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REAL ESTATE PROFESSIONAL LEGAL UPDATE

In This Issue

Upcoming Event

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Foreclosure Trends and Related Issue

April 24th, 2012
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NEW CASE SHOWS THAT CREATIVE ARGUMENTS CAN UNDERCUT EXCULPATORY CONTRACT PROVISIONS: DUNCAN V. MCCAFFREY

By Rinat B. Klier-Erlich

The new case of Duncan v. The McCaffrey Group Inc. (2011) 200 Cal. App. 4th 346 reminds us that the written language in a purchase agreement is final and binding, but as typically the case with the law, there is always a creative way to go around it, even if this eventually leads no where.

In Duncan, plaintiffs purchased 2 lots at a new development in 2006 and 2007. At the time they purchased the lots they were advised by the developers that the development was intended for custom homes only. Similarly, the CC&Rs for the development did not allow homes to be smaller than 2,700 square foot. After plaintiffs purchased their lots the developers amended the CC&Rs to allow minimum home sizes of 1,400 square foot, and they began constructing tract homes. Plaintiffs filed a lawsuit and alleged that this conduct diminished the value of their lots.

The issue on appeal was a dismissal of plaintiffs' Unfair Business Practices claim and fraud claim following a demurrer, and the dismissal of plaintiffs' breach of fiduciary duty cause of action following a motion for summary judgment. In particular, the Court of Appeal was focused on the parol evidence rule and how it would affect the presentation of evidence.

The parol evidence rule is codified in Code of Civil Procedure section 1856. It prohibits the introduction of evidence that would vary, alter, or add to the terms of a written agreement that is integrated. An agreement is integrated when it is the complete, final and superseding written agreement between the parties.

In Duncan, paragraph 9(a) of the parties' agreement specifically permitted the developers to change the development plan, their marketing methods and price, and it allowed them to sell products on more favorable terms including, building residences of different types.

The agreement in Duncan was also integrated. Paragraph 18(d) stated that the agreement was the only agreement between the parties and all prior and contemporaneous negotiations were merged into it and superseded by it, and that the only representations made by the developers were those set forth in writing in the agreement.

Based on the foregoing, the Court of Appeal agreed with the lower trial court that most of the claims were barred by the parol evidence rule. The plaintiffs in the case would not be able to admit evidence of different representations since they agreed in the purchase contract that they did not rely on any representations not in the agreement and that the developers could do what they ended up doing–maximize their profits by any means.

However, the Court of Appeal reversed the dismissal of the Unfair Business Practices Act. The Unfair Business Practices Act and specifically Business & Professions Code section 17500 pertains to unfair competition and makes actionable any unlawful, unfair, or fraudulent business act or practice, or any unfair, deceptive, untrue, or misleading advertising. The Code requires however, that the plaintiffs have actual injury, which in this case, is the loss in value due to the purchase of the lots in reliance on the advertising that lots would be limited to 2,700 square feet of custom homes.

The developers alleged that the misrepresentations was unreasonable as a matter of law, because of the language of paragraph 9(a) of the agreement specifically permitting them to change the product they were selling.

Yet, the Court of Appeal disagreed. It found that this cause of action did not attempt to vary,

alter, or add to the terms of the written agreement by alleging that misrepresentations induced the plaintiffs to enter into the agreement like in the other causes of action. Instead, in the false advertising claim plaintiffs merely alleged that defendants engaged in a campaign of false advertising when marketing the lots. Plaintiffs did not argue that after entering into the terms of the agreement the developers were prohibited from building tract homes in the development. Hence, this cause of action was unrelated to the contract.

The reliance required in a false advertising claim is different from reliance required in common law fraud. In fraud, the deception must be actually false, known to be false by the perpetrator and reasonably relied upon by a victim who incurs damages. None of these elements are required in a false advertising claim. The reason is that although false advertising requires reliance, it focuses on the defendant's conduct, rather than the plaintiff's damages, because the purpose of the Unfair Business Practices statute is to protect the general public against unscrupulous business practices. In re Tobacco II Cases (2009) 46 Cal.4th 298, 312 ("While a plaintiff must show that the misrepresentation was an immediate cause of the injury-producing conduct, the plaintiff need not demonstrate it was the only cause.").

The interesting point about this is that the damages awardable in Unfair Business Practices claims are an injunction, possibly restitution of the profits made from the sale of the two lots and discretionary attorney's fees. Hence, this cause of action will not copmpensate the Duncan plaintiffs for their loss of value.

With respect to fraud, inconsistent promises that contradict the contract are inadmissible. While there are exception to this rule, after analyzing cases
that found an exception, the Court of Appeal concluded that the Duncan facts do not fall within the fraud exception to the parol evidence rule. Further, the language about which plaintiffs complain was not hidden in fine print, but was
highlighted for them, as they initialed the paragraph. Therefore, only the Unfair Business
Practices claim survived the parol evidence attack.

After the trial court dismissed the above causes of action the breach of fiduciary
duty against defendant broker continued and a motion for summary judgment was filed. A motion for summary judgment, as opposed to a demurrer, evaluates the evidence. In the motion, the defendant broker argued that the contract was clear that it did not represent the buyers. However, the Court of Appeals found that the contract was actually ambiguous. In one place it stated that the defendant broker was acting as both the listing and selling agent.

Once that ambiguity was found extrinsic evidence could be admitted to explain it (per the parol evidence rule). Further, this makes it a disputed fact as to whether the defendant broker
was in fact a dual broker, which would defeat summary judgment and send the case to trial by a jury.

This shows us that persistence in pleading Unfair Business Practices and breach of fiduciary duty against the broker may have kept this case from being dismissed, but it is still a long shot for success. The damages under Business and Professions Code are limited to an injunction and damages against a broker may be narrower than damages against a seller. Further, this teaches us that contract language can be very helpful (we must read contracts carefully) and when we use the contract to our advantage, we should be careful not to create any ambiguity.

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When Transacting With a Trust, Remember That the Trustees, Not the Trust Itself, Are the Correct Parties

By John P. Cogger

We often find ourselves in transactions or litigation with named parties in relation to a trust. It is important to remember that when litigating or entering into contracts relating to a trust, the real parties in interest are the trustees, not the trust. The Court of Appeals for the Third Appellate District recently reaffirmed that notion, serving a reminder that a trust is not a person for litigation purposes. Specifically, the Court held that a trust is not a person but rather a fiduciary relationship with respect to property. As such, a trust itself cannot sue or be sued. As a general rule, the trustee is the real party in interest with standing to sue and defend on the trust's behalf.

"A trust is not an entity and any action by or against the trust must proceed through the trustees. A judgment against trust assets must be asserted the same way, against the trustees in their representative capacity, as it is the trustees who hold title to the property held in trust." Portico Management Group, LLC v. Harrison, 2011 Cal. App. LEXIS 1642, 19-20 (Cal. App. 3d Dist. Dec. 28, 2011)

As the above Court noted in its' decision, formalities matter. Ensure that the proper parties are named. When dealing with a trust, the action must proceed through the trustees. When entering into agreements relating to a trust, make sure that the

agreements are signed by the correct parties in interest, the trustees. And when litigating with a trust (or resolving claims relating to a trust), make sure that the trustees are the named participants and signatories.

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Real Estate Broker Denied Compensation Despite Bringing Seller a "Full Price" Offer

By David I. Gorney

What does "or" mean? In a recent commercial real estate broker's commission collection case, it meant no compensation for a selling 'cooperating' broker trying to collect a commission from the seller after delivering a 'full price' offer based on what turned out to be an ambiguous provision in a listing agreement between seller and listing broker. In Realpro, Inc. v. Smith Residual Company, LLC (2/28/12) Cal. Crt. of Appeal, 4th App. District (E052369), the seller signed a commercial listing agreement containing the following price and terms:

> $17,000,000 cash or such other price and terms acceptable to [Sellers], and other additional standard terms reasonably similar to those contained in the [AIR standard form].

The listing agreement specifically provided that a 'cooperating broker' could enforce the terms of the listing agreement against listing broker or sellers "as a third party beneficiary hereof". In general, a person intended to be a 'third-party beneficiary' is entitled to enforce performance of a written contract between others.

Plaintiff selling broker submitted a 'full price' offer. The listing broker acknowledged receipt and via a counter-offer indicated that the price was being increased to $19,500,000 but that all other terms in the offer were acceptable to seller. Listing and selling brokers confirmed in writing their agreement to evenly split the 4% commission. While not explicitly stated in the opinion, it is obvious that selling broker's buyer client did not agree to pay $19,500,000 and the property either was taken off the market or sold to someone else.

Selling broker sued the seller for $340,000 (2% of the $17,000,000 'full price offer') based solely on the 'third-party beneficiary' provision of the listing agreement and specifically declined the opportunity provided by the Court to add the 'offer' and 'counter-offer' contract documents as the basis to sue. While the reasons are not stated in the decision, it is likely such documents would ~ as seller pointed out ~ have contradicted selling broker's contention that the sole basis of compensation was the listing agreement when obviously, the contract documents would have shown the absence of an accepted offer and, moreover, that the express terms of the offer indicated that this was "merely an offer" that would expire by a date certain.

The court of appeal affirmed the trial judge's decision to sustain seller's demurrer without further opportunity to amend. In lay language, both courts said selling broker had no legal basis to claim a commission against seller based on the language in the listing agreement even though selling broker had produced a 'full price' offer. Reaching back to a 1947 California Supreme Court decision (Palmtag v. Danielson (1974) 30 Cal.2d 517) observing that "Ordinarily, the price at which a broker is authorized to sell property is considered merely an asking price to guide the broker in his negotiations with prospective purchasers", the Realpro v. Smith court found that the operative language in the listing agreement (" . . . $17,000,000 cash or for such other price and terms acceptable to [Sellers]") was ". . . merely an invitation to submit offers" and thus, did not entitle selling broker to a commission even though the prospective buyer was "ready, willing and able" to perform.

Since plaintiff selling broker relied only upon the listing agreement, the Court had to decide if the compensation was contingent upon seller being brought a 'full price' offer of at least "$17,000,000 cash or for such other price and terms acceptable" to seller. Selling broker argued it's 'full price' offer met the first part of the disjunctive phrase ("$17,000,000 cash") by bringing seller an offer in that amount. Seller argued that this number was just the listing price and as such, merely represented an invitation to make an offer. The Court rejected selling broker's argument and observed that the word "or" applied only to the price term and not the "terms acceptable" provision. In essence, the court parsed the contract to mean '$17m cash or such other price and terms acceptable to the Seller', reasoning that meeting the price term alone is not enough to earn a commission because a real estate transaction ~ this one included ~ always includes other terms. In doing so, the decision approved the trial court's comment that "This listing isn't just bringing an offer with numbers . . . ."

At first blush, the court's strained parsing raises eyebrows. After all, the word "or" clearly separates two separate phrases and no creative use of commas could make this any clearer. But the court could not overlook the language of the actual offer and counter-offer placed in the record by seller ~ efforts resisted by the selling broker ~ which made it clear that this was just an offer and at that, one that would expire in a few days. Since the offer was just that, an 'offer', it neatly fell into the long-established Palmtag

rule that considered the listing price as simply an invitation to make an offer. No doubt also, the court did not appreciate selling broker's tactical decision not to include the actual offer and counter-offer in the record concluding (as it ultimately did) that the actual documents conflicted with selling broker's argument.

Absent a unilateral compensation agreement with the seller (which as a practical matter cannot be obtained), it is unlikely selling broker could have done anything to insure payment because it was stuck with the language in the seller-listing agent listing agreement. However, the Realpro decision would by the same logic have doomed listing broker's compensation claim had seller declined to accept a 'full price' offer. A listing broker should insist upon language making it absolutely clear that compensation would be earned if an offer in the amount of listing price were presented to seller. The Realpro court would have had a much more difficult time in ruling against either listing or selling broker if the listing agreement explicitly identified the specific events triggering an earned commission, such as "Compensation is payable if Broker presents Seller with one of the following two alternatives: (a) An offer of $17,000,000 cash; or (b) an offer for such other price and terms acceptable to Seller."

Residential selling brokers in California should not be confronted with this problem since the vast majority of transactions are governed by the Model Multiple Listing Service ("MLS") rules in which the compensation agreement between MLS members or participants is an implied in law contract between the listing and selling brokers in which compensation is due the selling broker upon close of escrow or receipt of monies by listing broker following buyer's default. The various California Association of Realtors listing agreement forms should insure that listing broker is paid since it very specifically says compensation is due upon presentation of a 'full price' offer OR seller's acceptance of an offer of other terms:

If during the Listing Period, or any extension, Broker, Seller, cooperating broker, or any other person procures a buyer(s) who offers to purchase the Property on the above price and terms, or on any price and terms acceptable to Seller. (Broker is entitled to compensation whether any escrow resulting from such offer closes during or after the expiration of the Listing Period.)

Accordingly, residential listing agents should try to avoid changing the language of these standard listing forms.

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