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ATTORNEYS AT LAW

A Basic Guide For Foreign Purchasers of Massachusetts Residential Property



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I. Introduction

The Greater Boston area has become one of the premier markets for real estate investment by foreign (non-U.S.) investors. In 2014, it ranked second among the top U.S. metropolitan markets (behind only Manhattan) as a destination for foreign investment, with \$4.6 billion of total investment.

This Guide is intended to inform and assist foreign nationals planning on investing in Massachusetts residential real estate. We discuss the nature of the Massachusetts residential real estate markets, identify the various real estate professionals, and describe the process of purchasing real estate, with particular emphasis on condominium units, which are currently the most popular vehicles for foreign residential investment.

II. The Massachusetts Real Estate Market

Each of the 50 states of the United States has laws and regulations governing the ownership of real estate. Cities and towns also play an important role in regulating real estate through zoning and other land use laws, and impose local real estate taxes measured by the value of real estate. The U.S. federal government plays a less important role in real estate regulation, but imposes federal estate and income taxation, which is a major factor in real estate investment. For information on the important tax aspects of investing in Massachusetts residential real estate, see *Tax Guide for Foreign Investors in U.S. Residential Real Estate*.

There are essentially no restrictions on foreign investment in Massachusetts real estate, although “housing cooperatives” may have rules prohibiting foreign ownership and other restrictions that may discourage foreign ownership. Fortunately, there are very few housing cooperatives in Massachusetts (unlike Manhattan); the condominium form of ownership is far more prevalent in Massachusetts. Each type of residential property is discussed in Section IV below.

A foreign national does not need to be a U.S. citizen or a U.S. resident with a “green card” in order to purchase U.S. real estate, although a foreign national may be required to obtain an “individual taxpayer identification number” (“ITIN”) from the U.S. Internal Revenue Service. An ITIN can be obtained by filing an application on IRS Form W-7 with the U.S. Internal Revenue Service.

Owning U.S. real estate does not give foreign owners any rights or privileges regarding legal residence or entry into the U.S. The usual visa requirements will apply.

In many U.S. states, the process of transferring title to real estate is largely conducted by “title companies,” which perform title searches, prepare deeds and other closing documents, and conduct “escrow” closings, often without substantial participation of attorneys. Massachusetts is different. A 2011 decision of the Massachusetts Supreme Judicial Court establishes that although non-attorneys may perform many of the functions necessary to transfer title, a Massachusetts real estate closing requires the “substantive participation of an attorney” to assure that the seller has marketable title and the deed (and mortgage, if any) effect a valid transfer of title. Since the interests of sellers, buyers and lenders are often conflicting, those parties to a Massachusetts real estate transaction are most often represented by their own separate attorneys. When a buyer is not experienced in Massachusetts real estate transactions, the engagement of an experienced attorney is essential.

III. Getting Started

Before starting to search for properties, it is wise to plan ahead as to how you intend to use your new home:

Will it be

- a vacation home?
- a home for your children when they attend college in Massachusetts?
- an investment property?
- a temporary place to live while you are working in or visiting Massachusetts?
- your eventual long-term residence?

IV. Types Of Residential Property

Residential property can take several different forms:

- A single-family home (usually consisting of a parcel of land and a free-standing dwelling suitable for one family).
- A multi-family dwelling (usually consisting of a parcel of land and a building containing several dwelling units).
- A condominium unit (consisting of one of several separately owned dwelling units owned by the buyer within one or more buildings). The buildings and related common areas are owned by a condominium association in which each unit owner owns a percentage interest. Condominium units can resemble apartments in a single high-rise or low-rise building, or can be units in detached or semi-detached buildings in a campus-like setting. Condominium units often include amenities for unit owners, such as swimming pools or recreational areas.
- A cooperative housing unit (consisting of a single building in which multiple owners own “shares” entitling them to perpetual “leases” of dwelling units). As mentioned above, cooperatives are rather rare in Massachusetts.

V. Real Estate Agents

In Massachusetts, as well as other states, real estate is sold principally through real estate agents (also referred to as realtors or brokers). Real estate agents are licensed by the state and are subject to strict ethical standards. Some real estate developers may use employees as their selling agents, but a “multiple listing service” (“MLS”) is more often used. Under an MLS system, any licensed real estate agent introducing a buyer to a seller can earn a commission on the sale. Such agents are independent business persons, but are nevertheless working for the seller.

A. SELLER’S AGENTS

It is worth keeping in mind that real estate agents are usually agents for the seller, not the buyer, and have a legal duty to look out for the seller’s interests. This means, of course, that they are interested in selling the property at the highest price and the best terms for the seller. The seller’s agent is paid a commission by the seller. There is nothing wrong or disreputable about this practice, but it is wise to keep in mind the role that the agent is performing.

B. BUYER’S AGENTS

It is possible for you to hire a “buyer’s broker” who will work for you, as the buyer, and have a legal duty to look out for your interests rather than the seller’s. Fortunately, the MLS system often provides for the splitting of the sales commission between the seller’s agent and the buyer’s agent. This means that you, as the buyer, do not have to pay the buyer’s broker. In order to engage a buyer’s broker, you will have to sign an agreement to that effect. Without such an agreement, your broker will be a seller’s agent.

C. DUAL AGENCY

In many cases, the agent will request your consent to serve as both the seller’s and the buyer’s agent. There is usually no good reason to refuse this request, so long as you understand his or her potential conflict of interest.

You should discuss your preferences for the type and location of property, as well as your budget, with your real estate agent, who will be an invaluable resource in locating a property that suits your needs, and in guiding you through the often-confusing process of buying a home. Many agents will assist you in selecting real estate attorneys and other professionals who can give you legal, tax and financial advice.

VI. The Legal Process

A. OFFER TO PURCHASE

Once you have selected a property, you will be asked to make an “Offer to Purchase.” This is a relatively short document that identifies the property, the purchase price, and the other terms of purchase, including a time period within which the parties must sign a formal Purchase and Sale Agreement (“P&S Agreement”). You will typically sign the offer and submit it to the seller, who may either accept it or reject it; if the offer is rejected, the seller usually responds with a counteroffer at a higher price or with more seller-favorable terms, or both.

*It is important to know that an Offer to Purchase can be, and in many cases, will be, a binding legal contractual obligation enforceable by court proceedings, even if it provides for the later signing of a P&S Agreement. In most cases, it is highly unwise to sign an Offer to Purchase unless it explicitly states that it is **not** a binding contract and the parties will be legally bound **only** by the Purchase and Sale Agreement. Failure to do so can lead to expensive and time-consuming legal proceedings. You should consult with an attorney before signing any Offer to Purchase.*

B. THE P&S AGREEMENT

Once the Offer to Purchase is signed, the buyer and seller, through their attorneys, will negotiate a longer P&S Agreement detailing the legal terms of the transaction, and setting a time schedule for performance, usually requiring a “closing” within 60 to 90 days after the signing of the P&S

Agreement, at which the deed to the property is to be delivered and the purchase price paid.

The P&S Agreement will provide for certain contingencies, such as the seller’s providing good legal title to the property, title insurance, the condition of the property, payment of any seller’s mortgage at closing, and often a “financing contingency” which allows the buyer to terminate the agreement if he or she cannot obtain mortgage financing to provide funds to purchase the property. Many P&S Agreements for commercial properties nowadays provide for a “due diligence” period of 30 days or more during which the buyer can research the condition of the property and terminate the P&S Agreement if its condition is not to the buyer’s liking. For residential properties, a briefer period of 10 days or so is usually given to perform the property inspection. See Section VII(D) below.

There are a number of different forms of P&S Agreements in use in Massachusetts. The most common one is probably the Greater Boston Real Estate Board form. The seller traditionally provides the first draft of the P&S Agreement, which is always overly favorable to the seller. The buyer’s attorney negotiates with the seller’s attorney and usually reaches a compromise.

Often the seller’s willingness to compromise in the Offer to Purchase or P&S Agreement stage depends on market conditions. If there are many prospective buyers, the seller will try to drive a “hard bargain;” if not, he or she will be more cooperative.

VII. Due Diligence

During the period between the signing of the Offer to Purchase and the P&S Agreement, the buyer and his attorney will engage in the process of inspecting the property (usually with the assistance of a home inspector), checking the status of the legal title to the property at the Registry of Deeds, and verifying the property's environmental and zoning status, etc.

Most condominium developers are well aware of this process, and are prepared to assist the buyer and his or her attorney in this process. In particular, a condominium developer will often be prepared to provide the buyer's attorney with a commitment for title insurance, which avoids a sometimes lengthy "title search" at the registry.

A. TITLE SEARCHES

The most important factor in any real estate purchase is establishing that the seller is the true owner of (i.e., has "marketable title" to) the property. The usual process of establishing title to real property in Massachusetts (and most other states), involves a search of the land records in the local registry of deeds; in Massachusetts, registries of deeds are located in each of the several counties of the state. All deeds, mortgages and other documents affecting the title to real property are required to be recorded and indexed in the registry of deeds. A title search requires the examination of these records for at least 50 years.

An alternative form of establishing title to real estate in Massachusetts (and in about eight other states) is through a legal process called "land registration," under which the Massachusetts Land Court makes a legal ruling as to the present ownership of the land. Once the court makes its ruling, the property becomes "registered land," and each successive new

owner gets a "certificate of title" certifying his ownership rights and listing all of the encumbrances and restrictions on the property. The process of searching title of registered land is thus much simpler than the title search required for unregistered land. Separate land registration offices are located in each registry of deeds.

The purpose of a title examination is to determine whether the seller is the true legal owner of the property, and whether the property is subject to any undischarged "encumbrances" or restrictions.

B. TITLE INSURANCE

During the last 30 years, title insurance has become the standard form of protection for buyers of real estate in Massachusetts. A title insurance company will issue a standard ALTA title insurance policy to a buyer insuring that he or she owns the property free of competing claims, such as mortgages, leases, easements and liens. A similar policy is issued to the

mortgage lender, if any. If a title defect (such as an old undischarged mortgage) should arise in the future, the title company will pay to clear the title.

Title insurance requires the payment of a single one-time premium, and the owner's policy is in effect for so long as the buyer owns the property. The amount of the premium depends on the value of the property; for example, the premium for a \$3 million owner's policy and loan policy will cost about \$7,500. If a title search is required, the buyer's attorney will usually arrange for a title policy. As mentioned above, many developers provide title commitments for condominium units, which greatly expedites the process.

C. LIENS, ENCUMBRANCES AND RESTRICTIONS

Most P&S Agreements require that the seller provide the buyer with "good clear record and marketable" title, free and clear of encumbrances and restrictions. A title search will reveal what kinds of encumbrances and restrictions exist. For example, a seller's property is often subject to a mortgage for a loan; the seller will customarily pay off and "discharge" the mortgage using the sale proceeds at the closing.

Most real property is subject to local city or town real estate taxes; the city or town has a "lien" or claim against the real estate for unpaid taxes. The city or town will issue a "municipal lien certificate" certifying the amount of any taxes due. The seller will ordinarily pay any currently due taxes and allocate any taxes not yet due between the buyer and the seller at the closing.

Other encumbrances, such as leases to third parties, mortgages securing seller's obligations, and liens and attachments by creditors of the seller, will usually be discharged at the closing in order to deliver good and marketable title. Some encumbrances are considered immaterial or beneficial to the property, such as easements providing utility services to the property and certain restrictions, and are not discharged.

Condominium units will always be subject to complex and lengthy legal documents, including a master deed and condominium association documents, which regulate the use of the condominium units and common areas. These documents are usually non-negotiable and should be carefully reviewed to make sure that they do not impose unacceptable restrictions on the buyer. Common issues of concern include parking and storage rights, restrictions on the keeping of pets and the leasing of units, and approval of past or future alterations to the unit.

D. PROPERTY INSPECTION

The P&S Agreement for the purchase of a single-family or multi-family property should contain a provision for a physical inspection of the property by a licensed home inspector. A home inspection will provide the buyer with a detailed report on the property's heating, cooling, plumbing, and electrical systems, its structural components, foundation, roof, masonry, and external and internal components, including any defects needing correction or repair. There are many reputable home inspectors in the Greater Boston area; your real estate agent should be able to recommend one or more.

E. ZONING REVIEW

Every Massachusetts city and town regulates the use and dimensions of real property within the municipality. A violation of the local zoning code can result in the loss of use of the property or the making of expensive building modifications. Properties used for residential purposes for many years rarely present zoning problems, but it is well worth the effort to check the local zoning code. Properties recently constructed or improved may require more detailed investigation to make sure that there are no zoning violations. Your attorney should be able to coordinate this task. Title insurance is also available to cover losses from zoning violations, as an endorsement to the title policy.

F. SURVEY

Purchasers of single-family and multi-family residences that are located on a lot of land may be concerned whether the buildings on the land encroach upon abutting property, or vice versa, or violate dimensional zoning requirements. This is rarely the case with condominium units.

A mortgage inspection plan showing the property and any encroachments or violations of zoning setback requirements can be obtained from a number of land survey firms for a reasonable fee. This is usually satisfactory evidence for the lender or title insurance company.

G. ENVIRONMENTAL ISSUES

Massachusetts has a number of laws protecting the environment which can affect residential property. Depending on the circumstances, the following issues may be important:

- Radon testing
- Lead paint testing
- Inspection of underground fuel storage tanks (“USTs”)
- Inspection of septic systems (where the property is not served by a municipal sewer system) (“Title 5”)
- Hazardous waste and pollution inspection
- Urea formaldehyde foam insulation inspection (“UFFI”)
- Pest inspection (including termites)
- Potable (drinkable) water testing
- Smoke detectors
- Asbestos inspection

Some of these issues may be dealt with by the home inspection. Purchases of unimproved land may involve other issues.

H. INSURANCE

Buyers should arrange for property insurance (against damage or destruction of the property by fire or other casualty) and liability insurance (against legal liability to third parties for injuries or property damage occurring on the property). Lenders will insist on insurance coverage naming them as mortgage holders. Most insurance brokers will provide a “binder” evidencing insurance coverage at the closing. Condominium unit insurance is discussed in Section IX below.

VIII. The Closing

At the closing, the various parties to the real estate transaction assemble and sign a great number of documents. Your attorney will prepare you for this event.

Most importantly, at the closing, the seller will deliver the deed to the property, the buyer will make payment for the property, and the buyer's lender, if any, will be given a note and a mortgage as security for its loan. The buyer, in most cases, will be required to provide "good funds" to pay for the purchase (ordinarily a bank or certified check or wire transfer of funds).

In addition, the parties will allocate the purchase price among the participants according to a "settlement statement," often using a standard government form called a "HUD-1." The matters dealt with by the settlement statement will include, in most cases:

- Allocation of real estate taxes between buyer and seller (see Section VII(C) above)
- The deposit (which is credited to the buyer)
- Payoff of seller's mortgage (seller's obligation)
- Payment of transfer taxes (seller's responsibility)
- Payment of real estate agents' fees (seller's responsibility)
- Payment of recording fees (usually split between buyer and seller)
- Payment of condominium fees and assessments (seller's responsibility in a condominium sale)
- Adjustments for public utility charges
- Title insurance premiums (usually the buyer's responsibility)
- Lender's fees and expenses (buyer's responsibility)
- Tax escrow deposit, if required by lender (buyer's responsibility)
- Land bank taxes (Martha's Vineyard and Nantucket)

- Attorneys' fees and charges
- Other fees and expenses

Some of the principal documents which may be delivered at the closing are listed below:

- Quitclaim deed to the property
- Settlement statement
- Promissory note to lender (if applicable)
- Mortgage to lender (if applicable)
- Truth-in-lending disclosure (if applicable)
- Rescission statement (if applicable)
- Title insurance affidavits
- Title insurance policies
- Insurance certificate (buyer and condo association, if applicable)
- Municipal lien certificate (local taxes)
- "Section 6(d)" certificate (re: payment of condo fees), if applicable
- Lead paint notice
- UFFI certificate
- Smoke and carbon monoxide detector certificate
- Foreign status certificate (certifying that the seller is not a foreign person)
- A tax lien waiver (if the seller is a corporation selling all or substantially all of its assets)
- Flood zone certificates
- Flood insurance (if applicable)
- Title 5 septic certificate (if applicable)
- Well water tests (if applicable)
- Certificate of compliance with homeowner association rules (if applicable)
- Certificates of legal existence and authority for parties that are entities

IX. Post-Closing Responsibilities

As the owner of a single-family dwelling, you will have the usual risks and responsibilities of home ownership, such as maintenance and repair, utility charges, home insurance, real estate taxes, personal property taxes, and motor vehicle excise taxes. As the owner of a multi-family dwelling, you will have the additional responsibility of finding tenants, collecting rents and repairing common areas.

These responsibilities are somewhat different for a condominium unit owner. Maintenance and repair costs and insurance for the common areas are paid by the condominium association and passed on to the unit owners through periodic condominium fees assessed by the association. Maintenance and repair within the unit are the responsibility of the unit owner. Unpaid condominium fees constitute liens against the applicable condominium unit

and can be enforced in court. Real estate taxes are assessed on the unit owners; no taxes are assessed on the association. Fire and casualty insurance for the buildings, structures and the common areas is also provided by the association and passed on through the condominium fees. However, a unit owner is responsible for obtaining “contents” coverage for personal property (such as furniture, clothing, artworks, and jewelry) kept within the unit.

X. Confidentiality

Many individual foreign national investors are concerned about publicity relating to their identities. In most cases, the identity of an investor can be kept confidential by using a separate entity. Complete anonymity, however, is not possible, since an investor's identity will be revealed to the IRS in tax returns. The IRS, however, has a rule of strict confidentiality, except of course in court proceedings to enforce the collection of taxes.

The U.S. Commerce Department in 2014 reinstated reporting requirements for foreign investors in U.S. businesses (including real estate investors). These rules require filing a report (or a request for exemption) on Form BE-13 reporting a purchase of real estate by foreign nationals. Purchases of real estate exclusively for personal use and not for profit-making purposes do not require a filing in most cases. The Commerce Department program is used to collect aggregate data on

foreign investment in the U.S. and information is to be kept strictly confidential by law.

The identity of an individual foreign investor owning real estate directly will be a public record in the registry of deeds, municipal tax records and other public records. Individuals investing through corporations, trusts and LLCs can, by careful planning, avoid public disclosure.

About Davis Malm

Founded in 1979, Davis, Malm & D'Agostine, P.C. is a premier mid-sized, full-service firm in Boston, Massachusetts. The firm provides sophisticated, cost-effective legal representation to local, national, and international public and private businesses, institutions, and individuals in a wide spectrum of industries. The firm's attorneys practice at the top level of the profession and consistently deliver successful results to clients through direct partner involvement, responsive client service, and practical and creative problem-solving.

The firm's interdisciplinary team of real estate, tax, and trusts and estates attorneys possess years of experience and in-depth knowledge on issues facing foreign investors. We take the time to understand each client's unique needs and objectives. Our team of attorneys works closely to provide coordinated and comprehensive advice and tax-efficient designs to meet each client's goals.

If you would like to discuss any of the topics in this guide, please contact either of its primary authors:



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Front Cover: Frederic Remington, *The Moose Country* (detail), courtesy Frederic Remington Art Museum, Ogdensburg, New York.

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