OREF, LLC Special Feature
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- A big thank you goes to our Forms Committee 2017 leadership Steve Russell, Wendy Adkisson and past FC Chairman Jeff Wiren for providing a majority of the topics.

- Answers provided by OREF, LLC Forms Committee legal counsel Phil Querin of Q-Law

Q and A: News You Can Use

OREF has developed a set of forms intended to provide useful guidance to real estate professionals documenting a variety of Oregon real estate transactions. In addition, OREF periodically provides, in its print and digital publications, guidance with respect to questions commonly posed by brokers. Neither OREF's forms, nor the statements made in its print or digital publications, are intended to constitute or provide legal advice. OREF encourages all brokers to seek guidance from their principal Brokers, and when necessary, from legal counsel, regarding real estate transaction questions. In addition, OAR offers members an annual subscription to the OAR Real Estate Hotline, which also provides brokers with consultation on real estate transaction issues. Brokers wishing to access the Hotline can find more information at http://oregonrealtors.org/legal/action/legal-hotline.

Question No. 1. How can a broker properly counter a buyer's offer in order to safely put them in backup position?

Answer. I read this question to deal with the following scenario: Listing broker receives an offer that seller is interested in keeping in play, while another, perhaps a more attractive offer is already being negotiated (or has been accepted). First, you should closely review the OREF Backup Offer Addendum (No. 009), to make sure you and your seller client fully understand your options, and the buyer's options. If you already have accepted the first-position buyer, then most certainly, you cannot accept the second offer without making sure it is in a back-up position. I have seen listing brokers permit their seller to accept one offer, and also a second offer, without making it clear (in writing) to the second buyer that their rights are subject to the first transaction being terminated.

So the take-away here is to draft the terms of the counteroffer in exactly the way you and your client want, but cross-reference it with Form 009, so that it is clear that the counter-offer, if accepted, is behind the first-position buyer. Remember, however, that all of the timelines in the back-up counteroffer, if accepted by the second position buyer, will not commence until that buyer is notified that they have been elevated to a "first position".

Question No. 2. What happens when the home doesn't appraise? Can a seller terminate the sale even if the buyer is willing to come up with the extra money? Can a buyer who is willing to come up with the extra money NOT notify the seller? Do you need any additional verbiage on an addendum that modifies the offer where the buyer and seller agree?

Answer. The standard OREF Residential Real Estate Sale Agreement (No.001) Section 5.2 provides that if the buyer:

> "…receives actual notification from Lender that any Financing Contingencies identified above have failed or otherwise cannot occur, Buyer shall promptly notify Seller, and the parties shall have _____ business days (two [2] if not filled in) following the date of Buyer's notification to Seller to either (a) Terminate this transaction by signing a Termination Agreement (OREF 057) and/or such other similar form as may be provided by Escrow; or (b) Reach a written mutual agreement upon such price and terms that will permit this transaction to continue. Neither Seller nor Buyer is required under the preceding provision (b) to reach such agreement. If (a) or (b) fail to occur within the time period identified in this Section 5.2, this transaction shall be automatically terminated and all earnest money shall be promptly refunded to Buyer. Buyer understands that upon termination of this transaction, Seller shall have the right to immediately place the Property back on the market for sale upon any price and terms as Seller determines, in Seller's sole discretion."

Technically, under this provision, the buyer is ***required*** to notify the seller if the home doesn't appraise, and the parties have two business days (unless another period of time is agreed upon) to reach a mutually satisfactory arrangement on going forward. If they cannot do so, the transaction is terminated.[1]

I read this provision to mean that if the buyer says "I'm willing to pay the difference", *the seller must still agree to this solution*, and if not (or another mutually satisfactory solution cannot be worked out) the deal is dead. Of course, the seller's likely response to a buyer's offer to pay the shortfall would be for the buyer to provide proof of funds, and then the parties would enter into an addendum memorializing this arrangement.

The OREF Forms Committee recently discussed this provision, and some members believed that there were agents who might interpret this differently, since the general rule is buyer contingencies are solely for the buyer's benefit, and can always be waived by the buyer. I don't disagree, ***except*** this specific provision requires "mutual agreement".[2]

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[1] As to the whether the buyer (in violation of the Section 5.2) can simply not inform the seller, I don't want to encourage the conduct. Quoting Robert Burns in *To a Mouse*: "The best laid plans of mice and men often go awry." One never knows if the plan to conceal the information from the seller will be later discovered. Murphy's Law says "Yes".

[2] If there a great hue and cry about this provision, readers should let OREF know, so that it can be changed to give buyers the right to unilaterally waive the appraisal contingency.

The obvious tip here is that if there is a bidding war going on, or there is a likelihood that the property will not appraise out, the buyer should be proactive, and either (a) expressly waive the appraisal contingency, or (b) waive it so long as the appraised value comes in *at least at $X*. Doing nothing in advance, and waiting until the appraisal comes in, gives the seller the opportunity to reject buyer's belated offer to pay the entire difference in cash, when there is a more attractive offer in the wings.

As an aside, it seems to me that in bidding wars, sellers should insist upon a significant earnest money deposit. It has to be high enough that the buyer is disincentivized to walk away from the deposit. Otherwise, the buyer's offer to pay the difference in cash means little, since the buyer can always break that promise, and simply forfeit their deposit.

Question No 3. How do you best explain FIRPTA to your clients without it being a huge long conversation and scaring them half to death?

Answer. The problem with FIRPTA is the penalty, i.e. making the buyer financially responsible to the IRS as its "collection agent" for the seller's taxes because the seller is a "foreign person". This is very draconian, and places the burden for vetting the seller's foreign status on someone (i.e. the buyer) who shouldn't really be expected to know or care.

Like so many other things about the IRS, FIRPTA *is* meant to scare people. If the law didn't have that *in terrorem* effect, it would get ignored. For that reason, and the fact that brokers should not be heard "downplaying" the significance of the law, there is no easy way to explain it without being accused of sugar-coating or downplaying, the issue.

This is, in my opinion, exactly why title companies and escrow officers really don't like to publicly discuss what role they will play in handling a transaction that involves a seller who is a "foreign person".

So, rather than trying to explain FIRPTA to clients "without scaring them half to death" I suggest that brokers provide their clients (sellers and buyers) with (a) a reliable information source (e.g. vetted online publications, or the IRS website) *and* (b) a recommendation that they reach out to their CPA, tax attorney, or other professional familiar with FIRPTA issues.

Remember, RMLS™ (and possibly other MLSs in Oregon) vet the issue at the listing stage, requiring the seller to declare whether or not they are a foreign person. This is the place to start. If the seller says they are a foreign person, then the buyer is on notice to secure professional assistance, if needed. In most cases, the title company will serve as the agent for purpose of withholding the proceeds and sending it along to the IRS. If the seller says they are not a foreign person, and there is no evidence to the contrary, I don't see much reason to be concerned. Since escrow must issue a FORM 1099 to the IRS and Oregon Department of Revenue, the question of seller's legal taxpayer status will likely arise early, since it will need sufficient identifying information from the seller to complete and transmit the form. If the seller has no taxpayer ID or social security number, a FIRPTA discussion is likely not far away.

However, this is not to say that a representation of non-foreign status in the seller's listing contract is a complete defense for buyers, should the IRS claim otherwise after closing. Ultimately, the only real defense upon which a buyer can rely is for the seller to sign a Certificate of Non-Foreign Status at the time of closing. If the seller refuses to sign such a Certificate upon request, and insists they are not a foreign person (or claims that although they are a foreign person, they are exempt), the seller should produce an opinion from their tax attorney or CPA to that effect. If not, it's time for the buyer to consider withdrawing from the transaction.

OREF FIRPTA forms and text (the Advisory, Addendum, and Section 15.2 of the 2017 Residential Sale Agreement[3]) all contain disclaimers to the effect that the parties should rely upon their own experts, and their real estate agent is ***not*** an expert.

Question No. 4. How should a listing broker properly respond to a Buyer's Repair Addendum without taking the risk that the lender will see it and then include the repair item(s) as a condition to obtaining the loan?

Answer. In my opinion, by the time things get to the Seller's Response, the potential problem has already started, i.e. alerting the underwriter of the need for significant repairs. The more substantial they are (as opposed to cosmetic) the greater the chance they could find their way into the loan commitment.

One way to handle material repair issues is to monetize them at the outset. For example, if the buyer's agent knows the inspection report says the roof is nearing the end of its useful life, a discussion should be held over the phone with the listing agent, to see if agreement can be reached, for example, to pay some of buyer's closing costs, or for a price reduction, or other buyer concessions, without focusing attention on the physical condition of the home. Then, the arrangement can be memorialized in an addendum, without ever having to develop a laundry list of repair items for the underwriter to see.

Question No. 5. What sort of discussion should I be having with my seller when we receive an offer in the name of the buyer that includes "and/or assigns"?

Answer. There are a lot of things to discuss, and the failure to do so before seller accepts the offer the better. What follows is a punch-list of considerations (there may be more):

- The first question is why does the buyer want to assign his/her interest? Look for a legitimate reason before agreeing to anything.
- Never accept an offer that does not place limitations on buyer's ability to assign the Sale Agreement; doing so without any limiting factors gives the buyer a free hand to determine who they will assign to, and the seller will have no ability to control the decision.

[3] FIRPTA is addressed in OREF's other Sale Agreements, but it may be assigned different section numbers.

- Sellers should *not* agree to permit an assignment with the proviso "seller's consent shall not be unreasonably withheld". Why? Because it's the seller's property, and the seller should be able to give or withhold consent in their "sole discretion". For example, what if the assignee had the same financial capacity as the buyer, but the seller thought the assignee was a jerk and didn't trust him? The only reasonable criteria for rejection would be the assignee's financial condition (all other things being equal), and if seller's consent cannot to be unreasonably withheld, seller might have legal difficulty refusing consent. (In other words, the issue is whether being a "jerk" is a reasonable basis to deny consent to the assignment? It's easier and safer for sellers just to reserve the right to give or withhold consent in their "sole discretion." That permits the seller to be arbitrary, without having to justify it.)
- Is buyer just going to flip the property? Does buyer even have the financial capacity to close the transaction on his own? Is it possible that the buyer has no intent or capacity to close, and is just looking for an assignee in order to increase the price and assign the contract to a third party, making a quick profit in the middle?
- Sometimes buyers want to assign to a related entity, e.g. an LLC, that has not yet been formed. While that isn't necessarily an unreasonable purpose, seller should still impose conditions, including that the buyer guarantee the assignee's performance (remember, the LLC may just be a shell). Also, assuming the seller has thoroughly vetted the buyer and is comfortable with them (or it), the seller should limit assignment to an entity in which the buyer has at least a 51% interest.
- Lastly, sellers should reserve the right to impose the same (or stronger) evaluation criteria of the assignee's finances, business dealings, reputation, etc.

Question 6: Why was verbiage added to the 2017 Residential Sales Agreement (Form # 001) requiring buyers to use the same lender from which they receive a pre-qualification letter. In my case, I'm a borrower with excellent credit that has multiple options for lending. It seems illogical that I would have to lock in a lender before offering. What is to stop a lender from giving me non-competitive terms once I am under contract and try to secure the actual loan if they are my only option?

Answer: It is no secret that we're still in a seller's market. This means, among other things, that sellers are quite anxious to know that the offer they've accepted is a solid one and will close on time. When most buyers make offers, they also submit a pre-approval letter. The stronger the lender (e.g. in reputation, local vs. internet, good closing ratios, accessibility, honesty, etc.) the better. So when there is competitive bidding on a property, and financing is involved, a strong well-recognized lender can prove to be the tipping point in a seller's acceptance of the offer. If a buyer got their Loan Estimate (formerly known as the "Good Faith Estimate") from the lender who signed the pre-approval letter, and then "shopped" it to other lenders, it would create undue delay. This is because under the TRID rules, the new lender has 72 hours to submit a loan estimate back to the buyer-applicant – i.e. up to three days.

See, Section 5.3 of Residential Real Estate Sale Agreement – Buyer's Representation Regarding Financing. This section contemplates a "lock-step" process, e.g. buyer agrees to make "completed loan application" within X business days (usually three). Under TRID this automatically triggers the 72-hour response requirement for lender's issuance of the Loan Estimate. Next, the buyer is required to thereafter notify the lender of their "intent to proceed" (which has a 3-business day default requirement in the Sale Agreement – in my opinion, the shorter the better). In the regular course, this means that confirmation of loan approval should take around ten days or less.

So you can see how, after the buyer's offer is accepted, that shopping the lender's Loan Estimate to one or more lenders, can completely disrupt the loan approval process. Not only is the seller kept in the dark for a prolonged period of time, but the later their buyer submits for a loan, the greater risk there is that the closing date may not be met. This is not what the seller agreed to when they accepted their buyer's offer. They understood that ABC lender "pre-approved" the buyer; they presumed that since pre-approval was issued (based upon the submission of financial information), when the "completed loan application" was received by that lender, approval should be a foregone conclusion. There is no such assurance when the buyer submits successive loan applications to unknown (and possibly objectionable) lenders after seller already accepted the buyer.

Is it fair that the buyer should be required to submit their loan application to the same lender that authored their pre-approval letter? By all means. In accepting the offer, the seller approved not only the buyer, but the buyer's lender. This is why today, most pro-active buyer brokers encourage their clients to thoroughly vet as many lenders as possible before submitting their offer. That way, there is no "borrower remorse" when a buyer is approved by a lender who issued their pre-approval letter.

Lastly, if there is a question of falling interest rates, the buyer does not have to lock the rate with their lender. If it is a question of rising rates, the buyer can get a loan lock. In short, they don't have to find another lender to secure a better rate.

So, either way, the buyer has control of the interest rate issue. As for different loan costs, that issue can be vetted by the buyer in advance of making their offer. In any event, the Sale Agreement does not say the buyer cannot apply for a loan from another lender; it merely says that before doing so, the buyer has to secure their seller's consent.

So, from the OREF Forms Committee's perspective, this new requirement was fair and equitable, given the marketplace we're in today.

The Q and A of the **August 2017, *Principal Broker Quarterly*** will be posted on the OREF, LLC website. After July 27, 2017, click on the associated links noticed in the e-news and this document will be linked to the website.