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FULL DISCLOSURE

Buyers Rely on 1968 Federal Law to Terminate Contracts



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In this recessed economy, where real estate prices and sales have plummeted, it should come as no surprise to developers that purchasers do not want to close on properties they contracted to buy when the market was hot. In new construction deals, it is common for a buyer to sign a contract as much as two years prior to closing, and in today's market, that could mean a substantial decrease in the value of the property from when the buyer originally signed the deal.

Although many developers were not worried about the decline in values with respect to properties that were under valid and enforceable contracts, some purchasers decided to just walk away from the deal and forfeit their deposits since the loss of deposit monies was far less than the loss in a property's current value.

Other creative purchasers, or shall we say those with creative attorneys, have turned to the Interstate Land Sales Full Disclosure Act of 1968 (15 U.S.C. §1701, et seq.), and the federal regulations promulgated thereto (24 C.F.R. 1710.1, et seq.) to get out of new construction contracts. The act was enacted in 1968 to protect purchasers who were buying land in another state that was advertised as a tremendous development opportunity. At that time, buyers would not typically visit a property until after the closing and would arrive to find a swamp or other worthless type of property. The act is still in effect today to protect buyers. It continues to impose certain obligations on developers who utilize state commerce and in today's technologically advanced world, any developer that offers properties for sale through the use of e-mail or a site dedicated to the project could subject themselves to the interstate land law.

The act requires developers to register subdivisions of 100 or more lots (including condominium units) with the Secretary of Housing and Urban Development (HUD) and to deliver to each purchaser a disclosure document (called a property report) prior to signing the purchase agreement. Section 1702 of the act does contain certain exemptions from the requirements. For instance, if under a contract of sale a developer obligates itself to complete construction of a unit within two years, then the act will not apply to that contract.

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As many practitioners know, it is a rare occasion that a developer will obligate itself, in writing, to complete a project within a specific time frame. As such, many new developments in New York City with 100 units or more would not be exempt from the requirements imposed under the act.

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There are a significant number of cases pending in the U.S. District Court in the Southern District and other federal courts in New York, Florida and other states throughout the country whereby the plaintiff purchasers are seeking return of their deposits claiming they had a right to rescind their purchase contracts based upon the developers' failure to comply with a number of requirements of the act, including the failure to register with HUD, to deliver the required property report, and/or to provide a seven day right of rescission disclosure. Some buyers have also argued that developers have violated the act by failing to deliver a deed for the property within 180

days after the contract was signed in cases where the purchase agreement did not include an identifiable description of the property, as required under the act (§1703(d)).

Violations of the act entitle an aggrieved party to certain rights and remedies including, without limitation, revocation of the purchase contract. The act provides, in relevant part, as follows:

In the case of any contract or agreement for the sale or lease of a lot for which a property is required by this chapter and the property report has not been given to the purchaser or lessee in advance of his or her signing such contract or agreement, such contract or agreement may be revoked at the option of the purchaser or lessee within two years from the date of such signing, and such contract or agreement shall clearly provide this right. (See 15 U.S.C. §1703(c)).

In addition to the right to terminate the contract, §1709 authorizes a purchaser to bring an action, at law or in equity, against a developer who violated §1703(a). Section 1709 provides that the "court may order damages, specific performance or such other relief as the court deems fair, just and equitable."

It appears that many developers chose to take the risk of not registering with HUD because, during the real estate boom, the benefits seemed to far outweigh the risks. In this new post-Madoff and federal bailout economy, this is no longer the case. Coincidentally (or not), since these lawsuits have been filed, there appear to be a number of registration applications recently filed with HUD by developers whose status is listed with HUD as "pending."

The Interstate Land Sales Full Disclosure Act seems clear: if a developer does not fall under any of the exemptions provided for in §1702, then it must register with HUD and comply with the requirements under the act. As of the date of this article, to our knowledge, none of the New York federal cases have been decided. Depending upon the outcome of those cases, the flood gates could open up to a significantly larger number of purchasers looking to terminate their contracts and seek the return of their deposits.

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