

RETURNING DEPOSITS TO GET DEALS DONE

Some developers opt to give old buyers down payments back and move on to new ones

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By Candace Taylor



In the midst of the real estate downturn, reams of new condo buyers -- facing job losses or simply spooked at the sudden drop in the values of their apartments -- refused to close on their units.

Equally spooked developers responded by sticking to their guns, refusing to return deposits that often reached six or seven figures. For a time, the resulting flurry of lawsuits and complaints to the Attorney General effectively crippled the new development market.

While some developers are still taking a firm stance on deposits, others are starting to negotiate with buyers who want out of their contracts. Given the high cost of litigation and the long wait for resolution by the AG, many prefer to cut a deal with unhappy buyers and move on to the next sale.

"At first it was, 'I'm going to fight you,'" said real estate attorney Allison Scollar of Gold Scollar Moshan. "But if [a developer] has 50 people threatening to sue, why not get rid of those people and start with a clean slate? They have to lower the prices anyway."

That's especially true in buildings already in severe financial distress, she said. A developer who already owes millions of dollars to the bank may not have the resources to litigate over individual deposits. Returning the deposit, or part of it, and reselling the unit to someone who is willing to close, even at a lower price, sometimes makes more sense.

"There is a cost to not being able to sell," said Alan Fried, a partner at real estate law firm Braverman & Associates. "If you have a \$4 million apartment that you can't sell because you're fighting over the \$600,000 deposit, it may be better to get [a lower price] than to keep the deposit after a year of nothing. It's an analysis each sponsor has to do."

As a result, the gridlock caused by the backup of contract disputes has finally started to clear, and few new squabbles are following in their footsteps, allowing sponsors and their lenders to move on.

"[With] a lot of these contracts, deals have been struck or deposits have been returned," said Steven Sladkus, a partner at Wolf Haldenstein Adler Freeman & Herz, adding that it's one reason why "things have picked up" for new developments.

That's quite a change from the aftermath of the Lehman Brothers collapse, when buyers backing out of their contracts often found developers unsympathetic.

One such buyer was James Pham, who with his wife Elizabeth lost a \$95,000 deposit on a two-bedroom apartment at new condo Maxwell Place in Hoboken. When it came time to close in the fall of 2008, banks said they couldn't get a mortgage without putting down at least another 10 percent.

The Phams had put their life savings into the deposit and couldn't come up with the additional money, James said. They appealed to Toll Brothers for the deposit back. James, who at the time was working as an agent at Keller Williams Realty, also offered to help resell the unit. Toll Brothers "refused to budge," said James. "They really didn't care."

The Phams sued, but an arbitrator found in favor of the developer since their contract, like the vast majority of those signed during the boom, had no mortgage contingency clause. The family, which spent thousands on attorneys' fees in addition to the lost down payment, was forced to move in with James' brother in California. "For them, \$95,000 is a drop in the bucket, but for us it was a significant portion of our wealth," James said.

In a statement, Toll Brothers said it was "pleased with the arbitrator's finding that the Phams are sophisticated real estate professionals who did not fulfill their contractual obligations."

Many developers initially reacted the same way, fearful that if they allowed one buyer to negotiate, others would want to follow.

But as the downturn marches on, some developers have found that there are benefits to negotiating. This can mean lowering the price to help a deal close, returning some or all of the buyer's deposit, or reassigning the contract.

Scollar recently represented a buyer at the new 130-unit condo Crescent Club in Long Island City, where buyers were given the "right of rescission" -- the opportunity to cancel their contracts and get their deposits back -- after the developer, NCF Equities, missed the promised delivery date. Scollar's client didn't ask for his money back before the 30-day window on the offer expired, but later changed his mind. To Scollar's surprise, the developer returned the deposit immediately.

Offering the right of rescission often spells financial disaster for a new condo, so developers may not feel it's worth the additional expense to battle individual buyers, she said.

Indeed, if there are a large number of buyers who want out, it may be better for the developer to let them go, and start over with new buyers who want to close. "You don't want 50 lawsuits," Scollar noted.

Crescent Club developer Ari Chitrik did not respond to calls for comment.

Even at projects in relatively good shape, developers now seem more willing to negotiate with buyers who want out of their contracts.

Developer Henry Justin recently returned half of a buyer's \$230,000 deposit while waiting for the AG's office to resolve their dispute over the contract. "It's almost like a divorce," Justin said. "You don't know where the judge is going to go. If you split the difference, you might be better off."

And cutting the buyer loose enabled Justin to resell the unit to someone else, albeit at a lower price.

Donald Capoccia, the developer of the Downtown Brooklyn condo Toren, said he has allowed several buyers to find new sellers to take over their contracts. But he emphasized that his compassion extends only to buyers who have legitimate reasons for not closing. "If they're being forthright with us, we'll work with them," said Capoccia, who developed Toren with partners Joseph Ferrara and Brandon Baron. Otherwise, "we have a contract and it allows for certain remedies. We'll pursue those."

Like Capoccia, many developers are less tolerant of flimsy excuses and more willing to work with buyers who have legitimate reasons not to close. Sladkus recently represented a buyer at a new development in Chelsea who discovered that the living room of her unit "was literally half the size of what was represented in the [offering] plan," he said.

His client filed a request to have the matter decided by the AG's office. While they were waiting for a decision, the developer "offered a significant concession in the price," and the deal closed, Sladkus said.

"There are costs associated with duking it out," he said. "It ends up being a cost-benefit analysis."

That's especially true when an unhappy buyer files a lawsuit as opposed to a complaint with the AG. Not only are lawsuits more expensive, but often the unit can't be resold until the dispute is resolved, meaning the developer must continue to pay carrying costs on the apartment.

The good news is that as more of these disputes are settled, there are few new ones taking their place, now that many of the boom-time buyers' closing dates have come and gone.

The clearing of that logjam is one reason sales activity is beginning to accelerate, now that developers can reduce their prices and find new buyers.

"There's been a flushing out," said Wayne Heicklen, cochair of the real estate group at Pryor Cashman. "Those cases are slowing down."