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Are We In Or Out Of Contract?

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April 5, 2013

Our current market (low inventory, multiple offers, etc.) has caused an increase in specific performance actions by buyers and deposit disputes prompted by a seller's cancellation of a contract for alleged non-performance by the buyer. These disputes cause clients to ask whether they are in or out of contract. The answer is never a simple one: among other factors, it turns on contract formation, performance, cancellation, and the legal concept of equity. This article identifies some of these issues/questions that a lawyer examines in order to determine if the parties are in or out of contract.

Contract Formation. The starting point is whether the contract and all addenda, requests for repairs, etc., have been signed by all parties. Also, has the acceptance been timely, and has there been delivery of that acceptance in the manner specified in the contract? If there has been an attempt to revoke, was that revocation communicated orally or in writing? What is the timing of any revocation in relationship to delivery of acceptance. Are there any emails or other documents confirming the timing of these acts?

Has the contract been signed by one party on behalf of another? Does that party have the authority to do so? What is the source of that authority, and has it been confirmed? These questions will arise if a power of attorney authorizes the sale of a property or if all trustees of a trust have signed a contract and it needs to be determined whether these entities actually authorized to do so. If a corporation or other entity is involved, is a corporate resolution necessary, has one been issued, and, if so, does it provide the individual signing the contract with the authority to do so? The same analysis may apply to partnerships or LLCs.

Determining whether all parties have initialed the liquidated damages clause or the arbitration clause is

always part of a lawyer's review of contract documents. When these clauses have not been initialed, what does the preprinted language of the contract require? If a counteroffer is involved, typically the preprinted language eliminates those clauses from the contract if they are not signed by all parties.

All of the foregoing issues can be affected by the conduct and statements of the parties. If these issues are overlooked and the parties continue to act as though there is a contract, that may provide a basis for overcoming a technical deficiency in contract formation. If there has been a material and detrimental change in a party's position in reliance upon their being a contract, that may give rise to an estoppel. Waiver and/or ratification of the contract, which occurs when a party knowingly proceeds as though there is a contract in place, may prevent that party from arguing that there is no contract for one of the foregoing reasons.

Unfortunately, there are no fixed time frames in which these rules suddenly apply. Each case has its own unique facts and circumstances, and in each case the equities must be taken into account as well.

The concept of equity focuses on the fairness of a situation and is determined by a judge or an arbitrator, who has broad latitude in determining what is equitable or fair in a transaction. Typically, this involves an assessment of a party's motivations, whether its conduct and statements are consistent with those motivations, and whether those motivations are reasonable under the circumstances. Ultimately, a judge or an arbitrator has to decide whether the equities outweigh any technical deficiency in contract formation. Any analysis of this kind is going to be based upon not only the contract documents but also any other communications, both oral and written. How a party presents itself, including tone, demeanor, and ability to recall or recollect, will also have an impact on this assessment.

Many other issues may affect contract formation, including the clarity and certainty of the contract terms, whether there are any conditions precedent or subsequent to contract formation, whether mutual agreement on all material terms exists, and whether any party has not acted in good faith.

Contract Performance. What a buyer and seller are contractually required to do, when they are required to do it, and whether their performance matches the contractual terms are some of the issues a lawyer will evaluate in this area. For example, has the buyer's deposit been made in a timely manner and with good funds that have cleared a bank? Does any pre-qualification or pre-approval letter meet the preprinted terms of the contract, and has it been provided in a timely manner? Has there been timely proof of funds, and are there any hidden terms or conditions related to the liquidation of those funds? Is there an appraisal contingency and, if so, is that contingency based upon the lender's appraisal or an independent appraisal? Have the parties discussed or agreed what will happen in the event the property does not appraise? Is that agreement part of the contract? Has the seller provided all documents required by the contract? Are those documents completed fully? If not, what are the ramifications?

Where contingencies are in play, have they been removed in a timely manner? Is that removal subject to any requests for repairs or other acts on the part of the seller? What is the impact of any qualified or conditional contingency removal? If there is an extension of a contingency time frame, has it been

confirmed in writing, signed by all parties, and delivered before any cancellation?

As with contract formation, the answers to these questions are often affected by the statements and conduct of the parties and real estate licensees, as well as any time delays. The concepts of waiver, estoppel, ratification, and equity discussed above will impact any assessment of contract performance as well.

Whether a party has the right to continue to perform will be affected by what the contract requires for it to be cancelled. The timing and adequacy of any notice to perform needs to be evaluated, as does the impact of any deficiency in such a notice. Notices to perform are required for contingency removal and other contractual obligations.

With respect to the close of escrow, what does the preprinted language of the contract require? Does it require a demand to close escrow? If there is no contractual obligation, is there a legal obligation to tender performance? A tender requires an offer to perform. For a buyer, it typically involves depositing all necessary funds, signing escrow instructions, and otherwise indicating in writing that the buyer is ready, willing, and able to perform. There may be instances in which a tender is not necessary, such as where a seller has repudiated the contract or where performance by a buyer would be futile. For the seller, where there is no contractual obligation to demand a close of escrow, tender of performance typically requires signing the grant deed and escrow instructions and otherwise indicating that the seller is ready, willing, and able to close escrow.

An analysis of these issues will be affected by oral and written statements of the parties and the real estate licensees, as well as by the equities. For example, if a cancellation agreement has been signed by a party and if the reason for the cancellation given in that agreement could have a significant impact on the outcome, emails indicating the motivations of the party cancelling or attempting to explain the party's conduct or performance (or lack thereof) will certainly have an impact on this analysis.

In conclusion, determining whether a buyer and seller are in or out of contract is complicated. It involves analyzing not only the terms and conditions of the contract but also of the parties' performance, statements, and conduct. It also involves assessing the equities. The next time this question presents itself, remember to consider the issues and queries raised in this article before offering an answer.

Laurie and I had two very challenging real estate rights issues that we were advised were going to be difficult to prevail on. The RHRC team engaged with us and helped us understand our rights and prevailing position. RHRC were thoughtful advocates for us from the beginning to conclusion of our cases. We feel fortunate to know we will always be able to call on the firm in the future and that they are our legal counsel.

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The California law firm of Rossi, Hamerslough, Reischl & Chuck provides legal representation to real estate and business clients throughout Silicon Valley and the San Francisco Bay Area including San Francisco, San Jose, Palo Alto, Los Altos, Los Gatos, Menlo Park, Gilroy, Hollister, Santa Cruz, Santa Clara, Aptos, Monterey, Carmel, Salinas, Morgan Hill, Saratoga, San Francisco County, Santa Clara County, Santa Cruz County, San Benito County, Alameda County, San Mateo County, Monterey County, and Contra Costa County.