

Contract of Sale--Security Deposits; Contract Changes

Legal Opinion: GHM-0061

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Subject: Contract of Sale--Security Deposits; Contract Changes

December 21, 1992

MEMORANDUM FOR: Brigid Bohan, Chief Counsel, Newark Office, 2.5G

FROM: George L. Weidenfeller, Deputy General Counsel
(Operations), GG

SUBJECT: Contract of Sale for Salem Lafayette Apartments
Jersey City, New Jersey, Project No. 031-84001
(601645i/GHM:L-1318)

This is in response to your memorandum of November 13, 1992, regarding the contract of sale for Salem Lafayette Apartments, Jersey City, New Jersey. Pursuant to the memorandum signed by me on September 21, 1992, Delegation of Responsibility to Regional Counsel to Prepare Contracts of Sale for the Disposition of HUD-Owned Multifamily Projects ("Delegation Memorandum") (see attachment), if Counsel are asked to prepare a contract of sale that requires substantial changes to the Model Contract, they must submit a draft of those provisions for review and approval by the Office of Insured Housing and Finance, Multifamily Mortgage Division ("Multifamily"). As the proposed contract of sale drafted by you deviated substantially from the model contract, I forwarded your memorandum along with the proposed contract of sale to Multifamily for their review.

Your memorandum raises several concerns regarding the language in paragraph 4(b) of the Model Contract captioned "Security Deposits." New Jersey State law provides that a tenant is entitled to interest on his or her security deposit upon refund of that deposit. The Model Contract does not refer specifically to interest on security deposits because the law differs from State to State. However, Multifamily has revised paragraph 4(b) to make clearer HUD's responsibility with regard to the interest earned on security deposits. The revision of paragraph 4(b) is as follows:

4(b) Any security deposits collected from residents and paid over or credited to Seller prior to the Closing, together with any accrued interest if State or local law requires that security deposits be maintained in an interest bearing account for the benefit of the tenants, shall be transferred and assigned to Purchaser at Closing.

Therefore, this paragraph should be substituted into the Model Contract for use in the contract of sale of Salem Lafayette Apartments and any future sales.

Your memorandum questioned why the contract of sale must be recorded. Multifamily is unclear why you think that they require the contract of sale to be recorded. The Delegation Memorandum explains at page 2 that the Riders to the contract of sale should be made a part of the deed, which is to be recorded:

"Attached to the Contracts, and incorporated by paragraph 26 of the Contracts, are Riders that should be used in preparing a Contract of Sale, when they are applicable. Upon closing, the Riders will become deed restrictions. You should prepare a deed to be recorded that includes those restrictions." (Emphasis added.)

Additionally, the language of the Riders provides: "The Deed shall include the following provisions." The deed should be drafted so that the restrictions outlined in the Riders run with the land. This is required by paragraph 25(b) of the contract.

With respect to the contract in general, the Model Contract should be utilized with the changes approved in this memorandum. Paragraphs 1-26 of the Model Contract are necessary for most sales because they provide a consistent and uniform method of selling and closing sales of multifamily properties. It is important that HUD be consistent in the sales contracts that it offers to prevent purchasers from lobbying different Regions for different terms of sales. Additionally, the standard provisions of the Model Contract have been written because of past problems or lawsuits involving the sales and closing of multifamily projects. Also, it is important to keep in mind that the contract was concurred on by Housing.

As this is a sale from HUD to the City of Jersey City (Municipal Purchaser), and from the City to the Housing Assistance Corporation of the New Jersey Housing and Mortgage Finance Agency (State Purchaser), the contract should, as in the proposed contract of sale, where appropriate, refer to the Municipal Purchaser and the State Purchaser. It is generally the policy of Multifamily to draft a contract between HUD and the City, and require the City to draft the contract between it and the entity purchasing the project. However, as this is a simultaneous closing and the sale to the City is for the express purpose of removing liens, the contract may reflect both transactions.

The following changes may be made to the Model Contract:

- (1) The paragraph, as set out on the first and second pages of this memorandum, regarding security deposits may be substituted for paragraph 4(b);
- (2) The following paragraph from the proposed contract, 5A, may be added to section 3 of the Model Contract,

"Closing, Closing Expenses and Transfer of Possession":

"The Municipal Purchaser shall receive no income, nor be responsible for any expenses, associated with the current operation of the Property before or after the sale, provided, that there are no municipal liens attached to the Property when it transfers title to the State Purchaser."

(3) The following paragraph may be substituted for paragraph 18 of the Model Contract, "Acknowledgement of Terms and Conditions of Sale":

"Purchaser affirms that it has full knowledge of the terms, conditions, and requirements contained in this Contract."

Multifamily has a couple of other concerns with the proposed contract of sale. The proposed contract of sale just requires an initial deposit at Closing into the Reserve Fund for Replacements Account. The contract should also provide for an annual contribution to be paid monthly. See paragraph 2 of the Delegation Memorandum and paragraph 2(b) of the Model Contract.

The proposed contract of sale does not require a letter of credit, yet the authorization provides for repairs to be made to the project. If repairs are to be required of the purchaser, the contract of sale must include paragraph 3(c) of the Model Contract which requires the purchaser to provide a letter of credit. See paragraph 3 of the Delegation Memorandum.

The contract of sale should include the Rider entitled "Equity Participation" as the price of the project is \$1.00. Where HUD suppresses the price of a project, an "equity kicker" should be included in the contract of sale. See paragraph 14 of the Delegation Memorandum.

The Riders to the contract should provide a space for the purchaser and the HUD representative to initial the Riders, since they are attachments to the contract of sale and the signatures to the contract might not suffice to provide evidence of notice to both parties. See page 2 of the Delegation Memorandum.

If you have any questions, please contact Gayle E. Bohling at (202) 708-4107.

Attachment