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July 21, 2011

VIA EMAIL & FIRST CLASS MAIL

Grand Rapids Association of REALTORS®
Attn: Pam Dyke, Senior Vice President
660 Kenmoor Avenue, SE
Grand Rapids, MI 49546

Re: Payments for Personal Property Outside of Closing or Short Sales

Dear Pam:

The Grand Rapids Association of REALTORS® ("GRAR") Board of Directors has requested a written opinion with respect to a practice which is becoming prevalent not only within GRAR's market, but elsewhere in Michigan.

GRAR is beginning to observe short sale transactions in which the Seller, upon completion of the closing, receives cash as a result of the purported sale of personal items by the Seller. These personal items and the terms of their purchase are often listed on a separate addendum, the existence of which is not disclosed to the lender who has approved the short sale on terms which do not include the Seller receiving cash for personal items. Further, the sale of the items and the Seller's receipt of cash are not referenced on the HUD-1. In addition, the fair market value of the personal items does not remotely equal the amount paid for them. I note this practice is used either to provide cash to a Seller as part of the transaction or to provide additional compensation to a junior lienor in an amount not approved by the lender with the first priority in order to induce the junior lienor to discharge their lien.

Section 4 of the Real Estate Settlement Procedures Act ("RESPA") requires that a standard state form for the statement of settlement costs be used in all transactions which involve federally related mortgage loans. This form is commonly known as the HUD-1. Lines 102 and 402 of the HUD-1 specifically require the disclosure of any payments made by the Buyer to the Seller for personal property. If the sale of personal property occurs before or after the closing, but is part of the transaction, then it would be reflected on the HUD-1 as "POC" for "Paid Outside of Closing."

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Obviously, the failure to include the personal property on the HUD-1 constitutes a violation of RESPA. However, that may be the least of the problems a Seller could encounter by inducing a lender to agree to a short sale while concealing from the lender the fact the Seller is receiving cash from the Buyer allegedly for the sale of personal property.

Bank fraud under federal law is described in 18 USC § 1344. The statute provides:

Whoever knowingly executes, or attempts to execute, a scheme or artifice –

- (1) to defraud a financial institution; or
- (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises;

shall be fined not more than \$1,000,000 or imprisoned not more than 30 years, or both.

The undisclosed receipt of cash by the Seller in a short sale which would have otherwise been paid to the lender, but for the knowing concealment of the transaction by the Seller could be a violation of this law.

The risk of being guilty of bank fraud under the above-cited statute is not limited to the Seller who receives the cash. Other persons with knowledge of the transaction may also be liable as aiding and abetting in the crime under federal law. 18 USC § 2 provides:

- (a) Whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal.
- (b) Whoever willfully causes an act to be done which if directly performed by him or another would be an offense against the United States, is punishable as a principal.

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It should be noted under this statute, a person who aids and abets in a crime is punishable as a principal, *i.e.*, is equally guilty. In other words, if the listing or selling REALTOR® has knowledge of the cash transaction and proceeds with the closing, they very well could be in violation of this statute.

Criminal liability could also be asserted against persons other than the Seller under another provision of federal law. 18 USC § 1349 Attempt and Conspiracy provides:

Any person who attempts or conspires to commit any offense under this chapter shall be subject to the same penalties as those prescribed for the offense, the commission of which was the object of the attempt or conspiracy.

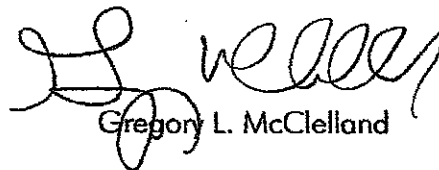
Again, if the listing or selling REALTOR® has knowledge of the cash transaction, he or she could be deemed to have conspired with the Seller and thus would be subject to the same punishment.

I note that there are parallel state criminal laws which also could come into play in this situation. I have not provided references to those laws, as the above-described federal laws should be sufficient to demonstrate the potential seriousness of participating in a transaction where the Seller's receipt of cash for personal property is knowingly concealed from a lender and is not reflected on the HUD-1.

Unlike during the real estate boom days when there seemed to be little concern about mortgage fraud through over valuation of properties, state and federal authorities have now committed substantial resources to policing mortgage or bank fraud. REALTORS® must distance themselves, *i.e.*, not participate in transactions where a Seller is receiving cash in the context of a short sale through the dubious purchase of personal property which is knowingly concealed from the lender approving the short sale and is not reflected on the HUD-1. It will be extremely difficult to formulate an effective defense for the REALTORS® if they have knowledge of and participate in this type of transaction.

Please contact me if you have any questions. Thank you.

Very truly yours,



Gregory L. McClelland

GLM/jkb

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