

EARNEST MONEY DEPOSITS AND FAILED TRANSACTIONS

Almost every day, the Michigan Realtor[®] Hotline receives at least one call from a Realtor[®] who is holding an earnest money deposit (or “EMD”) on a failed transaction. This article contains a number of rules that hopefully should help guide Realtors[®] who find themselves in this situation.

Consider the following hypothetical:

A purchase agreement has a financing contingency. The home does not appraise anywhere close to the agreed-upon purchase price, so the buyer’s loan application is denied. Buyer terminates the purchase agreement. Seller is so angry about the low appraisal, he refuses to sign the broker’s standard release form authorizing the release of the EMD to the buyer.

What do the Realtors[®] involved in this transaction need to know?

1. A Realtor[®]’s “standard” release form typically provides that the buyer and seller release each other and the real estate brokers involved from any liability relating to the transaction. While it is a good business practice to obtain such a release, a Realtor[®] cannot condition the release of an EMD on the signing of such a release.
2. A Realtor[®] can condition the release of the EMD on the signing of a release form that is nothing more than an agreement as to which party is to receive the EMD. However, the law does not require such written authorization. The law says only that a broker cannot release an EMD “for which the buyer and seller have made claim.” In other words, if both the seller and the buyer claim to be entitled to the EMD, then the Realtor[®] must hold the EMD.

3. The rule that the Realtor[®] must hold the EMD if there is a dispute over who is entitled to the EMD applies even if one of the parties is clearly wrong.
4. The rule that the Realtor[®] must hold the funds if there is a dispute refers to a dispute over the EMD. It is not necessary that buyer and seller have resolved all of their differences. Assume that a seller announces that he is breaking the sale contract, will not sell his home, and immediately authorizes the release of the EMD to the buyer. In that situation, the EMD may be released to the buyer even if the buyer intends to sue the seller for breach of contract (provided the release is not conditioned on the buyer waiving all claims against the seller). For purposes of the Occupational Code and Rules, the question is only whether the parties disagree over who is entitled to the EMD.
5. Once there is a dispute, the Realtor[®] does need a written agreement in order to release the EMD. The Realtor[®] does not need (and cannot require) a full release of all claims, but simply a written agreement over the disbursement of the EMD.
6. The fact that the buyers and sellers do not agree on the release of the EMD does not prevent the sellers from relisting their house. If there is no disagreement over the fact that the purchase agreement has been terminated, then the sellers can and should relist their house. (If on the other hand, the buyers indicate that they intend to try and enforce the purchase contract, then the sellers should talk to a lawyer before obligating themselves under a second sales agreement.)
7. There is a process – called an “interpleader” action – whereby a broker can turn over the EMD to a court and have the court decide whether the buyer or seller is entitled to it. However, the process requires the broker to file a lawsuit and, therefore, the broker will need to hire an attorney to interplead an EMD. Michigan Realtor[®]'s online law library has an “Interpleader Packet” designed to assist broker’s counsel in doing so.
8. If the EMD is less than \$5,500, the sellers or buyers may ask the small claims court to issue an order directing the release of the EMD or awarding them the EMD.
9. EMDs that are “dormant” (*i.e.*, unclaimed for a period of 3 years) must be turned over to the State. The filing deadline is July 1 of each year

and Realtors[®] can face interest and significant penalties if they fail to do so. An article discussing the escheats process in detail is available online in the Michigan Realtor[®]'s law library.

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