Michigan Realtors®
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# OVERVIEW OF SELECTED BASIC CONTRACT PRINCIPLES

## I. INTRODUCTION

Now, more than ever, REALTORS® must have a solid understanding of basic contract principles in order to assist their clients and customers in the world of short sales and REO properties. While the means and methods by which REALTORS® carry out their business are changing on what seems to be a daily basis, the legal foundation for buying and selling real estate and contract real estate law remains carved in granite.

## II. DISCUSSION

The negotiation and formation of purchase agreements is often the source of conflict and misunderstanding. This article is intended to provide REALTORS® with a general overview of select contract issues relating to the negotiation and formation of purchase agreements. Knowledgeable REALTORS® can anticipate, address, and resolve potential problems with greater ease. This article should be read in conjunction with the article entitled, "Inspection Contingency Clauses and Contract Law."

### A. Contract Formation

A contract for the sale of land must be specific. Michigan law generally requires that the contract clearly identify the property, parties, price and terms of payment. The purpose of this requirement is to ensure that the contract clearly establishes the obligations of the parties. The written contract alone should be sufficient to determine the parties' intent. In addition to Michigan law generally, the rules promulgated under the Occupational Code require REALTORS® to make certain that all terms and conditions of the real estate transaction are

included in the offer to purchase. While standard form purchase agreements typically include the basic elements, deal-specific terms such as the personal property to be included in the sale or special contingency clauses need to be carefully drafted.

Once a purchase agreement becomes binding, it can be difficult to negotiate changes. Both parties are bound by the agreement, and neither is legally required to make concessions or modifications. Therefore, it is essential that REALTORS® determine their client's needs before an offer is presented or accepted. Taking the time to anticipate problems will significantly reduce the likelihood of costly litigation later.

### 1. Signatures

To be valid, a purchase agreement must be signed by all the parties. Generally, the signatures do not need to be witnessed or notarized. If multiple parties are purchasing property together, each buyer's signature is required. Where property is being sold by a married man, his wife's signature is required even if the property is held in his name alone, due to the wife's dower rights in the property.

A party cannot orally authorize someone else to sign a real estate contract on that person's behalf. Oral permission, even to a spouse, is insufficient. REALTORS® are sometimes asked to sign a purchase agreement on behalf of a client. REALTORS® who sign a purchase agreement on behalf of a client run the risk of the client later claiming that a particular provision – or the contract as a whole – is unacceptable to that client. Since most clients are accessible via fax, overnight delivery or electronic mail, this is rarely necessary and should be discouraged. A party's faxed signature or e-signature should be sufficient, particularly if the contract includes a

clause permitting these types of signatures. If a REALTOR® feels it is necessary to sign a purchase agreement as an agent for a client, the REALTOR® must first obtain a power of attorney specifically authorizing that signature. The REALTOR® should also sign the purchase agreement so as to demonstrate the capacity in which they sign, *e.g.*, "REALTOR® Jones acting as attorney-in-fact for Seller Smith."

If REALTORS® wish to deliver offers, counteroffers, acceptances and other contract documents as attachments to electronic mail or by similar means, it is necessary under federal and state law that the seller and buyer agree in writing to that means of delivery. It is also necessary to demonstrate that the seller and buyer have provided email addresses by which they can receive email. These written terms can be included in the purchase agreement. Further, the purchase agreement can be executed through electronic signatures.

As an aside, we would recommend against drafting a clause that provides for facsimile or electronic signatures "with originals to follow." This language could create an ambiguity as to when the contract becomes binding – whether upon the transmission of the facsimile or electronic signature or upon the delivery of the original. Language such as the following is preferable:

> Any written notice or communication in connection with this transaction may be given to a party or party's agent by sending or transmitting it to any email address or fax number provided by the parties. Any such written notice or communication shall be deemed delivered at the time it is sent or transmitted.

## 2. Presentation of Offers

Licensing rules require REALTORS® to promptly present an offer to a seller. In the case of multiple offers, REALTORS® must present all offers, but, contrary to popular belief, the law does

not require REALTORS® to present multiple offers in the order in which they are received. Nor is a seller required to reject one offer before considering another offer. A listing agent has a fiduciary duty to advise his client about all offers prior to having that client make a decision on any offer. The seller can then accept the most desirable offer and reject – or simply ignore – the other offers.

The Occupational Code provides that once an offer has been accepted, a REALTOR® is under no obligation to present additional offers received after the purchase agreement has been fully executed, unless required by the listing agreement. This provision of the Occupational Code may not protect a REALTOR® from a claim that he breached his fiduciary duty by failing to present such an offer. Accordingly, REALTORS® who do not want to present additional offers after a purchase agreement is signed should expressly so state in their listing contracts.

Example 1

REALTOR® receives an offer from Buyer A. REALTOR® is anticipating an offer from Buyer B later that day. REALTOR® waits until both offers are received and presents them to Seller the next morning. Buyer A is angry that his offer was held until another offer was received.

*REALTOR® is required to present offers within a reasonable amount of time. Holding an offer a few hours in anticipation of another offer is not prohibited by the rules, and may be in the Seller's best interest.*

Example 2

REALTOR® receives offer A, followed by offers B and C. REALTOR® determines that offer A isn't as good as offers B and C. REALTOR® presents offer B first, followed by offer C. Seller decides to accept offer C, so REALTOR® does not present offer A.

*REALTOR® has violated the rule requiring the presentation of all offers received before a binding purchase agreement is signed. Moreover, REALTOR® has breached his fiduciary duties owed to the Seller by failing to disclose the existence of offer A.*

Example 3

REALTOR® presents offers A and B to Seller. Seller accepts offer B. The next day, REALTOR® receives offer C.

*In order to protect himself, a REALTOR® should present offer C to the seller unless there is a provision in the listing agreement that indicates that subsequent offers will not be presented after the purchase agreement is signed. Seller, however, is bound by the acceptance of offer B, assuming the acceptance of offer B has been delivered.*

Sellers faced with multiple offers are often tempted to counter more than one of the offers. Obviously, a seller with two (or more) outstanding counteroffers runs the risk that both will be accepted and he will be contractually obligated to sell the property to two different buyers. A seller should never have two outstanding counteroffers at the same time – at least without some carefully drafted language which protects the seller from having more than one accepted counteroffer.

Any REALTOR® that has been involved in the short sale process understands that not only is the seller's acceptance of an offer required, but also the approval of the seller's lender to the terms of the proposed sale. Typically, a seller who accepts an offer on a short sale does so contingent upon approval by the seller's lender and upon the seller's approval of the lender's terms for the short sale. We have received many calls over the MAR Legal Hotline which demonstrates some confusion among REALTORS® as to the "rules" which apply to submission of

offers in short sales to lenders. Unlike offers submitted to listing REALTORS®, there is no provision in the Occupational Code or in NAR Code of Ethics that requires that the accepted offer be submitted to the seller's lender within any specific period of time. Obviously, in discharging their fiduciary duties to their seller, listing REALTORS® should submit an accepted offer to the seller's lender within a reasonable period of time.

In some instances, listing REALTORS® have sellers who accept more than one offer in a short sale. The sellers are relying on their lender to approve only one of the accepted offers. There is no rule requiring a listing REALTOR® to submit more than one accepted offer to the seller's lender. In submitting accepted offers to a seller's lender, a listing REALTOR® must be guided by their instructions from the seller and the REALTOR®'s own experience in dealing with a specific lender. As a practical matter, some lenders are simply incapable of processing more than one accepted offer, and submission of multiple accepted offers will simply freeze the process. There are, however, other lenders who can deal readily with multiple accepted offers on a short sale. Again, REALTORS® will need to rely upon their seller's instructions and their own experience.

### 3. Rejection/Acceptance/Counteroffer

An offer typically remains open until one of the following occurs:

1) the offer automatically expires at a specific date and time set forth in the offer;

2) the offer is revoked;

3) the offer is rejected or countered; or

4) the offer is accepted.

If none of these events occur, courts have generally held that the offer expires after a "reasonable" time.

Frequently, offers contain express expiration dates. Such a clause usually provides that if the offer is not accepted by a specific date and time, it becomes null and void, and cannot thereafter be accepted. Occasionally, a party will want to revoke an offer prior to the stated expiration date. The Michigan Supreme Court has held that in the absence of a payment or other consideration, an offer can be revoked prior to its stated expiration date. *Hollingshead v Morris*, 172 Mich 126 (1912).

If an offer has been presented to the seller, but the buyer changes her mind, the offer can be revoked before it is accepted by the seller. A revocation does not need to be in writing, and can be conveyed to either the seller or the seller's agent (this could be either the listing agent or a sub-agent, if there is one). Once an offer is revoked, it cannot be accepted by the seller.

A counteroffer is deemed a rejection of the offer and itself becomes an offer. Sellers cannot simultaneously "accept" and modify an offer. Accepting an offer with any material change creates a counteroffer and is not binding unless accepted by the other party. Almost any modification, no matter how small, constitutes a material change.

Likewise, once an offer is rejected, it cannot be accepted. If a counteroffer is rejected, the seller cannot later change his mind and accept the original offer.

Example 1

Buyer presents an offer to Seller for $100,000. Seller accepts, but adds a provision requiring proof of financing approval within 30 days.

*Seller has rejected Buyer's offer and presented a counteroffer with a new condition. There will not be a binding purchase agreement unless and until Buyer accepts the counteroffer.*

Example 2

Buyer presents an offer to Seller for $100,000. Seller presents a counteroffer for $105,000. Buyer rejects the counteroffer. Seller signs and delivers the original $100,000 offer. Buyer refuses to accept the executed purchase agreement.

*The purchase agreement is not binding because the Seller's counteroffer constituted a rejection of the Buyer's original offer. Seller's attempt to accept the Buyer's original offer would operate as a new offer to the Buyer.*

An offer is not accepted until it is signed and the fact that the offer has been signed is communicated to the offeror. Typically, unless the contract expressly provides otherwise, this communication must be in the form of delivery of the signed acceptance. Delivery can be to the offeror or his agent. Orally communicating the fact that the offer has been signed is not sufficient to bind a party to the purchase agreement, unless the contract expressly so provides. An offer may be rejected through electronic delivery, as discussed above, if the parties have previously agreed in writing to this form of delivery.

As stated above, delivery can be made to either the party or their agent. Years ago, when nearly all REALTORS® involved in residential transactions represented the seller, the rules governing delivery were simple – delivery to the listing or selling REALTOR® constituted delivery to the seller. Now that selling brokers are often acting as buyers' agents, this general rule no

longer applies. It is now necessary to assess who a REALTOR® represents to determine at what point the parties have a binding purchase agreement. Delivery to a buyer is effective when received by a REALTOR® acting as the buyer's agent. Similarly, delivery to the seller is effective when presented to a REALTOR® acting as the seller's agent, whether as a listing agent or a sub-agent.

### Example 1

Buyer makes an offer through REALTOR® Smith, who is acting as a buyer's agent. REALTOR® Smith delivers the offer to the listing agent who presents it to Seller. Seller accepts the offer and delivers it to the listing agent. The listing agent delivers the signed purchase agreement to REALTOR® Smith.

*The parties have a valid, enforceable contract for the sale of the property. Buyer could not then revoke or withdraw her offer, and Seller could not then revoke or withdraw his acceptance.*

### Example 2

Buyer makes an offer through REALTOR® Smith, who is acting as a buyer's agent. REALTOR® Smith delivers the offer to the listing agent who presents it to Seller. Seller accepts the offer and delivers it to the listing agent. The listing agent calls REALTOR® Smith and states that the offer has been accepted. Before the listing agent can deliver the signed purchase agreement to REALTOR® Smith, Seller calls the listing agent and informs the agent that Seller wishes to revoke his acceptance.

*The listing agent should not deliver the document to REALTOR® Smith. The contract is not enforceable because it was not delivered to the buyer or the buyer's agent. Generally, unless the contract provides otherwise, oral notification of acceptance is not sufficient to bind a party to a purchase agreement.*

### Example 3

Buyer makes an offer through REALTOR® Smith, who is acting as a buyer's agent. Seller accepts the offer and delivers it to the listing agent. The listing agent delivers the signed purchase agreement to REALTOR® Smith. The listing agent returns to the office and gets a call from Seller saying Seller wants to revoke the acceptance. Before REALTOR® Smith has a chance to deliver the purchase agreement to Buyer, the listing agent calls and informs REALTOR® Smith that Seller wants to revoke the acceptance.

*The contract is enforceable and cannot be revoked by Seller or the listing agent. Even though Buyer does not yet know the offer has been accepted, it was signed by Seller and delivered to the Buyer's agent. If Seller refused to proceed with the sale, Seller would be in breach of contract. The Buyer could sue for specific performance of the contract.*

## Example 4

Buyer makes an offer through a REALTOR® Jones who is acting as a sub-agent for Seller. Seller accepts the offer and delivers it to the listing agent. The listing agent delivers the signed purchase agreement back to REALTOR® Jones, who prepared the offer for Buyer. Seller calls the listing agent who notifies REALTOR® Jones that Seller is rescinding the acceptance.

*If REALTOR® Jones, who is acting as a sub-agent, has not already delivered the purchase agreement to Buyer, REALTOR® Jones should not deliver it now. As a seller's agent, a sub-agent owes a fiduciary duty to the Seller which would be breached if the contract is delivered against the Seller's wishes. If the purchase agreement has not been delivered to Buyer, the acceptance is revoked and the contract is not enforceable.*

As can be seen from the above examples, timing can mean everything in the context of revocation of offers, counteroffers and acceptances. An additional wrinkle can arise when the parties are delivering offers, counteroffers, acceptances and revocations by electronic mail. The following hypothetical demonstrates this additional wrinkle.

Buyer makes an offer through REALTOR® Green, who is acting as a buyer's agent. Seller rejects the offer, but makes a counteroffer which is delivered by the listing REALTOR® to the buyer's agent. While the counteroffer is pending, the listing REALTOR® holds an open house. At the open house, another prospective buyer appears and makes an offer on the spot. The seller accepts the offer made by the prospective buyer at the open house. Upon returning to her office, the listing REALTOR® discovers that the buyer's agent has emailed to her the initial buyer's acceptance of the seller's earlier counteroffer.

Even assuming that the initial buyer and the seller agreed to delivery of documents by electronic mail, there is still the issue as to when the acceptance of the counteroffer shall be deemed delivered to the listing REALTOR®. Did delivery occur when the buyer's agent hit the "send" button? Was acceptance delivered when the buyer's agent's email hit the server of the listing REALTOR®? Is the acceptance of the counteroffer not deemed to be delivered until the listing REALTOR® actually opens her email and prints the buyer's acceptance of the counteroffer? Under the common law, a strong argument could be made that delivery of acceptance of the counteroffer did not occur until physical delivery of the acceptance of the counteroffer, *i.e.*, until there is a printout of the counteroffer in the hands of the listing REALTOR®. To avoid uncertainty, when agreeing to the electronic delivery of documents, sellers and buyers should also agree as to <u>when</u> delivery will be deemed to have been made. There is no law specifying when delivery is made by electronic mail. Three (3) other states have addressed this issue and MAR has adopted a policy following the lead of those states. Under MAR's model provision with respect to electronic delivery of documents, it is provided that

delivery occurs upon a REALTOR®'s transmission of the document, *i.e.*, when the REALTOR® hits the "send" button.

There is a misconception among some REALTORS® that a purchase agreement is not binding until "bottom lined." In actuality, there is a valid, binding purchase agreement once an offer is presented by the purchaser and accepted by the seller. The "bottom line" signature serves only as verification that the signed purchase agreement has in fact been provided to the buyer. (The Occupational Code requires licensees to deliver "true executed copies of the acceptance" to the buyer – the bottom line signature merely serves as a confirmation that this was done.) Even if a buyer refuses to sign the "bottom line" of a purchase agreement, it is nonetheless binding and in full force and effect.

> Example
>
> Buyer presents an offer to Seller. Seller accepts the offer by signing and delivering it to Buyer without making any changes. Buyer has changed his mind and refuses to "bottom line."
>
> *The purchase agreement is binding. Buyer's refusal to "bottom line" the agreement does not alter its status as a fully executed, legally binding contract.*

Finally, REALTORS® representing buyers who have put in offers on a home are often frustrated when they receive no written response from the seller, particularly where the buyer's offer is at or close to the listing price. A buyer who receives no counteroffer or other indication in writing that the seller has considered and rejected his offer, may question whether his offer has in fact been presented to the seller. REALTORS® representing a buyer in this situation often call the MAR Hotline to inquire as to whether the seller is required to reject the offer in writing. The

simple answer to this question is "no." A seller who receives an offer can accept, reject or counter that offer in writing. In addition, the seller can simply do nothing. A buyer can request that the seller respond in writing, however, the seller has no legal obligation to do so. If the seller neither accepts nor rejects the offer, the offer will expire after a reasonable time (or until it expires under its own terms or is otherwise revoked by the buyer).

### 4. Backup Offers

In the current market, there would appear to be very little call for backup offers in the traditional sense, *i.e.*, multiple bids at or above a list price sufficient to pay off seller's mortgage AND leave the seller with pockets full of cash. Nonetheless, there is an ongoing practice which is resulting in multiple offers which can result in some of the same issues. These multiple offers are occurring in the case of both short sales and sales of REO properties. In this section, we will first cover the contract principles applicable to backup offers generally and then relate those principles to multiple offers in the context of short sales and sales of REO properties.

Problems with backup offers appear to arise under essentially the same set of facts. REALTOR® Jones has a listing for the Smith property for $100,000. The Browns become interested in the Smith property and offer $99,000 for the property, subject to contingencies which include an inspection. The Smiths accept the Browns' offer. Within 24 hours, the Greens (who previously looked at the Smith property) submit an offer for $98,500. The Smiths express concerns about the contingencies in the Browns' offer, and request that REALTOR® Jones take whatever steps she needs to take in order to keep the Greens interested in the property.

REALTOR® Jones prepares a counteroffer to the Greens' offer in which it is indicated that the Smiths are accepting the Greens' offer as a backup to the Browns' "purchase agreement dated March 16, 2011." This counteroffer is accepted by the Greens.

In the meantime, the Browns undertake their inspection of the Smith property. The Browns discover problems with the septic system and the well on the Smith property, and initiate a negotiation to amend the purchase agreement dated March 16, 2011 to obtain a credit for $2,200, which is equal to the estimate that the Browns have obtained to fix the problems with the septic system and the well. The Smiths discuss this proposed amendment with REALTOR® Jones, and ultimately conclude that it is acceptable. On March 28, 2011, the Smiths and the Browns enter into an amendment to the purchase agreement dated March 16, 2011. A closing is scheduled for April 20, 2011.

Unfortunately, on April 20, 2011, REALTOR® Jones cannot conduct a closing of the sale from the Smiths to the Browns. The closing cannot occur because the Greens have filed a lawsuit and filed a lis pendens against the Smith property, claiming that they have a binding purchase agreement with the Smiths to purchase the property. The Greens' position in court is that their offer was a backup to the Browns' "purchase agreement dated March 16, 2011." When the Smiths and the Browns amended the March 16, 2011 purchase agreement, the Greens argue, the Smiths and Browns entered into a new deal dated March 28, 2011. Thus, it is the Greens' position that their backup offer became effective on the date that the Smiths and Browns modified the March 16, 2011 purchase agreement.

Prior to the decline in the real estate market, there were a number of cases filed based on this scenario. There are no known judicial decisions of record based on this set of facts for a very simple reason. The Smiths want to sell their home and both the Browns and the Greens claim they have binding contracts to purchase the Smiths' home. Typically, the Smiths, along with REALTOR® Jones, end up paying one potential buyer to go away so that the transaction with the other buyer can be completed.

There is absolutely no reason for REALTORS® to find themselves, and the sellers and buyers whom they represent, in this situation. REALTORS® should develop consistently-used uniform language which has been approved by their counsel when they prepare backup offers. In the past, we have prepared a provision which REALTORS® could use with backup offers in order to avoid this situation. This clause provides as follows:

> Buyer acknowledges that this Agreement is a backup offer which shall be effective only in the event that the closing on the prior purchase agreement on the property does not take place for any reason. Buyer acknowledges that nothing in this Agreement shall in any way restrict the right of the Seller to modify the terms of the prior purchase agreement as Seller shall, in his sole discretion, deem advisable.

Obviously, REALTORS® can opt to use whatever clause they wish to use in handling backup offers. They simply need to make sure that they include language such as the above-quoted language in the backup offer to make certain that they do not end up with competing claims by buyers which tie up the property in court.

There is another potential issue with backup offers from the second buyer's perspective. In the above scenario, to what extent are the Greens bound to wait for the Smiths' home to

become available? Suppose four (4) weeks go by and the closing with the Browns is still up in the air. Can the Greens resume their search for another home to purchase or are they bound to wait longer to see if the Smiths sell their home to the Browns? Again, this can be clarified by including a specific provision in a backup offer. Our suggested language is:

> In the event that the Sellers do not notify the Buyers that this backup offer is in first position within _____ days of the date hereof, the Buyers may at any time thereafter declare this agreement null and void by providing written notice of same to the Sellers.

We have received many telephone calls over the MAR Legal Hotline involving the following situation: a REALTOR®, acting as a buyer's agent, has an accepted offer on an REO property or a short sale property but is waiting for the seller's lender's approval. In these calls, the REALTOR® has received a question from her buyers as to when they can terminate the REO transaction or the short sale transaction so they can get on with their search for another home. The answer is easy in the REO transaction – if the buyers have submitted an offer on an REO property that has simply gone unanswered, the buyer's agent may revoke the offer through the listing REALTOR®. The answer is not so simple in the situation where the seller has accepted the buyer's offer subject to approval by the seller's lender. If the purchase agreement is silent, there is no definitive answer that the buyer's agent can give to the buyer. If a buyer's agent wants to be in a position to provide these buyers with a definitive answer, a REALTOR® can insert a provision in the offer to provide clarification as follows:

> In the event that the Sellers do not notify the Buyers that the Sellers' lender has approved this agreement within ___ days of the date hereof, the Buyers may at any time thereafter declare this

> agreement null and void by providing written notice of same to the Sellers.

As discussed above, some REALTORS® in a short sale situation work with sellers who accept multiple offers on their property subject to approval by the seller's lender and the seller's approval of the lender's terms. Again, these REALTORS® and sellers are relying on the seller's lender to accept only one of multiple accepted offers which have been forwarded to the lender by the listing REALTOR®. Many REALTORS® have expressed concern that some lenders may inadvertently approve more than one offer accepted by a seller, resulting in the seller being subject to two or more binding purchase agreements. This risk can be avoided if after forwarding the first seller-accepted offer to the lender, all subsequent seller-accepted offers are designated as backup offers. In doing so, the listing REALTOR® will wish to make certain that the protective language discussed above for backup offers is included.

### 5. Time for Performance

Consider the following scenario. Seller Jones and Buyer Smith have entered into a buy and sell agreement which is contingent upon Smith obtaining financing within fourteen (14) days and requires a closing within twenty one (21) days. Smith's loan application is delayed several times. In the meantime, Seller Jones receives a second offer on his home which is better than Smith's offer. At what point is Seller Jones free to sell his home to the second buyer? Unfortunately, the law is such in Michigan that there is no date at which Seller Jones can proceed "risk free" with the second buyer. As will be discussed below, in the past, Michigan courts have not strictly enforced time deadlines in purchase agreements.

As REALTORS® are well aware, real estate closings often do not occur as planned, with sellers and buyers frequently seeking oral or written agreements to extend closing dates, based on financing delays, delays in the sale of the buyer's prior residence, or for numerous other reasons. While these delays might be irritating or frustrating to the seller, in general Michigan law does not permit the seller to terminate a purchase agreement and accept a more favorable offer, merely because the closing date specified in the purchase agreement has been delayed or postponed.

Michigan courts have held to these general rules for almost a century. Time of performance rules were first set forth in the leading case of *Waller v Lieberman*, 214 Mich 428 (1921). In that case, Waller signed a purchase agreement to buy property from Lieberman, and the deal was to have closed on September 8, 1916. Waller was hospitalized on September 7, and did not provide the money and documents needed by the escrow agent for closing before being hospitalized. Lieberman subsequently learned of Waller's illness and consented to postponing the transaction. However, Lieberman later attempted to cancel the transaction on December 12, claiming that Waller had defaulted, and Waller sued for specific performance.

In defense, Lieberman argued that "time was of the essence." In the real estate context, this basic principle of contract law means that where the parties have agreed that the time for performance is an essential element of the contract, the closing must occur on or before the date and time specified, or the agreement will be void. The court rejected Lieberman's assertion that in this instance, the parties had agreed that time was of the essence:

> [t]here is nothing in the written contract, or in the conduct of the parties, tending to establish the fact that time was of the essence of the contract, other than the naming of the due date; **and it has been frequently held that the naming of the date on which the payment shall become due does not in itself make time of the essence of the contract**. (Emphasis added.)

In addition, the court held that even where the parties to a purchase agreement do provide that the contract be performed within the time specified, they may waive the time condition by oral or written agreement to extend the time for performance. The waiver then operates "as a waiver of the vendor of the right to rescind, or forfeit the contract for the failure of the purchaser to comply strictly with the term [thereof] relating to payment."

Courts have continued to follow the *Waller* decision, making additional refinements to the basic rules set forth above. For example, in *Al-Oil, Inc v Pranger*, 365 Mich 46 (1961), the parties signed a purchase agreement for the sale of property on which the buyer wished to construct a gas station. The purchase agreement obligated the buyer to obtain the necessary governmental permits and zoning within sixty days. While the buyer diligently worked on the approval process, keeping the sellers advised of his progress, the final approval was not obtained for more than four months. The sellers then refused to perform the contract, as they apparently believed that "they could sell the land for more money than [buyer] had offered if they could avoid carrying out their agreement."

The court rejected the sellers' argument that the sixty-day approval period made "time of the essence" for the performance of the contract, preventing the sellers from rescinding the agreement based on the delay in closing. Not only did the mere naming of the time for

performance in the purchase agreement not make "time of the essence," but the sellers had also knowingly waived any time for performance requirement by their awareness of the buyer's ongoing efforts to obtain governmental approval. The *Al-Oil* court did note that rescission by a seller might be possible under very limited circumstances:

> Where a stipulation for performance at a particular time has been waived, the party in whose favor the waiver operates is thereafter bound only to perform within a reasonable time, except in a case where there has been a specific extension of time, in which case it is held that the new time fixed becomes of the essence, as was the case in the original contract. **So, where the time fixed by the contract for performance is permitted to pass, both parties concurring, the time of performance thereafter becomes indefinite, and one party cannot rescind until full notice and a reasonable time for performance is given**. (Emphasis added.)

Michigan courts have repeatedly emphasized that due to the drastic effect of a "time is of the essence" provision in a real estate purchase agreement, *i.e.*, the complete termination of the agreement if the specified closing date is not met, the buyer and seller must clearly intend time to be an "essential element" of their agreement. While the intent to include time as an essential element can be implied from the nature of the contract and the surrounding circumstances, such an intent must "necessarily" be implied. *Nedelman v Meininger*, 24 Mich App 64, 74 (1970).

Courts have also held that the use of form purchase agreements prepared by state or local boards of REALTORS®, and the inclusion of a specific closing date or time limit in the space provided on the form, does not independently make "time of the essence" to the parties' agreement. *Kennedy v Brady*, 43 Mich App 760, 763-764 (1973). As courts recognize, these types of forms are used for convenience, and do not constitute a true negotiated expression of

the parties' intent to stress the importance of a specific time for performance. For example, in *In re Day Estate v Plumb*, 70 Mich App 242, 246 (1976), the court rejected a buyer's attempt to rescind a purchase agreement based on delay by the sellers, where the testimony of the real estate broker indicated that he inserted the 30-day closing requirement in the purchase agreement as a "matter of course," not because of any concern by his clients that the contract be executed immediately.

The clear message from the above cases is that there is no foolproof manner for imposing time deadlines in purchase contracts which will be strictly enforced by Michigan courts. When faced with this issue, courts will look at the specific facts of the case to determine first whether the parties to the purchase agreement negotiated or otherwise stressed the importance of time deadlines in the purchase agreement and if so, whether the seller later waived or extended those time deadlines. Reliance on the time deadlines to rescind a purchase agreement based on the alleged failure to meet the time for performance established in the purchase agreement is a risky proposition. This is particularly true where the seller seeks to rescind in order to accept a better offer. REALTORS® who have clients who seek to terminate a purchase agreement as a result of the seller's or purchaser's failure to meet certain time deadlines should advise those clients to seek the advice of an attorney.

### B. Contract Termination

A purchase agreement can be terminated in many ways. A party may terminate it as permitted under one of the contingencies, the buyer may elect to terminate under a statutory

provision (such as the Seller's Disclosure Act), the parties may agree by mutual consent, or a party may breach the contract.

Contrary to popular belief, there is no 3-day right of rescission for contracts for the sale of real estate. There are consumer protection statutes which provide a rescission period in certain circumstances (such as telephone or door-to-door sales); however those statutes do not apply to contracts for the sale of real estate.

REALTORS® are sometimes approached by buyers or sellers who have changed their minds and want to be released from the contract. The REALTOR® may be inclined to try to convince their clients that they must go forward with the sale so that the REALTOR®'s commission is not jeopardized. However, REALTORS® should be wary of doing so in light of their fiduciary duties. It may be in the client's best interest to obtain a release. If a REALTOR® is approached by a client who now wants out of the contract, the REALTOR® should advise the client to seek the advice of an attorney. It is in a REALTOR®'S best interest to have his client rely on the advice of an attorney as to the enforceability of the contract.

It is not uncommon for both parties to agree to terminate the contract. For example, the buyer may be having difficulty obtaining financing at the desired interest rate, and the seller may have other interested buyers in a position to close. The parties may agree to terminate the purchase agreement by signing mutual releases. Such releases should always provide for the disbursement of the earnest money deposit.

If the parties do not mutually agree to a release, but one party refuses to go forward with closing, the contract is terminated by the party's breach of contract. The non-breaching party

may have legal remedies including specific performance or damages incurred as a result of the breach. REALTORS® should never make determinations as to whether a party has in fact breached the contract, but again should refer the client to an attorney. While a breach of contract by the buyer likely means the seller is free to sell the home to someone else, in the absence of a release, this determination should be made by an attorney. A REALTOR® does not want to be responsible for putting a client in a position where two buyers are claiming they have a valid purchase contract.

Based upon calls received on the Legal Hotline, there appears to be a common misconception that if the contract is terminated, a house cannot be sold to someone else while the earnest money is in dispute. This is incorrect. The status of the earnest money has no bearing on the seller's ability to sell the home. The primary concern is that the seller might still be bound by the first purchase agreement in the absence of a written release. A release can be executed leaving the earnest money in dispute. If a release cannot be obtained, the REALTOR® should advise the sellers to contact an attorney to determine whether they are in fact free to sell the home to another buyer.

When a sale does not close, the earnest money is frequently in dispute. License law provides that where there is a dispute, a REALTOR® cannot disburse the earnest money to either party in the absence of signed releases or a court order. In addition, a REALTOR® who releases money to one party may find himself obligated to pay the other party if a court should later disagree with his assessment of the rights of the parties. A REALTOR® faced with a buyer and seller who both claim the earnest money deposit can bring an interpleader action, in which a

court will make the determination as to the proper disbursement of the funds. REALTORS® are not required to bring such an action. Rather, they can retain the money until such time as the parties agree – or a court issues an order – as to the disbursement of the funds.

## III. CONCLUSION

REALTORS® should utilize their knowledge of contract concepts to help make the process go smoothly. A solid understanding of the concepts addressed in this article will enable REALTORS® to better serve their clients and reduce their own potential liability. When problems arise, however, REALTORS® should advise their clients to contact an attorney rather than offer legal advice as to the interpretation and/or enforcement of the contract terms.