

Real Estate Empowerment Series

What you need to know Before Buying a HUD Home



by

Jerry Becker GRI, ABR

WHAT YOU NEED TO KNOW BEFORE BUYING A HUD HOME

As I talk with people who have expressed an interest in purchasing a HUD home or bank foreclosure, I'm amazed at some of the misconceptions that many have. Because of this fact, I've written two separate books to educate the general public about HUD home and bank foreclosures. In this book, I'll be dealing entirely with HUD homes and the often misunderstood purchasing process. The fact that this process causes confusion shouldn't be too surprising, because, after all, you are dealing with a government program. There are even many real estate brokers who are confused about the HUD home buying process. This probably explains why the majority have elected not to serve the public by becoming a registered HUD broker. What I'm going to try and do with this space is explain HUD homes and some of things you will need to know about the purchasing process. In no way can it cover every question that you may have, or may come up with, in a HUD transaction. Save those questions for your registered HUD real estate broker.

Another thing I hope to provide is the opportunity to educate yourself without having to register or 'sign up' with many of the websites offering you information. Very few things are free, as many of these sites are second party sites. That means they are offering you information that you could have gotten directly from other sources. Basically these sites are trying to trade you public information for your personal information, so they can hopefully 'cultivate' you as a future client. There's nothing illegal or wrong with this; just be aware of what you're getting into.

Let me also make a point of clarification. You'll see the word foreclosure used from time to time in this book, however, I want you to understand that a HUD home is not in foreclosure. It was in foreclosure as it went through the foreclosure process, but once HUD acquires the home it has completed the process of foreclosure. Now it's a home that is being sold by a seller. The seller in this instance just happens to be the federal government, which is selling it through HUD.



WHAT IS A FORECLOSURE?

Let's start with the basics. A foreclosure is where a borrower has ceased to make payments to the lender that loaned the money for the purchase of the property. If the borrower's loan was an FHA loan, then it was insured by HUD, The Department of Housing and Urban Development. When the borrower can't make the payments, HUD pays the lender what they're owed, and takes over the property. At this point it becomes a HUD property. It can be a single family home, condo, town home, or 2-4 unit apartment building. If the property wasn't financed with an FHA loan, then this type of foreclosure would most likely be foreclosed through the public trustee system that we have here in Colorado. I've covered those types of foreclosures in a separate report.

One thing a foreclosure isn't is an automatic "great deal!" I say that, because there seems to be a perception among the general public, that when someone mentions 'foreclosure' they start to salivate. Some are good deals and some aren't, it's as simple as that. Another thing to keep in mind is that different people have different ideas of what constitutes a "good deal." A couple trying to buy their first home may be tickled to get a home for 5-10% below the market value,

while an investor, who plans on fixing up a home, so they can resell it for a profit, may have to find one that's 30% or more below market value, so the numbers will work in order for them to make a profit. Before you think that's the kind of discount you want to have, you need to know that these aren't as common; they require lots of cash to make them livable. Plus, if you don't have a record of doing this for a living, most lenders won't lend you the money. I don't want to take up space explaining why this is, so I'll leave that explanation up to your real estate professional.

One thing a foreclosure isn't, is an automatic "great deal!"... Some are good deals and some aren't, it's as simple as that

WHY WOULD I WANT TO BUY A HUD HOME?

As I just mentioned, not all home in foreclosure are good deals. However, if that's what you're looking for, then I think you have a much better chance with a HUD home. We frequently make jokes when we're talking about how much fun it is dealing with the government, but when the government is responsible for getting thousands of repossessed homes off the books, they don't fool around. The government has no emotional attachment to these homes and they don't have to worry about making a profit or avoiding a loss. That's why they usually price these homes slightly below the market and then let the market forces determine the value by a bidding process. If a home has been on the market for a couple of bidding terms with no buyer, then they lower the price, and continue to lower it until the home sells. No messing

around. This is totally different than the approach a conventional lender will usually take. The object of the conventional lender is not to lose money, so they frequently price homes at what they think is the market price, often times going against the advice of the broker they hired to sell the home. That's why homes owned by lenders can sit on the market for months. The lenders have to be "taught" by the market what the true price is.

One important thing I want to mention about HUD homes is that they aren't always in the best condition. It's not unusual to find that they need carpet, have appliances missing, have missing or damaged doors, need a new furnace, or need drywall repairs. These are the most common but they aren't always the same for each property. The more items like these associated with a property, usually the longer it takes to sell and the lower the price HUD will accept. This is where you can get the best bargains. Don't be afraid of the term "sweat equity." Dirty carpets can be cleaned, walls can be painted, drywall can be repaired, and used appliances can be purchased at quite a savings. The longer the list of needed repairs and the worse the property condition is, the more likely this property would be purchased by an investor.

If you're wondering why most HUD homes aren't in good condition, the answer is easy. In most cases, prior to HUD acquiring the homes, while the homes were in the foreclosure process, the sellers were trying to get their home sold before it went to auction or sheriff's sale. If the sellers were the type of owners that took care of their property, than the odds were very good that it sold on the open market, and never ended up going all the way to the auction. In today's buyers' market, homes that aren't in great condition usually won't sell unless the price reflects the condition, and even then many people will pass these homes up because they don't want a fixer upper.



Don't be afraid of the term "sweat equity." Dirty carpets can be cleaned, walls can be painted, drywall can be repaired, and used appliances can be purchased at quite a savings.

Do HUD homes in good condition exist? Yes, but not very often, and when one hits the market, it doesn't last very long. HUD homes in good condition frequently get bid up higher than the HUD asking price. People often tell me they aren't afraid to do a little fixing up. However, when that home in perfect condition hits the market, they're on it like flies on sugar.

WHERE DO I FIND HUD HOMES?

If you have access to a computer, you can find HUD homes by going to www.hud.gov/homes/index.cfm. There you

will find a listing of all fifty states and US Territories. Click on the location of your choice, and then do your property search by selecting either county or city. HUD doesn't sell the homes directly. HUD has contracted with various companies to handle these sales throughout the country. These contractors represent HUD, and they in turn, contract with select real estate firms to list these homes in the local areas. Even though these contractors will differ from state to state, the process is pretty much the same. New listings come out on Friday and are available for bids until 11:59 PM of the second Sunday after they are listed. That gives you roughly nine days to view any of the latest offerings you're interested in and submit your bid. All new listings are only available for owner occupants. If a property isn't purchased after the initial listing period, then HUD will also open it up to investors, in addition to owner occupants. After a home is opened up to investors and no offers come in for several weeks, then HUD may drop the price. If HUD drops the price on a home, or a home that's under contract fails to close, then it will be re-listed for owner occupants, but only for five days. After the five days pass and no offer is submitted, then HUD will also open it up to investors. Results of accepted bids are generally posted by 2:00 PM on the Monday after the bid period. The only person that can place your bid on a HUD property is a **registered HUD real estate broker**.

WHAT DO I NEED TO KNOW AND DO PRIOR TO PURCHASING A HUD HOME?

First of all, you need to start working with a lender to get pre-qualified for a loan. Getting pre-qualified is

extremely important because HUD requires that you submit a letter from your lender with your contract, stating that you can qualify to purchase the home you just made an offer on. You need to make sure that your lender has experience in working with the HUD process. Dates are extremely critical in the HUD process and if the lender is even one day late in getting the package to the HUD designated closing agent, it could cost you \$375 for a 15 day extension. Lenders are required to have their final figures and closing instructions to the closing agent a minimum of 8 business days prior to closing. Ask your lender if they know how many days prior to closing, they're supposed to have these items to the closing agent, and if they can't give you a correct answer or don't know what you're talking about, then you need to find another lender. Your HUD registered real estate professional can always recommend lenders that understand the process.

VERY IMPORTANT:

If you are using FHA financing, it's very important that you don't bid over the HUD asking price. These homes are priced using FHA appraisals and if you purchase a home by bidding over the asking price, you will be required to pay the difference between HUD's asking price and the price you bid, if it's higher. That's in addition to the normal FHA down payment.

While meeting with your lender, you will be discussing various loan options, based on your income, credit scores, and available funds. Traditionally, one of the best loans for first time buyers has been FHA. If this is your only option, then fine, at least you qualify for a loan. You may also want to see if you qualify for other loans besides FHA because not all HUD homes qualify for FHA financing. The more work that a home needs, the better the odds that you won't be able to use FHA financing. When you are looking at the details of the listed homes, you will also see what kind of financing they qualify for.

SOME WORDS ABOUT FINANCING

When you're looking at the details of a particular property, you will notice they list the type of FHA financing that's available. The three categories are **IN**, **IE**, and **UI**. When referring to an FHA loan, the correct title is FHA 203(b), however, nearly, everyone will simply use the term FHA.

The first is **IN**, which stands for Insured. This means you can get an FHA 203(b) loan on the home.

The second is **IE**, which stands for Insured with Escrow. This means the property needs repairs to bring it up to the minimum property requirements (MPR). If the amount required is less than \$5,000, than you can use a regular 203 (b) loan, and add up to 110% of the FHA estimated repair cost to the original loan amount. The amount by which the loan was increased will be escrowed at closing. That means the funds are set aside and held by the title company or the

lender. When the contractors are finished doing the repair work, the entity holding the funds will then pay the contractors. You are not allowed to do the work and then pay yourself.

The third category is **UI**, which means uninsurable, as far as FHA is concerned. You could use conventional financing, as you could on any HUD property, or you can use one of these two FHA loans. The first is called an FHA 203 (k) and it's used for uninsurable properties, where the cost of repairs exceeds \$5,000.

One thing to keep in mind when doing an FHA 203 (k) loan, is that they are a pain in the neck for the lenders. It requires much more paper work for the time invested, so most lenders will not offer to do them. Bottom line is there are few lenders that actually do these loans. Your real estate agent should be a good source for lenders, so start with them. Many lenders have their own product that does what an FHA 203 (k) does, but with much less brain damage. Because the 203 (k) loan was so unpopular with lenders, FHA came out with the Streamlined 203 (k) program, as a second type of loan you could use with these types of properties. This loan can be used on homes marked as insurable with repairs under \$5,000, or on uninsurable homes with repairs costing over \$5,000, but not more than \$35,000. The great thing about the Streamlined 203 (k), is that is supposed to be much easier for lenders to process, hence, it's more likely they will offer them. I was just informed at an HUD seminar, that FHA is still experiencing lenders that haven't heard of the Streamlined version. When they hear the words 203 (k), some lenders automatically say they don't

do those, so you or your agent, may have to help educate your loan officer about this new product. Even though HUD said this loan product is supposed to be easier, at the present time lenders haven't been sharing their enthusiasm for this product. Maybe by the time you read this, HUD will have made it more acceptable to lenders. You'll just have to ask.

I can't stress enough how important it is to sit down with a reputable lender early in the process. Even if you don't plan on buying for six months to a year, a lender can examine your credit and credit scores and make recommendations for you to follow that can improve your credit over the coming months. Bad credit can be improved, but it takes corrective practices and time.

Also, ask your lender or agent if your community has any loan assistance programs that you may qualify for. These are programs designed to help people with good credit but lacking in funds, qualify for a purchase. They sometimes give money as a grant or they will make a loan that doesn't have to be repaid until you sell, refinance, or pay off the

home. Many of these loans are either made with a very low interest rate or with no interest being charged.

*WITH YOUR FINANCING IN PLACE, LET'S CONTACT A
HUD REGISTERED BROKER*

This part isn't too hard, even though most brokers aren't registered. You may have a family friend who's registered, or you can obtain a list from the HUD web site, from which you searched for homes. You could also contact the agent that has the property listed, but I want to tell you that these agents are only being paid approximately \$200 by HUD for listing the property. They will be **extremely motivated** to get you to purchase their listing so they can make a better commission. That's why you may want to use a broker that doesn't list for HUD. That way there'll be no conflict of interest, they will only represent you and your best interest. That's why I don't list HUD homes; I only work with the buyers trying to acquire them. You can also contact me at the numbers following this article.

LET'S GO LOOKING AT HOMES!

Now it's time to start doing your research. Keep checking www.mcbreo.com every Friday for the new listings. Drive by the homes that look appealing so you can get an idea for the neighborhoods and location. For example, does it back to a busy street or commercial area, or is the neighborhood run down. Make an appointment with your HUD broker to actually tour the inside of prospective homes. Hint: Be sure to bring a flashlight, because HUD homes won't have the power on. I also highly recommend that you have your broker take you inside other homes that aren't HUD's in your chosen neighborhoods, so you can compare values. After all, how do you know if a home is a good deal if you don't have anything to compare it to? You can do an initial comparison yourself by going to www.JerryBeckerAndAssoc.com, and clicking on "Property Search". By doing this, you will get an idea of what the asking prices are for other homes in the neighborhood. Keep in mind it's no substitute for actually looking inside these homes. Now we have to go to the next level as you narrow your search. If there is a neighborhood that you want to purchase a HUD home in, you need to have your HUD broker pull up a list of recent homes that have sold. It's one thing to look at homes that are listed for sale, with

prices sellers hope to get, and looking at similar homes that have actually sold. In other words, what did people actually pay? This last piece of information will be the best indicator of true values in that neighborhood.

Now remember, if you are only qualified for an FHA loan, don't go looking at homes that don't qualify. On the web site some properties will have a line titled "Escrow Amount". This is the amount of repairs that HUD has determined that property needs. HUD will not do any repairs, but depending on the type of loan you're getting, lenders will include the repair estimate into the loan by increasing the loan amount. What happens is the lender will authorize the title company that closed the loan, to set that amount aside on your behalf, in a separate account, and then pay the bills of the contractors that do the repairs. For example, if the property needs a new water heater, HUD has determined what that will cost. If the cost is \$500, the lender will allow you to increase your loan by \$500 and that amount is escrowed, or set aside, in a special account at closing. After the work is finished, the contractor contacts the title company, and presents the bill for payment. You aren't allowed to do the work yourself and collect the money, and all repairs are done after closing.



You can get into big trouble if you try and have any work done prior to you owning the property.

Here's a hint that may save you some headaches. If the home you're purchasing has escrows, print the page from the HUD website that shows what the escrows are. There have been cases where lenders will dispute what the escrow payment is for and won't release the funds, to pay the contractors, until they have some type of verification from HUD. Since HUD is constantly purging sold listings from their computer, the information may not be readily accessible. If this happens, just present the lender with the print out, showing the escrow amounts and your problem should be solved.

Submitting Your Purchase Bid

Now that you've found a home that you want to purchase, what's next? Earlier, I had mentioned that these homes were sold by a bidding process. What that means, is that you will most likely be competing with other buyers for the same property. The winning bid is determined by whose bid will net HUD the most money. That's why you have to do so much 'homework' comparing properties. No one likes to pay too much, but you don't want to be left out by submitting ridiculous offers, either. On the HUD web site, you can go to "Bid Statistics" to get an idea for the variety of offers. You can also check "Bid Results" to see what the winning bid was on a particular property. As I mentioned earlier, the nicer the home - the higher the price.

If the home you're purchasing has escrows, print the page from the HUD website that shows what the escrows are.

HUD's master computer has a formula to determine the minimum bid HUD will accept. If you were the only person to bid on a property, and your bid was very low, HUD would not accept your offer. Frequently, the majority of first time bidders don't get their bids accepted because they bid too low. It usually takes until the third or fourth bid, before buyers figure out a bid price that will bring them success. This is because of the public mind set, discussed earlier, that banks and HUD are giving away these properties. They aren't, although HUD is more aggressive in pricing their homes to move!

If you're a little short on money, you can ask HUD to pay your closing cost. This is a great deal, because will pay up to 3% of the purchase price to cover those expenses. Just remember that doing this will decrease the net amount to HUD, and will make your bid that much less competitive. On a property priced at \$200,000, you and another buyer each bid \$195,000, but if they asked for HUD to pay 3% closing cost and you didn't, you would get the home. If you really need the closing cost, then you may want to consider raising the purchase price by the amount you're asking HUD to pay.

You will also need to write a check for earnest money to submit with your offer. At the present time, it's \$500 for anything priced below \$50,000, and \$1,000 for everything above that. There is talk about raising these amounts, but it hasn't happened, yet. Your check needs to be a cashier's

check made out to “HUD or your name” (HUD or John Doe), that way if your bid isn’t selected, you can endorse the check and redeposit it back into your account. If your name wasn’t on the check, it would be more complicated.

The reality is most people don’t get the first home they bid on. It takes a while for them to learn the system and develop a feel for what to offer. It can get frustrating, but don’t worry; you will eventually get a home you want.

YOUR BID WAS ACCEPTED, NOW WHAT?

Congratulations, you now have a contract on a home. From here on in your realtor will be responsible for getting required paper work to the respective entities and making sure the transaction stays on track. Your next hurdle will be to do a property inspection. HUD allows you 15 days from the time your bid was accepted, so you will have to move fast. While an inspection isn’t required, it is highly encouraged. The phone book is full of qualified home inspectors, or you can ask your realtor to provide you with a list. HUD homes will generally have the water and power turned off. You, through your agent, will have to make arrangements to get them turned on. As a buyer, you are responsible for all connection fees and usage charges by the utility companies, for turning these items on.

As you know, you are buying the property in it’s “as is” condition, however, if your inspection uncovers something that you can’t accept, you can request a cancellation of

contract form. HUD is a lot more lenient about returning earnest money to owner occupants than they are with investors. If the property has been damaged or vandalized, you also need to let HUD know in writing.

After the inspection, your realtor needs to notify HUD in writing that the inspection has been completed. This is especially important in winter, so HUD can re-winterize the property, if the water was turned on. If this wasn’t done and the pipes froze causing damage, you could be held responsible for that damage. Here’s a tip, if you’re doing an

inspection in the winter, you can have your inspector do an air test on the water pipes, instead of having the water turned on. If the system isn’t holding pressure, that means you have a leak somewhere. In Colorado, the HUD contractor will usually have the pipes air tested, prior to putting it on the market, and you’ll often see it referenced on the

Property Condition Report, because it will mention that the water lines wouldn’t hold pressure. If they did an air pressure test and it leaked, HUD will not allow you to turn the water on for an inspection. There’re two reasons why it’s advisable to also have your own inspector do an air test, even if HUD did one previously. First of all to be sure the HUD contractor didn’t miss having it done, and secondly, since you’ll be present, you may be able to hear the air escaping and hence, have an ideal of where the leak actually is. This can be helpful when you get a plumber out to repair it, after you take possession.

Your realtor should be watching critical dates and staying in communication with all the parties.

ALMOST THERE

After the inspection is completed, you really don't have much more to do except stay in contact with your lender, and provide whatever additional documentation they may need, ASAP. Remember, your lender needs to get the figures and closing instructions to the HUD designated closing agent a minimum of 8 days prior to closing. Your realtor should also be watching critical dates and staying in communication with all the parties. If everything goes as planned you should go to your closing as expected.

If problems arise, and you can't meet your closing date, you will have to file for an extension. The bad news is that it will cost you \$375 for a 15 day extension. The good news is that HUD generally will give the money back for an individual,

as compared to an investor. If another extension is required after that, HUD will charge you again and mostly likely keep the money. That's why it's so important to get your financing started early, with a lender you can depend on.

THE FINISH LINE!

Now that you've closed on your home, it's yours to start enjoying. One last bit of advice is that you don't get a key at closing. Your realtor will have to use his HUD key to let you in and after that you will need to put on new locks, to protect your property. That's why I give my HUD clients a gift of having their home re-keyed.

SPECIAL HUD PROGRAMS

GOOD NEIGHBOR NEXT DOOR PROGRAM-GNND

If you or your spouse are full time teachers, law enforcement officers, fire fighters, or emergency medical technicians, you can buy a HUD home for half price! Now before you get too excited, you need to know that there are some specific conditions. First, the home must be in a HUD designated revitalization area in need of economic and community development. **Also, you cannot own any other home**, at the time you close on your HUD home. As before, you must use a HUD approved real estate broker, but HUD won't pay the commission, you have to add it to your mortgage amount. HUD will not pay any closing cost and you must bid the asking price. HUD also requires you to live in the home for a minimum of three consecutive years. At the time of closing HUD requires you to sign a second loan for the half of the purchase price, that's being given as a discount. For the three years you live in the home, HUD won't charge you any interest or expect you to make payments, on this second. If you break any of the requirements, HUD will then record that second loan, and you'll have to start making payments on it. If you're still in

the home after three years, HUD will cancel the second loan. In the event there are multiple buyers for an individual property, the computer will randomly select the winning bid.

Homes that qualify for the GNND program are marked different ways on the HUD contractor's web sites. The properties may be marked with an "**Officer Next Door**" button that you'll see next to the property or they may be

in a "**special programs**" section. All of these sites have a "**contact us**" button, where you can inquire about the location of special programs homes, on that contractor's site.

NON-PROFIT AGENCIES

If you are a community or faith based non-profit agency, you may qualify to purchase HUD homes, at up to a 30% discount. The intent is that your organization would buy these homes, fix them up, and then sell them to first time homebuyers or low to moderate income families. Your agency must first be approved by HUD.

CONCLUSION

If you do purchase a HUD home as an **owner/occupant**, please be aware that you must live in it for at least 12 months after closing. If you violate this rule, it is a felony and you could be fined \$250,000 and/or receive two years in prison. HUD uses computers and human checkers to catch people. If you want to buy a second HUD home as an **owner/occupant**, you have to wait 24 months from your previous purchase. As an investor, you can purchase as many as your lender will allow.

I hope you've enjoyed reading this report and found it to be of value. You can also get more detailed information by navigating through the HUD website, but at least now, you'll have a better understanding about what you're

reading and how the system works. As you venture down the path to home ownership, I want to wish you the best of luck on your HUD home purchase.

If I can be of assistance to you, either in the purchase or with questions, feel free to email me at jbeckerhomes@comcast.net.

Sincerely,
Jerry Becker
Metro Brokers
Jerry Becker & Associates

Qualifications Brief for Jerry Becker

OBJECTIVE

To assist my clients in achieving their real estate goals, by utilizing sound planning, professional ethics, and persuasive skills, while maintaining a loyal commitment to the people who put their trust in me.

EDUCATION/TRAINING

- Licensed Real Estate Broker, Wisconsin – 1974
- Licensed Real Estate Agent, Colorado – 1982
- Graduate Realtor Institute, GRI – 1992
- Completed Colorado Broker's Exam – 1995
- Past Member of New Homes Sales and Marketing Council
- Prior Member, Million-A-Month Club (President, Vice-Pres, Treasurer)
- Past Member, South Suburban Board of Realtors®
- Member, National Association of Realtors®
- Member, Denver Board of Realtors®
- Accredited Buyer Representative, ABR – 2001
- Author Of, *“Money Saving Tips for Buyers and Sellers”, “What you Need to Know Before Buying a HUD Home”, and What you Need to Know Before Buying Foreclosure”.*

COMMUNITY INVOLVEMENT

- Ken-Caryl Ranch Resident since 1985
- Ken-Caryl Ranch Committee and Task Force Involvement
- Ken-Caryl Ranch Master Association Board Member, 1990-1995
- Ken-Caryl Ranch Master Association, Vice-President 1994-1995
- Ken-Caryl Ranch Master Association, Treasurer 1991-1993
- Jefferson County Jail Ministry, 1998-Present
- Staff Instructor For The Home Ownership Center, 2004 - Present