

Flipping out over condo flipping

While brokers bought investment units without problem during the boom, doing so now is cooking up controversy February 01, 2010 07:00AM **By Candace Taylor**



During the real estate boom, it was common and even encouraged for brokers to buy units in the new development buildings they were marketing. After all, what endorsement could be better than a six-figure down payment?

But now that buyers are scarce, a number of problems with brokers purchasing units have surfaced, from unethical dilemmas with flipping to price inflation to whether brokers can be considered "bona fide" purchasers. These issues often went unnoticed when prices were roaring upward, but can threaten a condo development's very existence in today's litigious environment.

"In the past, there was absolutely no issue because these buildings were sold out, and who cares what the broker did?" said Anne Salisbury, an attorney in the real estate litigation group at Guzov Ofsink. "Now that you've got empty units, it can become an issue."

For years, marketing firms urged their brokers to buy units in the new development buildings they were tasked with selling.

"It's a sort of stamp of approval for the building," said Jennifer Lee, the director of new business development at aptsandlofts.com, who noted that the brokerage encourages its agents to purchase property.

When the lead agent at the Edge in Williamsburg, Jordan Silver of the Developers Group (which has since merged with TREGNY), went into contract for a one-bedroom unit in the building in April 2008, his firm put out a press release bragging that the building "is so hot" that its

"exclusive sales and marketing agents are not only selling its apartments, but will soon be calling it home."

Silver said his dual status as agent and future resident (units in the building haven't yet closed) gives more weight to his sales pitch.

"In a lot of ways I've really put my money where my mouth is," said Silver, who has lived in Williamsburg for years and expects to be a regular on the full-length basketball court at the Edge.

But unlike Silver, many agents bought apartments as investments rather than places to live. And with prices rising during the boom, they were able to resell their units for hefty profits, sometimes without even closing on them. That practice, known as "flipping" a contract, was done by some of the industry's most high-profile brokers. In 2005, for example, Corcoran Group CEO Pamela Liebman purchased a \$1.21 million two-bedroom condo at the Orion Condominium, a 58-story tower marketed by her firm, according to city documents. In March 2007, Liebman and the sponsor signed an agreement giving another purchaser, Mehran Shahsavari, the right to buy the apartment. In exchange, Shahsavari -- who eventually closed on the unit -- was to pay Liebman a fee of \$468,223. Liebman did not return calls for comment.

The 550-unit Orion quickly sold out, so her flip likely had little impact on the fate of the building. But in the current climate, new developments are selling slowly and many buyers are suing to get out of their contracts -- both of which can make brokers' purchases problematic for new condos.

First, there's the question of whether brokers are considered legitimate buyers. In order for a new condo plan to be declared effective, the sponsor must sell 15 percent of the units to "bona fide buyers"-- in other words, buyers other than the sponsor, the selling agent, the managing agent or one of their relatives or business associates, explained Richard Cohen, a real estate attorney at Friedberg Cohen Coleman & Pinkas.

A developer also needs at least one of the bona fide buyers to close on a unit within a year of the project's original projected date of completion. If not, all of the purchasers must be offered their money back.

It's not entirely clear whether the law considers sales agents bona fide buyers, but when buyers were plentiful, it didn't matter much. Now that projects are struggling to sell, however, more developers are counting brokers among their bona fide buyers. That gives ammunition to purchasers suing to get out of the contracts, many of whom claim that brokers can't be classified as legitimate buyers.

In December 2008, tenants at the condo conversion 30 Lincoln Plaza sued the developer, demanding the offering plan be revoked. Among other things, they claimed that sales to brokers in the building -- including Prudential Douglas Elliman's Matthew Gulker, Lor Gozum from Bellmarc Realty, Halstead Property's Michelle Kim and Oren Shalev from Anchor Associates -- should not be included in the 15 percent needed for the offering plan.

The developer, Howard Milstein, had submitted an affidavit counting those as bona fide sales (see ["Milstein dynasty back in fray"](#)). The Milstein family declined to comment on the lawsuit.

"Each of the foregoing brokers who purchased units in their own name received commissions from the sponsor and should have been considered business associates of the sponsor," the suit said.

Salisbury said the courts will likely evaluate each situation individually to determine whether the agent in question is a legitimate buyer.

The situation becomes infinitely more complicated when brokers are allowed to flip their contracts.

In Florida and other areas rife with boom-time speculation, buyers frequently signed contracts on new condos, waited for prices to rise, and then assigned the contract to someone else for a fee. Since all of this occurred before closing, the flipper avoided closing costs.

Real estate attorney John Serpico explained that traditionally, the permission required from a developer to assign a contract was rarely given in New York, but as prices skyrocketed during the boom, contract assignments like Liebman's began occurring more frequently.

One of the most high-profile examples is the now-notorious new development One Madison Park, which is embroiled in a flurry of lawsuits from buyers and brokers. The developers of the Flatiron tower, Ira Shapiro and Marc Jacobs of Slazer Enterprises, made it clear from the beginning that buyers -- including brokers -- would be allowed to flip their contracts, insiders said. In fact, the developers themselves even engaged in the practice, according to court documents, which state that Shapiro and Jacobs offered buyers Harvey and Marcia Schiller \$850,000 to terminate their contract after receiving a higher offer.

Several of the Brown Harris Stevens agents marketing the project, including top brokers Wendy Maitland and Wilbur Gonzalez, purchased units in the building. City documents show that Maitland flipped her contract for unit 11A to buyers Rosanne and Edward Braun of Northport, Long Island, for an undisclosed sum. The Brauns became the first buyers to close in the building.

Brown Harris Stevens defended its brokers. "Any sales and the subsequent assignments by BHS agents at One Madison Park were done with the full knowledge and consent of the developers," a statement from the company said. "Based on documentary evidence, BHS agents were not in breach of any disclosure obligations or fiduciary responsibilities."

But experts say allowing insiders to purchase low-priced units with plans to flip them is risky. Not only does it falsely inflate prices and sales figures, but it also leaves the building in jeopardy if those buyers are unable to quickly unload their units.

"It creates this false appearance to the buyers about how well it's selling," said Cohen.

For brokers, there's also an ethical component to flipping. A broker has a fiduciary duty to the seller and in theory should never try to sell their own units while still working for the developer, explained Marilyn Harra Kaye of MLBKaye International Realty.

"You're representing the seller," she said. "You're not there to make money on this guy."

When units were selling fast, the rule likely seemed immaterial. But now, flipping by brokers may constitute a conflict of interest.

"Now that the market is slower, knowing that there's an extra apartment owned by the broker on the market in addition to all the unsold units, it becomes an issue of, 'Are you creating competition on these sales by trying to flip your apartment?'" explained attorney Debra Guzov, the co-founder of Guzov Ofsink.

One Madison Park sold quickly at first, but was never more than 70 percent sold, explained Elliman's Tamir Shemesh, who is now marketing the building. Then, more sponsor units became available as buyers pulled out of their contracts, noted Shemesh, who said he is currently selling 35 of the roughly 70 units in the building.

Brokers and buyers allege that Maitland and Gonzalez, who had signed contracts for units in the building, directed potential buyers to their listings rather than the sponsor's.

Maitland, who has since sued the developer over a loan she claims was never paid back, denies any wrongdoing.

"I did nothing unethical," she wrote in an email to *The Real Deal*. "Of course there was no action that was ever taken that was done without the sponsor's consent and blessing, with full disclosure."

Shemesh said Elliman no longer allows contracts to be reassigned in the building. "The developer realized that giving the right to flip is actually hurting the project at the end of the day," he said.