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We have been receiving many inquiries from agents and brokers about another real state scheme in which they are being asked to participate. This month's article describes the new short sale scam of which brokers and agents should be aware.

NEW SHORT SALE SCHEME

In this new short sale scheme, an agent lists a short-sale property. An investor buyer makes an offer to purchase the property and handle all interactions with the lender to negotiate the short sale. The offer includes a full commission to the agent, 6% in concessions from the seller, and a 1% "negotiation fee." The purchase agreement includes an addendum that provides that upon acceptance by the seller, the investor buyer will immediately market the property for sale to a second buyer. The second buyer attaches an addendum to the purchase agreement that discloses the intent of the investor buyer and the second buyer to the seller and supposedly also to the seller's lender. The investor buyer and second buyer set up a double escrow on the property. They assure the seller that the investor buyer will use his or her own separate funds to close the short sale purchase transaction before the immediate transfer of the property to the second buyer.

If the ultimate buyer is an FHA buyer, the investor buyer will step back and just ask for the negotiation fee to avoid violating the FHA ninety-one day no-flip rule. The investor buyer will also step back if he or she is unable to negotiate a sale with the seller's lender at a low enough price to allow resale of the property at a profitable higher price.

Kelly Neavel, attorney at Giardinelli & Duke, APC contacted the Department of Real Estate, the California Association of REALTORS®, and the Riverside District Attorney's Office to obtain their opinions of this scheme. Here are their responses:

California Association of REALTORS® (CAR)

Most banks will not talk directly to a buyer. An investor buyer who is talking to the bank as the representative of the seller must be a real estate agent or broker. The "negotiation fee" appears to be compensation for real estate activity. Stepping back and getting a negotiation fee is only allowed if the investor is a real estate broker. If the seller's lender and the seller are informed that the investor buyer is going to flip the property, an investor buyer may buy from the seller on a short sale transaction with the seller's lender for the express purpose of resale. Additionally, if a Notice of Default (NOD) has been recorded, the investor buyer must use a contract that complies with the Home Equity Sales law, such as the CAR form Notice of Default Purchase Agreement (NODPA).

Department of Real Estate (DRE)

This scheme may constitute fraud and dishonest dealing and misrepresentation, in violation of the California Business and Professions Code (Sections 10176(a) and 10176(i)). The person doing the

“negotiating” must be licensed to engage in real estate activities. The underlying question is why would the seller/lender sell the property for less to the investor buyer if they knew (from disclosures in the purchase agreement addendum) that the property could be sold for more to the second buyer? Real estate brokers and agents owe a fiduciary duty to the buyer and seller. That duty includes an obligation to be honest. It is dishonest for the investor buyer to advise the seller that the property is worth less than the price he will sell it for to the second buyer immediately on close of the first escrow. It is dishonest for the investor buyer to convince the second buyer that the property is worth more than the price the buyer is paying.

District Attorney

The violation of the applicable California Business and Professions Code sections (see below) is a misdemeanor, which makes this scheme a crime. Complaints against licensed agents should be filed with the DRE. Complaints against unlicensed agents should be filed with the District Attorney’s Office. The Riverside District Attorneys’ Office can be reached at (877) 723-7779.

California Business & Professions Code

The B&P Code sections that may apply to real estate schemes include the following (bold emphasis added):

10175. *Upon grounds provided in this article and the other articles of this chapter, the license of any real estate licensee may be revoked or suspended in accordance with the provisions of this part relating to hearings.*

10176. *The commissioner may, ... investigate the actions of any person engaged in the business or acting in the capacity of a real estate licensee within this state, and he or she may temporarily suspend or permanently revoke a real estate license at any time where the licensee, while a real estate licensee, in performing or attempting to perform any of the acts within the scope of this chapter has been guilty of any of the following:*

(a) Making any substantial misrepresentation.

(b) Making any false promises of a character likely to influence, persuade or induce.

(c) A continued and flagrant course of misrepresentation or making of false promises through real estate agents or salespersons.

(d) Acting for more than one party in a transaction without the knowledge or consent of all parties thereto.

(e) Commingling with his or her own money or property the money or other property of others which is received and held by him or her.

(f) Claiming, demanding, or receiving a fee, compensation or commission under any exclusive agreement authorizing or employing a licensee to perform any acts set forth in Section 10131 for compensation or commission where the agreement does not contain a definite, specified date of final and complete termination.

(g) The claiming or taking by a licensee of any secret or undisclosed amount of compensation, commission or profit or the failure of a licensee to reveal to the employer of the licensee the full amount of the licensee's compensation, commission or profit under any agreement authorizing or employing the licensee to do any acts for which a license is required under this chapter for compensation or commission prior to or coincident with the signing of an agreement evidencing the meeting of the minds of the contracting parties, regardless of the form of the agreement, whether evidenced by documents in an escrow or by any other or different procedure.

(h) The use by a licensee of any provision allowing the licensee an option to purchase in an agreement authorizing or employing the licensee to sell, buy, or exchange real estate or a business opportunity for compensation or commission, except when the licensee prior to or coincident with election to exercise the option to purchase reveals in writing to the employer the full amount of licensee's profit and obtains the written consent of the employer approving the amount of the profit.

(i) Any other conduct, whether of the same or a different character than specified in this section, which constitutes fraud or dishonest dealing.

...

(m) Generating an inaccurate opinion of the value of residential real property, requested in connection with a debt forgiveness sale, in order to do either or both of the following:

(1) Manipulate the lienholder to reject the proposed debt forgiveness sale.

(2) Acquire a financial or business advantage, including a listing agreement, that directly results from the inaccurate opinion of value, with regard to the subject property.

10185. Any person, including officers, directors, agents or employees of corporations, who willfully violates or knowingly participates in the violation of this division shall be guilty of a misdemeanor punishable by a fine not exceeding ten thousand dollars (\$10,000), or by imprisonment in the county jail not exceeding six months, or by a fine and imprisonment.

How to Respond to Proposed Schemes

In summary, real estate agents and brokers need to be careful if asked to participate in this short sale scheme or similar schemes because it may be performing real estate activity without a license, could result in investigation and loss of the agent's real estate license, and it may be unlawful and subject the agent to criminal prosecution and monetary fines. Before participating in a transaction that is suspect, contact the DRE, CAR, the District Attorney, or the attorneys at Giardinelli & Duke, APC.

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