraised value of the property close to the way the bank will see it. Meanwhile, Denver area buyer interest in short sale opportunities has remained strong.

Daniel Hilty is a Realtor with The Denver 100 and is a Certified Distressed Property Expert as well as REO Specialist.

Hilty's most recent short sale package, completed last month and now with the lender for evaluation, is a duplex in Denver's Park Hill area. With an appraised price at around $200,000, Hilty had 16 showings the week the property was listed; and ended up with a bidding war that raised the packaged offer to the bank.

"The situation with distressed properties is worse in many other states than here, however this is still enough of an issue that buyers need to be aware of the alternatives," says Jack O'Connor, broker/owner of The Denver 100. Daniel Hilty is on the web at www.DMHHomes.com, or call 720-256-4703. For a subscription to Jack's Report, a monthly letter on real estate trends by O'Connor, call 303-880-8561, or visit TheDenver-100.com.

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