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Our first Courtside Newsletter for 2010 reports on yet another short sale fraud scheme and discusses some issues arising in REO transactions where the MLS Rules and Code of Ethics need to be considered.

### *ANOTHER SHORT SALE FRAUD SCHEME*

Another real estate fraud has emerged in short sale transactions that involves large banks. The National Association of REALTORS® has reported that about 12% of home sales in 2009 were “short sales” (a sale in which the lender allows the property to be sold for less than the value of the loan). In today’s market, a large number of owners who are in trouble have two or more loans on their properties. To complete a short sale, the second and all subsequent lenders must release their liens, otherwise the escrow cannot close and the property will likely go into foreclosure. The first lienholder generally offers a partial payment to the subordinate lienholders to obtain their cooperation in releasing their liens. Typically, the subordinate lienholders will accept because otherwise they will be eliminated by the foreclosure and receive nothing.

Here’s where the new short sale fraud scheme comes into play. Some subordinate lienholders are requesting payments outside of escrow (often a cashier’s check before closing) from the buyers or the real estate agents. The first lienholder is unaware of the side payment, because it is not included on the HUD settlement statement. The nondisclosure of the side payment is made a clear condition of the subordinate lienholder’s agreement to release its lien and allow the short sale.

According to a representative at HUD, the secret kickback payment to the subordinate lienholder is a clear violation of the Real Estate Settlement Procedures Act (RESPA) and is illegal. RESPA was enacted in 2008 to protect consumers from various forms of kickbacks that increase the cost of settlement services. Commonly known as “Section 8(a)”, RESPA requires that consumers receive full disclosures during a residential sale transaction and provides that: “no person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.”

Large banks that have been identified as participating in these schemes include Citi Mortgage, Bank of America and JP Morgan Chase, as reported by CNBC. To view a video of the news telecast on this topic go to [www.cnbc.com/id/34877347](http://www.cnbc.com/id/34877347).

Brokers and agents should be aware of this fraud scheme and understand that it is illegal and violates RESPA. Participation in this type of short sale scheme would expose the agent and the brokerage to investigation, damages and possible criminal proceedings. Incidents of such proposals and demands should be reported to HUD.

FOR SALE SIGNS ON REO PROPERTIES

The current REO real estate market has resulted in some practices that differ from those for which the MLS Rules were originally created. Banks establish relationships with agents to sell their REO properties, often using a blanket listing agreement rather than individual separate listing agreements for each property. Before a property is ready for sale, an agent may, on his or her own initiative or on the bank's instruction, place a "For Sale" sign on a property without a specific listing agreement for that property and prior to placing the property into the MLS. When a buyer's agent sees the "For Sale" sign and tries to get the property information on the MLS, there is no listing. When the buyer's agent calls the listing agent to get information on the property, he is told the property is not yet ready for sale. However, if a potential buyer without an agent inquires about the property, the listing agent encourages the caller, gives information about the property, asks for and obtains the potential buyer's name and information, and says they will be contacted when the property is ready to be shown.

The agent's conduct in this example violates the MLS Rules in several respects, creating potential liability for the broker. First, the MLS Rules require the listing broker to obtain and have possession of a fully executed written agreement from the seller expressly granting authority to list the property on the MLS. A blanket agreement between the listing broker and the bank to cover unspecified property may not satisfy this requirement.

Second, the listing agent must input the listing into the MLS within 48 hours of obtaining the executed listing agreement.

Third, placing a sign on the property constitutes advertising. The MLS rules prohibit advertising a property unless you are the listing broker or have prior consent of the listing broker (except regarding Internet displays). The agent cannot rely on the excuse that the vacant property requires contact information in case there is an emergency. There are other ways to post the owner's or contact person's information on the property (for example a notice on the door or in the window). Using the agent's "For Sale" sign is not an appropriate method of providing emergency contact information. Advertising a property for sale when it is not actually ready for sale or listed in the MLS may be a form of false or misleading advertising, which is also prohibited in the MLS Rules. Marketing a property that is not listed would be a violation of the MLS Rules.

Finally, the discouragement of agents and the encouragement of unrepresented potential buyers in order to double end a sale transaction may violate the Code of Ethics. Article 2 requires agents to avoid exaggeration, misrepresentation, or concealment of pertinent facts regarding a

property or transaction; Article 3 requires agents to cooperate with other brokers and not misrepresent availability of access to show or inspect property; Article 12 requires agents to present a true picture in advertising and representations to the public and not offer for sale without authority by seller; and Article 16 prohibits placing signs without consent of the seller.

When listing and selling REO properties, agents should remember that the MLS Rules and Code of Ethics still apply, regardless of what the bank instructs or wishes the agents to do. Agents should obtain the proper specific listing agreement for each property, place the listing in the MLS in a timely manner, or obtain the bank's specific instruction in writing to withhold the listing from the MLS if the property is not ready to sell, and refrain from posting "For Sale" signs on the property until it is ready to be listed and shown.

The author of this month's newsletter is Sylvia J. Simmons, Attorney with THE GIARDINELLI LAW GROUP, APC. She can be reached at [Sylvia@glawgroupapc.com](mailto:Sylvia@glawgroupapc.com) or 951/ 245-9163.

THE GIARDINELLI LAW GROUP, APC

Riverside County Office  
31772 Casino Drive, Suite C  
Lake Elsinore, CA 92530  
951 / 245-9163

Orange County Office  
1601 East Orangewood Avenue, Suite 175  
Anaheim, CA 92805  
714 / 978-2060

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