Lead Committee: Transaction and Regulatory Committee
Level of Government Committee: Legislative Committee

12/15/2013

BROKER INDEMNITY REQUIREMENTS FOR AUCTION COMPANIES

THE QUESTION

Should C.A.R. sponsor legislation to require auction companies to indemnify or "hold harmless" the listing broker in a transaction against any liability that results from the auction company's fault when they have been required (by a lender/servicer) to verify value in a sale?

ACTION REQUIRED?

Optional.

POSSIBLE POSITIONS

1. Sponsor legislation to require auction companies to indemnify listing agents for auction company acts of negligence or malfeasance.
2. Prepare contract addenda, disclosures and educational resources for agents and principals that will explain the role of an auction company and protect listing agents from liability from the auction.
3. Other.
4. Take no action.

DISCUSSION

Some lenders or servicers have begun to experiment with the use of auctions as a way to validate the fair market value of a potential short sale. In addition to traditional valuation methods like a broker price opinions (BPO) or appraisals, the servicer will approve an accepted short sale contract

contingent upon the short seller (and sometimes his or her agent) agreeing to allow the home to be put out to the public at auction for some period of time.

In the Nation Star/Auction.com model, for example, the servicer requires the short seller (and buyer) to allow the property to be put at auction by the auction company for about three weeks, after which the property may be approved for sale (still a short sale) to the high bid. If the initial short sale contract is higher, and is high enough to meet the servicer's reserve price, the sale will be approved. Auction.com indicates that while a five percent buyer's premium applies to successful bidders, the original buyer will not be charged the premium, even if the buyer participates in the auction as a bidder and bids up the price in order to buy the home.

During discussions of the (now sunsetted) Distressed Property Task Force, and in communications with REALTORS® in the field, considerable concern has been expressed that the loss of control over the sales transaction during the auction process might create liability for the listing agent. Several theories have been raised, including: some sort of interference with contract rights, inherited liability for an auctioneer's inappropriate conduct or botched disclosures, or even violation of fair housing laws because the buyer's premium (which normally cannot be charged to a buyer in FHA and VA transactions) might create a "disparate impact" fair housing violation by prejudicing protected groups.

Staff is not aware of any lawsuit yet in which the listing agent has been hit with inherited liability from the auction company, but the widespread use of auctions to validate pricing is a relatively new phenomenon.

Is it appropriate for C.A.R. to sponsor legislation to proactively address indemnity liability protection?

It should be remembered that auctions of single family homes, especially if they are held by lenders as "REO" or post-foreclosure properties, are not a new event nor are they alleged to be illegal. The new permutation is the interjection of the auction mechanism into an accepted short sale as a way for lenders to validate the fair value of the proposed short payoff.

Both auction companies and lenders and servicers will be inclined to oppose an attempt to preemptively impose liability upon their transactions, especially if no track record of illegality or of liability can be demonstrated. An alternate or supplemental path might be to provide REALTORS® auction-specific documents and disclosures that can appropriately manage customer expectations, and which can preserve agents against liability.

Note that not only listing agents are covered in the proposal -- cooperating or selling agents have other concerns, especially regarding the expectations of their buyers who may be distressed to see

"their" property being offered at auction, and maybe even starting at a lower price. Agents may also fear that buyers, especially investors, may try to game the system by going to contract with a "low-ball" offer and then trying to preserve it at auction.

Would it be better to educate REALTOR® members about how to respond to an auction and to provide them with tools to manage client expectations than to sponsor a potentially controversial bill?

Or would it be better to attempt BOTH the indemnity legislation and the education campaign?