



Accepting offers “subject to bank approval” and short sale issues

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In this environment of increased numbers of homes on the market that are in the process of foreclosure, or that have been foreclosed, Realtors are becoming involved in more unique and complicated transactions. In some of these transactions, the seller does not have sufficient equity to sell the property without coming to closing with additional cash to fund the difference. Where the seller does not have enough equity, does not have money to make up the difference, and has to sell due to circumstances outside his or her control, the seller may contemplate a “short sale”.

Although people define this term in many ways (some definitions we hear might even surprise you), the concept is simply that the seller owes more to the bank than the sale to the interested buyer will fund, and the seller is asking the bank to release the mortgage, despite the fact that the sale won't itself satisfy the debt owed to the bank in its entirety.

The focus of this article is the technique many agents have used, writing on a purchase agreement that it is “subject to bank approval”. Putting aside for a moment the fact that this language is vague, does not contain a date the parties are requiring a response from the bank, and that it does not explain what will happen if the bank fails to approve the agreement, there is a more pressing issue. We have heard the following scenario on multiple occasions:

- Buyer 1 makes an offer to purchase Seller's property for an amount less than Seller owes to the bank;
- Seller accepts the offer “subject to bank approval” and submits it (Agreement 1) to the bank for their review/approval on a “short sale”
- Seller then receives a second offer (from Buyer 2), and accepts it (Agreement 2) “subject to bank approval” without telling Buyer 2 that Seller has already accepted an offer, and without making the Agreement subject to cancellation of a previous agreement

“Subject to bank approval” is quite simply a contingency. It is very similar to “subject to an inspection”. If Seller accepted an agreement with Buyer 1, subject to an inspection contingency, would Seller then be in a good position to enter an agreement to sell the property to Buyer 2, also subject to an inspection contingency? Of course not, unless the second agreement was contingent upon cancellation of the first.

The problem that could arise in the inspection scenario is that both buyers could have an inspection and determine they like the property enough to proceed to purchase under the original terms of the agreement. The same problem exists with a seller accepting two offers “subject to bank approval”. The Seller then has two valid agreements, both of which have a contingency to be met by the bank.

The bank could then decide to approve both agreements (removing the contingency), to increase their chance that one of the two agreements will ultimately proceed to closing. The bank knows that the problem of dealing with the two accepted agreements is now the issue of the Seller, rather than the bank. With the “subject to bank approval” contingency lifted, the Seller has the potential liability for having sold the property to two different buyers.

The result is that listing agents and sellers in short-sale transactions need to carefully consider this issue and avoid the scenarios described here. Listing agents should not be afraid to refer sellers to their attorney for advice and guidance, or to seek legal counsel when in doubt on the effect of issues such as negotiating or accepting multiple offers in a short sale.

