

# LAW OFFICES OF KEN KOENEN

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October 1, 2010

Mr. and Mrs. Homeowner  
4321 Underwater Drive  
Anytown, CA 94321

RE: Short Sale Liability Report and Opinion Letter  
4321 Underwater Drive, Anytown, CA 94321

Dear Mr. and Mrs. Homeowner:

I am in receipt of your request for a report and opinion letter as to your rights and obligations related to the mortgage or mortgages at the above referenced property.

This report is based upon the information on the Short Sale Liability Report Questionnaire that you completed and provided to me. It is very important that the information that was provided is accurate. The report is also based on current California and Federal laws currently in effect. Changes in the law prior to the actual transaction date of a short sale or foreclosure could result in a different outcome.

## **PROPERTY DETAILS:**

Address: 4321 Underwater Drive, Anytown, CA 94321  
Date of Purchase: April 1, 2006  
Purchase Price: \$600,000.00  
Original Down Payment: \$60,000.00  
Current value: \$420,000.00  
Primary Residence: Yes

This report is broken down into 3 categories. The categories are as follows: 1) Whether there are any Tax implications, 2) whether the lenders can seek a deficiency judgment and attach other assets, and 3) the potential credit rating implications.

## **TAX IMPLICATIONS:**

First Mortgage with Acme Bank:  
Current Principle Balance: \$480,000.00  
Past Due Amount: \$8,500.00  
Purchase Money Loan: Yes

A short sale of this property would result in a shortage to the lender in the amount of approximately \$85,000.00, which would result in a forgiveness of debt, which is in many cases taxable to the owner of the property as ordinary income. In California, a loan made to

purchase real property and secured by that property is a non-recourse loan, which means that the borrower is not personally liable for the debt. If this is a purchase money loan, there will be no tax liability. If this was a refinance, and therefore, not a purchase money loan, the situation could be different. If this property is your primary residence, then it is covered by legislation passed by both the Federal Government and the State of California. That legislation provides an exception to the tax liability that would normally be involved in a short sale or foreclosure.

**OPINION IN YOUR CASE: BECAUSE THIS IS YOUR PRIMARY RESIDENCE AND A PURCHASE MONEY LOAN, THERE IS NO TAX LIABILITY FOR THIS LOAN.**

Second Mortgage with Thrifty Bank:

Current Principle Balance: \$100,000.00

Past Due Amount: \$4,500.00

Purchase Money Loan: No

Cash-Out Refinance: Yes

A short sale of this property would result in a shortage to this lender in the amount of approximately \$100,000.00, resulting in a forgiveness of debt, which is in many cases taxable to the owner of the property as ordinary income. In California, a loan made to purchase real property and secured by that property is a non-recourse loan, which means that the borrower is not personally liable for the debt. If this is a purchase money loan, there will be no tax liability. If this was a refinance, and therefore, not a purchase money loan, the situation could be different. If this property is your primary residence, then it is covered by legislation passed by both the Federal Government and the State of California. That legislation provides an exception to the tax liability that would normally be involved in a short sale or foreclosure up to the amount of the original loan amount. If, during a refinance, additional cash was taken by you from the equity, that amount is not covered by this legislation, and could amount in a tax liability. If that is the case, there may be other exemptions from the tax liability, such as the "Insolvency Exemption."

**OPINION IN YOUR CASE: OF THE \$100,000.00 BALANCE ON THIS LOAN, ONLY \$60,000.00 WAS IN THE ORIGINAL PURCHASE LOAN. THE BALANCE OF \$40,000.00 COULD BE TAXABLE AS ORDINARY INCOME.**

**DEFICIENCY JUDGMENT LIABILITY:**

California has a number of statutes in place to protect homeowners from deficiency judgments in the case of a short sale or foreclosure. The first is known as the "One Action Rule" which limits the lender to one action against the homeowner. Because the lender is required to proceed against the property first, they have the choice of a non-judicial foreclosure (Trustee Sale) or a judicial foreclosure in which they would be required to file a lawsuit in order to obtain a money judgment. Very few lenders, especially those in first position, elect to obtain a judicial foreclosure. They are more costly and time consuming, and provide the borrower with a right of redemption of the property. The other reason that the lenders use the non-judicial method of foreclosure is based upon the next statute that protects borrowers from deficiency judgments.

A deficiency judgment is prohibited after the foreclosure of real property that secures a purchase money loan for an owner occupied property of one to four units. This means that

for an owner occupied property, where the loan was made at the time of purchase, there can be no demand for a deficiency judgment after foreclosure. This rule does not affect a refinance of a purchase money loan or a home equity line of credit made after the original purchase. There is presently legislation in Sacramento waiting for the signature by the governor that could change the law to include refinances of purchase money loans and home equity lines of credit. Should those be signed, there is still a question as to whether or not the law would be constitutional because it would impose new laws against old loans that were made under the previous laws.

OPINION IN YOUR CASE: THE FIRST MORTGAGE HOLDER, ACME BANK, IS BARRED FROM SEEKING A DEFICIENCY JUDGMENT BECAUSE THE LOAN IS A PURCHASE MONEY LOAN. THE SECOND MORTGAGE HOLDER THRIFTY BANK IS **NOT BARRED** FROM SEEKING A DEFICIENCY JUDGMENT UNLESS THEY ARE THE ONES THAT FORECLOSE (NOT LIKELY). IF THERE IS A FORECLOSURE BY THE FIRST MORTGAGE HOLDER, THE SECOND WOULD BE ABLE TO FILE SUIT AGAINST YOU. IT WOULD BE BEST TO ATTEMPT A SHORT SALE WHEREBY THE SECOND WOULD RECEIVE SOME MONEY IN EXCHANGE FOR A FULL RELEASE. **ANY SHORT SALE DOCUMENTS SHOULD BE REVIEWED BY AN ATTORNEY BEFORE YOU SIGN THEM.** A BANKRUPTCY WOULD ELIMINATE OR GREATLY REDUCE THE AMOUNT OF OBLIGATION THAT YOU MIGHT HAVE TO A SECONDARY LENDER.

#### **CREDIT RAMIFICATIONS**

This area is very subjective, and based on the eyes of the credit grantor. Many credit card providers are slashing or cancelling lines of credit for borrowers who are past due on their mortgage payments.

The information that I have received from various lending sources is that a short sale will be better on your credit report. The lender will show that the account was "Settled for less than full amount owed," or something similar. If there is a foreclosure, the lender will show it as such. Unfortunately, there are millions of people in this country who now have a foreclosure on their records. It is likely that in 2-4 years, someone with a foreclosure on their record will be able to obtain a good mortgage loan.

#### **CONCLUSION:**

I cannot advise you on what is best for you in your situation. The purpose of this report is to provide you with the information that you require to make an informed decision based on the tax and legal ramifications that you might face in a short sale transaction or a foreclosure event.

Sincerely,

Ken Koenen  
Attorney at Law

cc: File

# SHORT SALE LIABILITY REPORT

## QUESTIONNAIRE

We need some information about you:

Name: \_\_\_\_\_

Spouse Name: \_\_\_\_\_

Home Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_

Contact Phone No.: \_\_\_\_\_

Other Phone No.: \_\_\_\_\_

Email: \_\_\_\_\_

Do you have a Real Estate Agent? If yes,

Name of Agent: \_\_\_\_\_

Company: \_\_\_\_\_

Address:

City: \_\_\_\_\_ State: CA Zip: \_\_\_\_\_

Phone No.: \_\_\_\_\_

Email: \_\_\_\_\_

We need some information about the property:

Address, if different: \_\_\_\_\_

City: \_\_\_\_\_ State: CA Zip: \_\_\_\_\_

Date of Purchase: \_\_\_\_\_

Purchase Price: \_\_\_\_\_

Down Payment: \_\_\_\_\_

Approximate Value: \_\_\_\_\_

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Next, what is your current financial situation?

Total Debt, including all credit cards, mortgages or other obligations that you currently have:

\$ \_\_\_\_\_

Total Asset, including all real property, personal property, bank, accounts, etc. you have:

\$ \_\_\_\_\_

Finally, tell us about your mortgage(s):

First Loan:

Who are the named borrowers on the loan: \_\_\_\_\_

Name of Lender: \_\_\_\_\_

Amount of Loan: \_\_\_\_\_

Date of Loan: \_\_\_\_\_ Was this a Refinance?      Yes      No

Present Balance: \_\_\_\_\_

Monthly Payments: \_\_\_\_\_

Past Due Amount: \_\_\_\_\_

Has this lender filed a Notice of Default?      Yes      No      Not sure

Have they filed a Notice of Trustee Sale?      Yes      No      Not sure

Second Loan:

Who are the named borrowers on the loan: \_\_\_\_\_

Name of Lender: \_\_\_\_\_

Amount of Loan: \_\_\_\_\_

Date of Loan: \_\_\_\_\_ Was this a Refinance?      Yes      No

Present Balance: \_\_\_\_\_

Monthly Payments: \_\_\_\_\_

Past Due Amount: \_\_\_\_\_

Has this lender filed a Notice of Default?      Yes      No      Not sure

Have they filed a Notice of Trustee Sale?      Yes      No      Not sure

If there are any other loans, please add another page and complete the above questions.

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### VERIFICATION

I/We completed this information to the best of my/our knowledge, and have reviewed the information for accuracy. I/we understand that the validity of the Short Sale Liability Report is based upon the foregoing information. After reviewing the information provided to the Law Office of Ken Koenen, we verify that it is truthful and accurate as of \_\_\_\_\_.

\_\_\_\_\_  
Print Name: \_\_\_\_\_

\_\_\_\_\_  
Print Name: \_\_\_\_\_