

Use Caution With REO Agreements



Many real estate buyers and sellers like to focus on Real Estate Owned, or REO, properties because these can be inexpensive compared to the standard real estate transaction. REO properties are usually owned by the bank or real estate company, but are not as safe as one might think in regards to your Errors and Omissions liability.

REO properties are often homes that have gone through foreclosure, been taken back by the bank, and usually sold “As Is” to the next buyer. Many homeowners or business owners are quite distressed at the time of foreclosure and do not have the financial ability to physically maintain the property. Unfortunately, when selling the property to a new owner, the bank, lender, or other owner of the property may not be required to provide a disclosure statement, leaving buyers to fend for themselves in discovering defects of the property or other damages left by the previous owners.

Many real estate professionals have been taking advantage of REO listings because people are interested in acquiring properties for flipping purposes or to renovate and sell them for a profit. Not only can “flipping” lead to adverse outcomes, but REO contracts can also be precarious. These agreements can leave firms exposed to liability not covered by typical E&O policies such as those provided by Pearl Insurance. According to the article “Lenders Stick Listing Agents With REO Liabilities” by Matt Carter in Inman News (www.inman.com), “some lenders are crafting listing agreements that attempt to shift the risk that comes with sales of bank-owned homes—including property defects and personal injury claims—onto real estate brokers.”

Other real estate professionals are picking up REO properties for the sake of having as many listings as possible to offer clients. In the aforementioned article, real estate attorney Harold Justman is quoted as saying, “Some of these listing agreements are lethal or have lethal provisions in them. You may have a knee-jerk reaction, and say, ‘Oh boy, now I have 100 listings.’ But a year from now, one lawsuit might wipe out all your profits.”

The lesson to be learned is to take time to analyze any REO contract before signing it. Banks and lenders are adept at protecting themselves with legal jargon, and often these agreements can be upwards of 30 pages. Since the property is sold “As Is,” spend substantial time considering the risks of unforeseen defects or other problems with the property in the future.

In addition, most E&O policies have exclusions, including when you agree to assume the liability of others—common in the case of REO properties. Yet it’s often part of an REO agreement, so again, read the contract carefully. Pearl Insurance E&O Consultants advise their clients to never sign a listing agreement that contains this last provision since it essentially makes you liable for the alleged misrepresentation of or failure to disclose property defects. Help protect yourself from claims involving REOs and questionable REO contracts—spend the necessary time to understand any REO agreement you’re contemplating and what your E&O insurance will or won’t cover.

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