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Sniffing out deals headed to foreclosure

BY ABBY LUBY

As weak spots develop in New York's residential market and headline writers fret about rising foreclosures, bargain house hunters are querying real estate discussion boards to find out how they can get their hands on foreclosed homes.

But the strategy for pursuing these homes—and even homes merely on their way to foreclosure—is complicated.

Fortunately for homebuyers, there are many Web-based courses, classes and intensive weekend-long seminars to explain the ins and outs. These courses are drawing an increasing number of eager students, not to mention producing a barrage of advertising.

One of the first principles the seminars teach is for buyers to search for lis pendens. Latin for "suit pending," a lis pendens is a legal filing that occurs before foreclosure as a homeowner falls behind on mortgage payments.

But even though they outline initial steps for investors like that, foreclosure gurus warn that getting a jump on homes headed for default is not a guarantee of easy money.

"It's the one caveat I tell people—that this is not about getting rich overnight," said Jessica Davis, president and publisher of Profiles Publications, a foreclosure listing service based in Jackson Heights, Queens. Davis teaches foreclosure seminars at New York University and has taught at the Learning Annex in the past. "You can make money and it doesn't require talent or a degree, but you have to educate yourself, and you have to work at it. You have to learn how to minimize your risks by minimizing potential mistakes."

Also teaching investment strategies in the foreclosure market is Matthew Lucks, director of training at PropertyShark.com. Lucks has been designing Internet-based courses but is now planning to teach his course in person starting this month.

Other courses are luring students with promotions that certainly seem intended to put

dollar signs in one's eyes. An ad that has run in Metro New York features a picture of Donald Trump and a headline: "If you're not a millionaire by December 2008, you didn't attend my foreclosure workshop."

Is it a deal?

Rick Sharga of RealtyTrac.com, an online marketplace for foreclosure properties, sees lis pendens filings as a bona fide signal for experienced investors to capitalize on a default situation. He warned, however, that many of these properties have already been stripped of their equity.

"If you're in a market like Queens and you see the prices depreciating and the number of lis pendens increasing, the challenge is to find a property entering foreclosure that has equity," explained Sharga. "People may have overextended themselves and got involved with very risky financing, and there may not be any equity. In fact, the price of the property over the ensuing period may even be a negative equity situation."

Investors usually end up working out what's known as a short sale, said Sharga.

"This is where you negotiate with the bank, and the bank agrees to accept less of what's due on the mortgage as payment in full for the property. Maybe the home owner paid \$500,000 for the house, but the bank accepts \$400,000 to sell the house."

In other words, the bank is cutting its losses, realizing that in a down market, "it would cost them more money to hold and eventually re-sell the property," said Sharga.

Roger Roisman, attorney and partner at the law firm Tannenbaum Helpen Syracuse & Hirschtritt, explained that a lis pendens is basically a notice that "here's a property owner who is in trouble and who may lose the property to his lender."

According to Roisman, if the timing is right, a lis pendens filing may signal a worthwhile deal. "This may be a red flag for someone looking for a bargain, a bottom fisher, for example. It may be the time to talk to the lender, if there is one, about acquiring the note or mortgage at a discount, or working with the owner of the property who clearly has lost his equity in the property, and try to acquire the property."

But lis pendens may also signal different situations, such as when someone wants to prevent a transaction. Roisman laid out a sample scenario where the lis pendens acts as a buyer's protection. "I want to buy a property and give a 10 percent down payment, but I fail to close when I'm supposed to. Capital markets being what they are, I can't get a lender, or I can't get an equity participant, or I can't get either. The seller tells me he is taking my down payment, and he's selling the property to the next guy. I will then file a lis pendens against the property, which will prevent him from selling it to the next guy without first dealing with me in a courtroom."

Lis pendens filings in New York can be a sort of red herring, said David Schechtman, a commercial property broker with Eastern Consolidated. Schechtman, who heads the firm's turnaround and distressed group, said lis pendens may not indicate that there is real financial distress.

"It could be a partnership dispute and disagreement or a tactic between a borrower and a bank," he said. "It doesn't necessarily always signal real financial distress. The difference in Manhattan is that you need so much equity in the deal to get a lender. There just is no subprime in Manhattan for commercial and residential properties."

In New York City, it may not make that much difference, as the number of lis pendens filings is quite low in the first place. According to PropertyShark, in 2007, lis pendens filings for residential properties in all five New York City boroughs totaled 7,386, a number far lower than in other parts of the country. In Queens, 2,942 lis pendens were filed in 2007; in Manhattan, a mere 112.

But those numbers don't seem to be discouraging some bargain-hunters.

"The volume of students has steadily increased over the past few years," said Lucks of PropertyShark's free online courses.

Lucks and Davis said their classes attract people with a wide range of backgrounds, such as beginning investors, experienced brokers, agents and retirees who see the market as more viable than retirement accounts.

How it works

Once a property has a lis pendens filing, the clock starts ticking. According to Peter Schillinger, a partner with the White Plains-based real estate law firm Odesser Schillinger & Finsterwald, the process gives investors plenty of time to buy the pre-foreclosed property.

"If you are able to locate a property prior to auction, that period is generally 12 to 18 months," Schillinger explained, noting that a lender can start the clock when a property owner defaults on his or her mortgage.

"The filing of the lis pendens is the first thing that happens together with a summons and complaint. This is when the bank feels that the default has gone on long enough, and they want to start a lawsuit called a mortgage foreclosure action," he said.

Not all meritorious

In general, the lis pendens filed since the credit crisis in the summer of 2007 have not resulted in bank auctions, according to Schechtman. "They've generally been cured. The

borrower can cure it; they can get money from someone else to cure it. There are a lot of lis pendens filings, but just like a lot of lawsuits, they are not all meritorious."

For bargain-hunters, the next step is to find out what happens to those homes that were teetering on the brink. Since some of them end up in bank hands, buyers try to learn how to negotiate with lenders.

"We are also seeing more attention paid to bank-owned properties instead of lis pendens or auctions," Sharga said. "The reason for that is the inventory the banks are taking back has grown significantly over the last year, and the banks are more motivated to negotiate prices."

Of course, if you're not a bargain-hunter, this process cuts both ways. While saving a property from foreclosure by purchasing it in the lis pendens phase helps the distressed homeowner avoid the credit implications of a foreclosure, which can keep him or her from qualifying for loans or even getting a job, Lucks of Property Shark explained that the sale of foreclosed or defaulted homes has a distinct effect on neighborhoods. "Depending upon zoning and demand, investors may redevelop land, altering the face of the neighborhood. Some investors, especially now, are purchasing properties as a long-term rental. This creates a larger supply of rentals, thus driving the price of rent down in the area," he said.

Getting lis pendens listings, which are available on the Internet, gives potential investors some advantages.

"When you are dealing with lis pendens, you are dealing directly with the owner, which means you can look at the property, flush the toilets, even have the property appraised," said Bill Staniford, vice president of sales at PropertyShark.

Learning how lis pendens works and knowing how to use the data levels that playing field for both novice and veteran investors, said Staniford.

"As long as we can train people how to value a property correctly and identify the good deal, they should be able to generate a good purchase price, and values will go up," he said.

He continued, "This isn't a get-rich-quick mentality; this is a real business model people take seriously."