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TREC One to Four Family Contract

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TREC One to Four Family Contract Overview

I. Introduction

This paper will give a brief overview of the Texas Real Estate Commission's ("TREC") One to Four Family contract with a focus on provisions that warrant particular attention from the lender, address some frequently asked contract questions and discuss the proposed changes currently being considered by TREC.

TREC's Broker/Lawyer committee is very active and not shy to suggest changes to our promulgated forms when needed. These changes are made to reflect current practices, comply with new laws regarding required notices and adjust to new lending guidelines.

Currently, TREC has published additional changes for public comment with the intent that, pending comment, TREC will adopt the changes at their November 2020 meeting.

II. Current One to Four Family Residential Contract: (Attachment 1)

A. Paragraphs 1, 2 and 3.

These paragraphs cover the parties' names, the property description, and the consideration for the contract.

- 1) Frequent issues arise when the parties to the contract do not carefully read what is included in the definition of Property. For example, "mirrors" are included in the list of improvements to remain with the Property. However, only "permanently installed and built in" mirrors remain. License holders tend to take for granted that all bathroom mirrors must remain with the property whether permanently installed and built in or not.
- 2) Paragraph 2D is the place where Seller can exclude any items otherwise

covered under improvements and accessories. Note paragraph 2E was **recently added to keep license holders from trying to "retain" the oil, gas, and other minerals for the Seller under Paragraph 2D.**

- 3) To include non-realty items not otherwise covered in Paragraphs 2B and 2C, TREC has approved (but not promulgated) the **Non-Realty Items Addendum. (Attachment 2)**

The distinction between an approved form versus a promulgated form simply means a license holder may use any approved form and is not required to use this one. Promulgated forms are required to be used if they apply. The TREC Non-Realty Items Addendum is not mandatory.

The reason TREC did not promulgate their Addendum was because of the uncertainty as to how lenders handle non-realty items as part of the contract. Some lenders have no problem with non-realty items being listed as part of the contract while others do. Some say it cannot be part of the contract at all. Others say if the Buyer pays separate consideration, non-realty items are permitted to be part of the contract.

The confusion comes in the interpretation of the Fannie Mae guidelines which provide that sales concessions can take the form of non-realty items and the value of sales concessions must be deducted from the sale price when calculating Loan to Value ("LTV") and combined LTV ratios for underwriting and eligibility purposes.

Rather than having to put a value on such sales concessions, lenders may instruct Buyers to remove the items from the contract.

When the lender refuses to allow the non-realty items as part of the contract, the license holder simply makes it a side agreement. And, the lender knows it. This is not a wise practice.

Best practice is to encourage a payment of separate consideration for the items and allow the addendum to remain a part of the contract. Of course, the closing statement then must reflect the payment for the items.

B. Additional provisions of the contract:

- 1) Paragraph 5 covers earnest money. If the Buyer fails to deliver the earnest money within 3 days, Seller may terminate. Question: Arguably Seller terminates due to Buyer's default, but what remedies are available to Seller?
- 2) Paragraph 6 covers title and survey.
 - i. Paragraph 6A (8): If Buyer chooses the endorsement provided herein, the title company will more closely scrutinized the existing survey and may require a new survey. There is increased liability to ensure the accuracy of the survey on an owner's policy as opposed to the loan policy. *See Lawyers Title Insurance v. Doubletree Partners, LP*, No. 12-40692-CV (5th Cir. Jan. 14, 2014), *where the court held that the modification results in the title company insuring the accuracy of the applicable survey.*
 - ii. Paragraph 6C (2): When Buyer is ordering a new survey, the Buyer is deemed to receive it on the earlier of (a) actual receipt or (b) date specified for delivery in the contract. Sometimes lenders suggest Buyer not order the survey until Buyer Approval. If Buyer does not order the survey on time, Buyer may miss his/her right to object to defects shown on the survey.
- 3) Paragraph 7 covers inspections and repairs.
- 4) Paragraph 8 covers disclosure as to separate brokerage agreement.
- 5) Paragraphs 9 and 10 cover closing and possession.
 - i. Lending underwriting may have issues if there is a Seller

Leaseback. The Seller's Temporary Residential Lease provides for payment of all rent due under the lease to be collected at closing.

- ii. Additionally, in the heading of the Seller's Temporary Residential Lease, there is a notice stating that the lease can be for no more than 90 days. However, to qualify for an owner-occupied loan, the Buyer must take possession on or before 60 days from date of closing. If Buyer has already negotiated a 90-day lease with the Seller, this is an issue.
- 6) Paragraph 11 covers special provisions. TREC is adamantly opposed to license holders who insist on writing in special provisions, mostly because it usually constitutes the practice of law and the license holder is not an attorney. The second reason is because special provisions are often written to have the effect of having no consequences, or they are too vague to be interpreted.
 - 7) Paragraph 12 covers loan and closing fees paid by both parties.
 - 8) Paragraph 13 provides for prorations. It is important to note that if prorations are not current or accurate, the parties, under the contract, must re-prorate between each other.
 - 9) Paragraphs 14, 15, 16, and 17 cover casualty loss and repairs, default remedies, dispute resolution through mediation and payment of attorney fees for prevailing party in any dispute.
 - 10) Paragraph 18 covers issues on escrow deposits and releases under the contract. The escrow agent is entitled to recover expenses incurred by the escrow agent for the party receiving any refund or disbursement of the escrow. If the expenses incurred are the not the obligation of the person receiving the earnest money, the expenses cannot be deducted.
 - 11) Paragraph 19 covers survivorship. "All covenants, representations and warranties in this contract survive closing."

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