

Contracts

Objectives

Upon completion of this section, the student should be able to:

- Describe a typical buyer's concerns that cause them to be reluctant to enter into a representation agreement and how to address these concerns in a professional manner.
- Discuss various listing agreement addenda that may be used and when you would need to use them.
- Describe what happens when a listing agreement is terminated.
- Explain what happens to current listing agreements under the following situations:
 - Death of the designated broker;
 - Firm goes out of business;
 - Designated broker loses their license in a disciplinary action and listing broker transfers to a different real estate firm.
- Identify potential situations where the principal (buyer or seller) would default on a purchase and sale contract and some legitimate reasons for termination of a contract by a client.
- Describe when the licensee is liable or potentially liable from a poorly constructed/crafted contract and explain what possible disciplinary procedures may result.
- Explain how a properly constructed Purchase and Sale Agreement (PSA) with appropriate addenda (to address needed contingencies) can reduce the risk of default.
- In the event of a default or termination, describe what obligations the licensee has toward the client and describe how to protect the client in the case of a default.
- Discuss the appropriate level of detail to include in a financing contingency clause.
- Discuss the typical elements of a property management agreement and discuss the responsibilities and powers of the property manager versus what must be approved/authorized by the property owner such as fees, commissions, maintenance, and repairs.
- Identify the unique fiscal responsibilities associated with property management such as the duty to collect rents, funds management, accounting, and monthly income statements.
- Describe the typical provisions of:
 - An apartment lease;

- A residential lease.
- Explain the appropriate precautions and procedures when using unfamiliar or non-standardized forms of contracts and agreements provided by third parties such as a bank contract for the purpose of a foreclosure property (REO) and a contract provided by a developer for a new home purchase

Typical Buyer's Concerns

Let's look at some of the typical concerns that buyers may have about entering into a representation agreement with an agent and look at how these concerns might be addressed:

- Concerns about the knowledge of their broker
- Concerns about the communication with their broker
- Concerns about the broker having a solid knowledge of the area
- Concerns about being "tied" to just one broker
- Concerns that the buyer representation will cost them a commission
- Concerns that they will not be able to cancel the contract if they are not satisfied with their broker

Concerns About the Knowledge of Their Broker

Potential buyer clients may have concerns about the knowledge and expertise of a broker. When talking to potential clients, and before asking them to sign a buyer representation agreement, the key is to educate them on the buying process. This is indicative about your experience and knowledge and, at the same time, allows the potential client to become knowledgeable about the buying process and more comfortable with you as their representative. If there is still a concern, you can offer to furnish them with references from past clients.

Concerns About the Communication with Their Broker

Potential buyer clients may have concerns about the level and mode of communication with you. The best way to handle this is to just ask about their needs and level of communication. For example, ask if they would prefer to hear from you daily or only when something specific occurs. Another example would be their preference of communication mode (i.e., email, phone, text messages, in person, etc.).

Concerns About the Broker Having a Solid Knowledge of the Area

Most potential buyers clients will want to make sure that you have strong knowledge of the area. Talk freely about the homes that you've listed or sold in the area. Also, involve your potential clients with conversations about events in the community

Concerns About Being "Tied" to Just One Broker

Many buyers feel that it may be to their benefit to have the representation of more than one broker, "The more, the better" mindset. Explain your expertise and your services and that you work very hard for your clients. In return, you'll receive their loyalty.

Concerns That the Buyer Representation Will Cost Them a Commission

Potential buyers may think that they will have to pay 100 percent of the commission that you will earn because they are being represented by you. Explain that, in most circumstances, the seller pays the commission, and in the rare cases where they would pay a commission, it is clearly stated on the buyer representation agreement.

Concerns That They Will Not Be Able to Cancel the Contract If They Are Not Satisfied with Their Broker

Explain that you will ensure that the buyer representation agreement will be unilaterally cancelable. This means that either they or the broker can cancel the agreement without the other's permission, as long as it is done in writing.

Various Listing Agreement Addenda and When You Would Need Them

Amendments

Amendments are additions to the main PSA that cover specific or unique circumstances. They are commonly referred to as addenda.

Many of these addenda become contingencies to the contract.

A contingency is a provision in a real estate contract that specifies that the contract would cease to exist upon the occurrence or non-occurrence of a certain event. A contingency should be clearly written, concise, and have a definite time limit. As a real estate professional, it will be your duty toward your client to watch these time lines very carefully and act within their limits. Many of the contingency forms essentially state that silence construes acceptance, meaning that if you don't respond within the time period specified, you have waived the contingency.

A contract could be contingent on many items but some of the most commonly used in residential real estate are:

- Inspection addendum
- Financing addendum
- Optional clauses addendum
- Homeowner insurance addendum
- An addendum which would address the personal property or fixtures included in the sale
- Possession addendum (if not at the time of closing)

Inspection Addendum

An inspection addendum usually covers an inspection of the property and deals with structural issues, some pest infestations, and underground residential heating oil tanks and on-site sewage disposal systems.

INSPECTION ADDENDUM TO PURCHASE AND SALE AGREEMENT

Continued

Seller does not agree to all of Buyer's repairs or modifications, Buyer shall have an opportunity to reply, as follows: 48
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(ii) **Buyer's Reply.** If Seller does not agree to all of the repairs or modifications proposed by Buyer, Buyer shall have _____ days (3 days if not filled in) from either the day Buyer receives Seller's response or, if Seller fails to timely respond, the day Seller's response period ends, whichever is earlier, to (a) accept the Seller's response at which time this contingency shall be satisfied; (b) agree with the Seller on other remedies; or (c) disapprove the inspection and terminate the Agreement, in which event, the Earnest Money shall be refunded to Buyer. 50
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ATTENTION BUYER: These time periods for negotiating repairs or modifications shall not repeat. The parties must either reach a written agreement or Buyer must terminate this Agreement by the Buyer's Reply deadline set forth in paragraph 1.c.ii. Buyer's inaction during Buyer's reply period shall result in waiver of this inspection condition, in which case Seller shall not be obligated to make any repairs or modifications whatsoever AND THIS CONTINGENCY SHALL BE DEEMED WAIVED. 56
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d. **Repairs.** If Seller agrees to make the repairs proposed by Buyer, then repairs shall be accomplished at Seller's expense in a commercially reasonable manner and in accordance with all applicable laws no fewer than _____ days (3 days if not filled in) prior to the Closing Date. In the case of hazardous materials, "repair" means removal or treatment (including but not limited to removal or, at Seller's option, decommissioning of any oil storage tanks) of the hazardous material at Seller's expense as recommended by and under the direction of a professional selected by Seller. Seller's repairs are subject to re-inspection and approval, prior to Closing, by the inspector who recommended the repair, if Buyer elects to order and pay for such re-inspection. If Buyer agrees to pay for any repairs prior to Closing, the parties are advised to seek the counsel of an attorney to review the terms of that agreement. 61
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e. **Oil Storage Tanks.** Any inspection regarding oil storage tanks or contamination from such tanks shall be limited solely to determining the presence or non-presence of oil storage tanks on the Property, unless otherwise agreed in writing by Buyer and Seller. 70
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f. **On-site Sewage Disposal Systems Advisory:** Buyer is advised that on-site sewage disposal systems, including "septic systems," are subject to strict governmental regulation and occasional malfunction and even failure. Buyer is advised to consider conducting an inspection of any on-site sewage system in addition to the inspection of the Property provided by this Form 35 by including an appropriate on-site sewage disposal inspection contingency such as NWMLS Form 22S (Septic Addendum). 73
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2. **NEIGHBORHOOD REVIEW CONTINGENCY:** Buyer's inspection includes Buyer's subjective satisfaction that the conditions of the neighborhood in which the Property is located are consistent with the Buyer's intended use of the Property (the "Neighborhood Review"). The Neighborhood Review may include Buyer's investigation of the schools, proximity to bus lines, availability of shopping, traffic patterns, noise, parking and investigation of other neighborhood, environmental and safety conditions the Buyer may determine to be relevant in deciding to purchase the Property. If Buyer does not give notice of disapproval of the Neighborhood Review within _____ (3 days if not filled in) of mutual acceptance of the Agreement, then this Neighborhood Review condition shall conclusively be deemed satisfied (waived). If Buyer gives a timely notice of disapproval, then this Agreement shall terminate and the Earnest Money shall be refunded to Buyer. 78
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3. **PREINSPECTION CONDUCTED.** Buyer, prior to mutual acceptance of this Agreement, conducted a building, hazardous substances, building and zoning code, pest or soils/stability inspection of the Property, and closing of this Agreement is not conditioned on the results of such inspections. Buyer elects to buy the Property in its present condition and acknowledges that the decision to purchase the property was based on Buyer's prior inspection and that Buyer has not relied on representations by Seller, Listing Broker or Selling Broker. 87
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4. **WAIVER OF INSPECTION.** Buyer has been advised to obtain a building, hazardous substances, building and zoning code, pest or soils/stability inspection, and to condition the closing of this Agreement on the results of such inspections, but Buyer elects to waive the right and buy the Property in its present condition. Buyer acknowledges that the decision to waive Buyer's inspection options was based on Buyer's personal inspection and Buyer has not relied on representations by Seller, Listing Broker or Selling Broker. 93
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Buyer's Initials Date Buyer's Initials Date Seller's Initials Date Seller's Initials Date

As a result of this inspection, the buyer can approve of the inspection, terminate the transaction, request additional inspections, or ask the seller to perform repairs or modifications. The seller may agree to perform the requests repairs/modifications or refuse. The buyer retains the right to proceed or terminate the contract. The form for responding is shown below (NWMLS Form 35R).

Financing Addendum

When an offer is contingent upon the buyer obtaining financing, NWMLS Form 22A can be used for example. This form specifies:

- Type of loan that the buyer will acquire
- Percentage of down payment
- Time frame to make application if they have not already done so
- Time frame for a loan commitment
- Consequence of an appraisal being less than the sale price
- Closing costs that the seller will pay for the buyer
- Homeowner insurance contingency

Note: Consider using this form even if your buyer is paying cash or the offer is not contingent upon financing for the following reasons: In the event that your clients decide to have an independent appraisal performed, the appraisal paragraph will allow the buyer to terminate the deal if the appraisal is less than the sale price. Most important, however, is paragraph #10 (See Form 22A below) NOTICE TO BUYER CONCERNING INSURANCE. This paragraph is, in effect, an insurance contingency and will allow the buyer to terminate the contract if they are unable to obtain homeowner's (hazard) insurance. Another option for assuring that your buyer will have an insurance contingency is to use NWMLS Form 22 VV. which is shown later in this section.

**FINANCING ADDENDUM TO
PURCHASE & SALE AGREEMENT**

Continued

4. **LOAN COST PROVISIONS.** Seller shall pay up to \$ _____; or _____% of the Purchase Price (\$0.00 if not filled in), which shall be applied to Buyer's Loan(s) and settlement costs, including prepaids, loan discount, loan fee, interest buy down, financing, closing or other costs allowed by lender. That amount shall include the following costs that lender is prohibited from collecting from Buyer: (a) up to \$300.00 for Buyer's Loan(s) and settlement costs for FHA/USDA/VA loans; and (b) unless agreed otherwise below, Buyer's share of the escrow fee for a VA loan. Seller shall pay the costs for (a) and (b), even if the amount agreed upon in this Paragraph 4 is insufficient to pay for those costs. If checked, Buyer shall pay Buyer's share of the escrow fee for the VA loan (note that VA regulations prohibit Buyer from paying loan and settlement costs exceeding one percent of the amount of the loan). 46-54
5. **EARNEST MONEY.** If Buyer has not waived the Financing Contingency, and is unable to obtain financing by Closing after a good faith effort then, on Buyer's notice, this Agreement shall terminate. The Earnest Money shall be refunded to Buyer after lender confirms in writing (a) the date Buyer's loan application for the Property was made, including a copy of the loan estimate that was provided to Buyer; (b) that Buyer possessed sufficient funds to close (e.g. down payment, closing costs, etc.); and (c) the reasons Buyer was unable to obtain financing by Closing. If Seller terminates this Agreement, the Earnest Money shall be refunded without need for such confirmation. 55-61
6. **INSPECTION.** Seller shall permit inspections required by lender, including but not limited to structural, pest, heating, plumbing, roof, electrical, septic, and well inspections. Seller is not obligated to pay for such inspections unless otherwise agreed. 62-64
7. **APPRAISAL LESS THAN SALE PRICE.** 65
- a. **Notice of Low Appraisal.** If lender's appraised value of the Property is less than the Purchase Price, Buyer may, within 3 days after receipt of a copy of lender's appraisal, give notice of low appraisal, which shall include a copy of lender's appraisal. NWMLS Form 22AN may be used for the notices in this Paragraph 7. 66-68
- b. **Seller's Response.** Seller shall, within 10 days after Buyer's notice of low appraisal, give notice of: 69
- (i) A reappraisal or reconsideration of value, at Seller's expense, by the same appraiser or another appraiser acceptable to lender, in an amount not less than the Purchase Price. Buyer shall promptly seek lender's approval of such reappraisal or reconsideration of value. The parties are advised that lender may elect not to accept a reappraisal or reconsideration of value; 70-73
- (ii) Seller's consent to reduce the Purchase Price to an amount not more than the amount specified in the appraisal or reappraisal by the same appraiser, or an appraisal by another appraiser acceptable to lender, whichever is higher. (This provision is not applicable if this Agreement is conditioned on FHA, VA, or USDA financing. FHA, VA, and USDA financing does not permit the Buyer to be obligated to buy if the Seller reduces the Purchase Price to the appraised value. Buyer, however, has the option to buy at the reduced price.); 74-79
- (iii) Seller's proposal to reduce the Purchase Price to an amount more than the amount specified in the appraisal and for Buyer to pay the necessary additional funds (the amount the reduced Purchase Price exceeds the appraised value) to close the sale; or 80-82
- (iv) Seller's rejection of Buyer's notice of low appraisal. 83
- If Seller timely delivers notice of (i) reappraisal or reconsideration of value; or (ii) consent to reduce the Purchase Price to an amount not more than the amount specified in the appraisal (except for FHA, VA, or USDA financing), and lender accepts Seller's response, then Buyer shall be bound by Seller's response. 84-86
- c. **Buyer's Reply.** 87
- (i) Buyer shall have 3 days from either Seller's notice of rejection of low appraisal or, if Seller fails to respond, the day Seller's response period ends, whichever is earlier, to (a) waive the Financing Contingency; or (b) terminate the Agreement, in which event the Earnest Money shall be refunded to Buyer. 88-90
- (ii) If Seller proposes to reduce the Purchase Price to an amount more than the appraised value, Buyer shall have 3 days to (a) accept and represent that Buyer has sufficient funds to close the sale in accordance with this provision; or (b) terminate the Agreement, in which event the Earnest Money shall be refunded to Buyer. 91-93

Buyer's Initials Date Buyer's Initials Date Seller's Initials Date Seller's Initials Date

**FINANCING ADDENDUM TO
PURCHASE & SALE AGREEMENT**

Continued

- (iii) If Seller consents to reduce the Purchase Price to an amount not more than the appraised value for FHA, VA, or USDA financing, Buyer shall have 3 days to (a) give notice that Buyer will buy at the reduced price; or (b) terminate the Agreement, in which event the Earnest Money shall be refunded to Buyer. 94-96
- Buyer's inaction during this reply period shall result in termination of the Agreement and return of the Earnest Money to Buyer. The Closing Date shall be extended as necessary to accommodate the foregoing times for notices. 97-99
8. **FHA/VA/USDA - Appraisal Certificate.** If this Agreement is contingent on Buyer obtaining FHA, VA, or USDA financing, notwithstanding any other provisions of this Agreement, Buyer is not obligated to complete the purchase of the Property unless Buyer has been given in accordance with HUD/FHA, VA, or USDA requirements a written statement by FHA, VA, USDA or a Direct Endorsement lender, setting forth the appraised value of the Property (excluding closing costs). Seller and Buyer shall execute a document setting forth the prior provision, or similar provision, known as the FHA, VA, or USDA amendatory clause, as required by lender. Buyer shall pay the costs of any appraisal. If the appraised value of the Property is less than the Purchase Price, Paragraph 7 above shall apply. 100-107
- Purpose of Appraisal.** The appraised valuation is arrived at only to determine the maximum mortgage FHA, VA, or USDA will insure. FHA, VA, or USDA do not warrant the value or the condition of the Property. Buyer agrees to satisfy himself/herself that the price and condition of the Property are acceptable. 108-110
9. **EXTENSION OF CLOSING.** If, through no fault of Buyer, lender is required by 12 CFR 1026 to give corrected disclosures to Buyer due to (a) a change in the Annual Percentage Rate ("APR") of Buyer's Loan(s) by .125% or more for a fixed rate loan or .250% or more for an adjustable rate loan; (b) a change in the loan product; or (c) the addition of a prepayment penalty, then upon notice from Buyer, the Closing Date shall be extended for up to 4 days to accommodate the requirements of Regulation Z of the Truth in Lending Act. This paragraph shall survive Buyer's waiver of this Financing Contingency. 111-116

Buyer's Initials Date Buyer's Initials Date Seller's Initials Date Seller's Initials Date

Optional Clauses Addendum

An optional clause addendum addresses such items as:

- Square footage, lot size, and encroachments
- Title insurance
- Grounds maintenance
- Items left by the seller
- Utilities
- Insulation for new construction
- Leased property
- Homeowner's association review board
- Other

Note: Paragraph #10 (See NWMLS Form #22D Optional Clauses Addendum below) is a convenient place to list items which will be included or excluded in the sale. Another important item that might be placed in this paragraph would address e-mail transmission. NWMLS Form 21 PSA, paragraph # m, states that "e-mail transmission of any document or notice shall not be effective unless the parties to this Agreement otherwise agree in writing." This might be a great place to have all parties agree to e-mail transmission, in writing, if that is the preferred method of transmission by your clients.

**OPTIONAL CLAUSES ADDENDUM TO
PURCHASE & SALE AGREEMENT**
Continued

Seller shall provide Buyer a copy of the lease for the selected items within _____ days (5 days if not filled in) of mutual acceptance. If Buyer, in Buyer's sole discretion, does not give notice of disapproval within _____ days (5 days if not filled in) of receipt of the lease(s) or the date that the lease(s) are due, whichever is earlier, then this lease review period shall conclusively be deemed satisfied (waived) and at Closing, Buyer shall assume the lease(s) for the selected item(s) and hold Seller harmless from and against any further obligation, liability, or claim arising from the lease(s), if the lease(s) can be assumed. If Buyer gives timely notice of disapproval, then this Agreement shall terminate and the Earnest Money shall be refunded to Buyer.

8. **Homeowners' Association Review Period.** If the Property is subject to a homeowners' association or any other association, then Seller shall, at Seller's expense, provide Buyer a copy of the following documents (if available from the Association) within _____ days (10 days if not filled in) of mutual acceptance:
- a. Association rules and regulations, including, but not limited to architectural guidelines;
 - b. Association bylaws and covenants, conditions, and restrictions (CC&Rs);
 - c. Association meeting minutes from the prior two (2) years;
 - d. Association Board of Directors meeting minutes from the prior six (6) months; and
 - e. Association financial statements from the prior two (2) years and current operating budget.

If Buyer, in Buyer's sole discretion, does not give notice of disapproval within _____ days (5 days if not filled in) of receipt of the above documents or the date that the above documents are due, whichever is earlier, then this homeowners' association review period shall conclusively be deemed satisfied (waived). If Buyer gives timely notice of disapproval, then this Agreement shall terminate and the Earnest Money shall be refunded to Buyer.

9. **Homeowners' Association Transfer Fee.** If there is a transfer fee imposed by the homeowners' association or any other association (e.g. a "move-in" or "move-out" fee), the fee shall be paid by the party as provided for in the association documents. If the association documents do not provide which party pays the fee, the fee shall be paid by Buyer; Seller (Seller if not filled in).

10. **Excluded Item(s).** The following item(s), that would otherwise be included in the sale of the Property, is excluded from the sale ("Excluded Item(s)"). Seller shall repair any damage to the Property caused by the removal of the Excluded Item(s). Excluded Item(s):

11. **Home Warranty.** Buyer and Seller acknowledge that home warranty plans are available which may provide additional protection and benefits to Buyer and Seller. Buyer shall order a one-year home warranty as follows:
- a. Home warranty provider: _____
 - b. Seller shall pay up to \$ _____ (\$0.00 if not filled in) of the cost for the home warranty, together with any included options, and Buyer shall pay any balance.
 - c. Options to be included: _____ (none, if not filled in).
 - d. Other: _____

12. **Other.**

Buyer's Initials Date Buyer's Initials Date Seller's Initials Date Seller's Initials Date

Feasibility Contingency Addendum

A feasibility addendum will often accompany an offer to purchase vacant land or commercial property. The buyer will be given a certain number of days to perform an independent study of the property which might include:

- Building or development moratoria
- Flood zones
- Wetlands and shorelands
- Roads
- Water
- Sewer
- Other utilities
- Capacity charges
- Assessments

Homeowner's (Hazard) Insurance Addendum

Homeowner's (hazard) insurance is important for almost all residential properties. Not only is it good risk management for the homeowner, but most lenders require it as a means of reducing their own risk.

There can be times when a buyer may be refused insurance on a particular property. This may be due to an unsatisfactory CLUE report. CLUE is an acronym for Comprehensive Loss Underwriting Exchange. It is a compilation of all insurance claims. The CLUE may be a report on a particular person or on a property.

Incorporating an insurance contingency into a PSA can protect your buyer. This can be done through such forms as previously shown on NWMLS Form 22A, paragraph # 10, or on an addendum specifically designed for this purpose

An Addendum to Address the Personal Property or Fixtures Included in the Sale

All personal property and trade fixtures which are included in the sale should be clearly specified in the PSA. There are a number of ways to do this:

- Some appliances are addressed on NWMLS Form 21, paragraph #5
- Use of a separate addendum
- NWMLS Form 22D, paragraph #10 (Other) has space to itemize personal property

Possession Addendum (If Possession Is Not at the Time of Closing)

In many circumstances, the date of possession is not the closing date. Usually this is because the seller will need to close their current home and receive the net proceeds from this home before they can purchase their next home. Even in an ideal situation where both homes close concurrently, the homeowner will need time to move to the next home.

There are also circumstances where the seller will need extra time to move for various other reasons.

An addendum should be drawn up and attached to the PSA which addresses all of the following:

- Length of the possession period by the seller
- Which party will insure the home during the “possession” period (this is usually the buyer through their homeowner’s insurance)
- What charge, if any, will be paid by the seller for this “possession” period

Note: Insurance liability is important. All parties should make sure that the property is insured during this time.

Another situation may arise where a buyer may want to take possession prior to closing, especially on a vacant home.

This situation should be avoided if at all possible for the following reasons:

- There’s always a chance that a buyer may move into a property, discover some unknown undesirable fact, and not want to proceed with the transaction.
- The insurance liability is extremely high. Example: should one of the buyer’s movers injure themselves, the seller may have to bear the liability.
- Should the transaction fail to close, the buyer already has possession of the property. Should the buyer refuse to leave, the seller may be forced to proceed with an eviction process.

Note: Before writing an addendum for early possession, consult with your manager first. There is also a risk of liability for you as a licensee and for your brokerage.

When a Listing Agreement is Terminated

Ways in Which a Listing Can be Terminated

A listing can be terminated in many ways. The following are some that are worth exploring.

Mutual Consent of Both Parties

In this situation, both parties agree to terminate the listing. The listing may be terminated with or without conditions.

Conditional Release of Listing

The Conditional Release of Listing is another common contract that residential agents use. In essence, it rescinds the listing agreement with the condition that the seller will still pay the broker a commission if a future buyer purchases the property who identified the property through means of the broker's advertising or showing within six months.

Note: A licensee cannot cancel a listing without a designated broker's signature and the seller's signature

Release of Listing That is Unconditional

In a situation where both the brokerage and the seller agree to unconditionally release the listing, Form 19, Status Change Input Sheet for All Property Types.

Death of a Seller

In the event of the death of the seller during a listing agreement, the agreement is cancelled. If there was more than one seller, the surviving seller would be required to enter into a new listing agreement with the broker.

Expiration of a Listing

At the end of the term of the listing, called the expiration date, the listing expires and is in effect cancelled.

Note: There is some verbiage in a listing agreement which could cause a commission to be paid after the expiration date.

Remedies for a Breach of a Listing

When a party to the contract fails to perform as promised in the contract, this is known as breach. If a seller cancels a listing agreement with a brokerage prior to the expiration of the listing, the seller may be in breach of the contract. The brokerage may be able to sue for damages and/or a commission.

There are also circumstances where a broker may be entitled to a commission after the expiration date:

Included within the verbiage of the statewide listing agreement is a clause which allows for the payment of commission within six month after the listing expires if a purchaser whose attention it was brought to through the efforts of the broker purchases the property. Furthermore, there is a clause which protects the broker if the seller cancels the listing agreement without legal cause.

Included in paragraph #3 of the listing forms 1A and 1B:

“Further, if Seller shall, within six months after the expiration of this Agreement, sell the Property to any person to whose attention it was brought through the signs, advertising or other action of Broker, or on information secured directly or indirectly from or through Broker, during the term of this Agreement, Seller will pay Broker the above [agreed upon] commission. Provided, that if a commission is paid to a member of MLS or a cooperating MLS in conjunction with a sale, the amount of commission payable to Broker shall be limited to the amount of commission which would have been payable pursuant to this Agreement less any commission so paid to another member of the MLS. Provided further, that if Seller cancels this Agreement without legal cause, Seller may be liable for damages incurred by Broker as a result of cancellation, regardless of whether Seller pays a commission to another MLS member.

All listings are owned by the brokerage and not the licensee. If a listing licensee would like to terminate a listing, he or she should go to the managing broker and explain the circumstances and reasons.

The brokerage has the option to assign the listing to another agent or cancel the listing (with the seller’s permission).”

What Happens to Current Listing Agreements under Specific Situations

Death of the designated broker – The agreement was between the brokerage and the seller. With the death of the designated broker, the agreement ceases to exist if the brokerage was a sole proprietorship. However, if the brokerage was a corporation or a

limited liability company (LLC), the corporation may be able to appoint a new designated broker and may have some claim to the listings.

Firm goes out of business – The listing agreements are terminated.

Designated broker loses their license in a disciplinary action and listing broker transfers to a different real estate firm – If the designated broker loses their license, there is a possibility that the state could appoint a temporary designated broker. In this situation, the listings would remain with the brokerage. Listings are never the property of a licensee and if the licensee transfers to another brokerage, he or she cannot take the listings to the new brokerage.

Potential Situations Where the Principal (Buyer or Seller) Would Default on a Purchase and Sale Contract

Let's first take a look at some legitimate reasons why a principal may want to terminate a PSA:

- Contingencies in the contract were not met
- Default of the other party
- Death of the buyer
- A voidable contract
- A void contract

Contingencies in the Contract Were Not Met

A contingency is a provision in a real estate contract that specifies the contract would cease to exist upon the occurrence or non-occurrence of a certain event. A contingency should be clearly written, concise, and have a definite time limit. If a contingency in a contract is not met, then the party requesting the contingency can legally terminate the contract.

Inspection Addendum

An inspection addendum usually covers an inspection of the property and deals with structural issues, some pest infestations, under-ground residential heating oil tanks, and on-site sewage disposal systems.

As a result of this inspection, the buyer can approve of the inspection, terminate the transaction, request additional inspections, or ask the seller to perform repairs or modifications. The seller may agree to perform the requested repairs/modifications or refuse. The buyer retains the right to proceed or terminate the contract.

Feasibility Contingency Addendum

A feasibility addendum will often accompany an offer to purchase vacant land or commercial property. The buyer will be given a certain number of days to perform an independent study of the property which might include:

- Building or development moratoria
- Flood zones
- Wetlands and shorelands
- Roads
- Water
- Sewer
- Other utilities
- Capacity charges
- Assessments

If the feasibility study is not favorable, the buyer would have the right to terminate according to the terms of the contract.

Default of the Other Party

If one of the parties defaults on the contract, the other party may have grounds to terminate the contract.

Example: The buyers have a structural inspection contingency on a property. They have the inspection done and their response is as follows.

The buyers approve of the structural inspection, with the following exceptions: Seller to repair, at seller's expense, the following:

- Replace hot water heater
- Fix leaking faucet in master bath
- Service the furnace
- Repair/replace broken light at outdoor doorstep

All work is to be performed within five days of the closing date and must meet with buyers' approval.

Four days before closing, the buyers do a walk through and discover that none of the agreed work had been performed as agreed. The buyers may be able to terminate the contract.

Death of the Buyer

The death of the buyer may be grounds for canceling the contract.

A Voidable contract

Either party may terminate a contract, if the contract is voidable.

Example: Both the buyer and seller signed a PSA. The contract did not have a full legal description attached to it. Either the buyer or the seller could terminate the agreement

A Void contract

A void contract is not legal and is unenforceable. If any of the following elements are missing, the contract is terminated:

Mutual agreement: Each and every party involved in the contract must agree to and accept the contract and its components. All parties must recognize and acknowledge that an agreement has been made and duly accepted.

Consideration: A contract must be mutually beneficial and all parties must recognize and accept the benefits from the contract. These benefits can include money, transfer of ownership, transfer of rights, exchange of services, or anything of value.

Legally competent parties: In the United States, a person or entity (such as a business, trust, or corporation) must be competent and at least 18 years old to enter into a contract. If the party is a business, the person representing the business must also be legally competent and have the authority to act for the business.

Lawful objective: A legal contract cannot require any party to knowingly break the law. If so, the contract is usually void.

Written contract: The Statute of Frauds is a Washington State law which requires that all real estate contracts be in writing.

Note: There are also situations where a principal to a contract may want to terminate a contract without a legitimate reason. This is usually referred to as a breach of contract. Some typical reasons might include:

- *Loss of a job*
- *Sudden illness*
- *Divorce*
- *A lawsuit or judgment*

When the Licensee is Liable or Potentially Liable from a Poorly Constructed/Crafted Contract and What Possible Disciplinary Procedures May Result

Licensees must use care when drawing up contracts as they could become liable for poorly constructed/crafted agreements. A lawsuit from a client or a disciplinary action from the director could result. Below is a detailed discussion of both.

Introduction to Torts

Tort law is a group of laws that addresses, and provides remedies for, civil wrongs not arising out of contractual obligations. A person who suffers damages may be able to use tort law to receive compensation from someone who is legally responsible for the injuries. In criminal law, in which the offense is against the state, the state becomes the plaintiff. In tort civil law, the offense is against a person and that person is the plaintiff. Torts cover accidents and acts that are intentional.

Negligence

Negligence – Negligence is defined as the failure to use ordinary or standard care. Let's look at a case study:

Case Study

The buyers wanted to purchase a vintage older home which was on a septic system. The buyers' agent did not recommend that the buyers have a structural inspection or an inspection of the septic system. After closing, the buyers moved in, they found massive dry rot under the eaves of the home and found that the drain field for the septic system was defective and that sewage was seeping up under the back lawn. The broker was sued for negligence for not recommending a structural inspection.

Unintentional Misrepresentation

Example: The buyer's agent stated that an in-ground pool could be built in the backyard of a home and that the home would be perfect for this family who had a child who was training to be an Olympic swimmer. After the buyers moved in, they found that there were underground utilities in the backyard and a pool could not be built there. The buyers sued their agent for unintentional misrepresentation, and then sued the broker for unintentional misrepresentation as well.

Negligent Misrepresentation

Negligent misrepresentation is a failure to disclose a material fact out of ignorance when the agent should have known otherwise. This is where the agent makes a statement without any reasonable grounds to believe that it is true. Here's an example:

Due to a recent earthquake, many homes in a particular neighborhood suffered major structural damages. The two homes next door to the subject's property were still being repaired and each still had scaffolding around them. While the sellers did not disclose this fact on their seller's disclosure statement, they did tell their agent about the earthquake. The broker failed to advise the buyers of the potential problems with the structural integrity of the home and said that he thought the structure was just fine. The broker was found liable for failing to disclose the potential problems.

Intentional Misrepresentation

Intentional misrepresentation is defined as "knowingly making a false statement about a material fact." It is also known as fraud. Claims of intentional misrepresentation would include:

- Knowledge by the agent that the information was false
- Damage to a consumer who relied on this false information

Example: The listing broker knew that there were external factors which influenced the habitability of a home. The seller had discussed the fact that because their home backed up to a supermarket, semi-trucks making deliveries at 4 am in the morning were a noise nuisance. The broker represented to the buyers that this home was in a quiet neighborhood. After the buyers moved in, they were awakened by the noise of the trucks and sued the broker for intentional misrepresentation.

Intentional Concealment

Intentional concealment is defined as "knowingly failing to disclose a material fact."

Claims of intentional concealment may include some of the following circumstances:

- A material fact was concealed or suppressed
- The fact was concealed with an intention to defraud
- An agent has the duty to deal fairly with all parties even if he or she does not represent them
- The consumer was damaged as a result of the concealment

Example: The listing broker had seen a burned area approximately six feet in diameter on the hardwood flooring of the porch. An oil lamp had burned through the hardwood and part of the sub-flooring. The broker placed a large fluffy area rug over the area to conceal the defect. When the new buyers moved in, they discovered that the

sub-flooring, which was particle board, had rotted from exposure and moisture. The buyers sued the broker for intentional concealment.

Note on Vicarious Liability

Licensees are agents for their designated broker. Under some circumstances, a designated broker may be liable for the wrongful actions of a licensee under his or her supervision. Vicarious liability is defined as “a person that is responsible or liable for the actions of another person.”

The theory behind vicarious liability is that the designated broker should not benefit from the fraudulence or misrepresentations of their licensees.

Major Grounds for Disciplinary Actions Against Licensees

[RCW 18.85.361](#) deals with the grounds for disciplinary action

Disciplinary action—Grounds.

In addition to the unprofessional conduct described in RCW [18.235.130](#), the director may take disciplinary action against any person engaged in the business or acting in the capacity of a real estate broker, managing broker, designated broker, or real estate firm, regardless of whether the transaction was for the person's own account or in a capacity as broker, managing broker, designated broker, or real estate firm, and may impose any of the sanctions and fines specified in RCW [18.235.110](#) for any holder or applicant who is guilty of:

(1) Violating any of the provisions of this chapter or any lawful rules made by the director pursuant thereto or violating a provision of chapter [64.36](#), 19.105, or [18.235](#) RCW or RCW [18.86.030](#) or the rules adopted under those chapters or section;

(2) Making, printing, publishing, distributing, or causing, authorizing, or knowingly permitting the making, printing, publication or distribution of false statements, descriptions or promises of such character as to reasonably induce any person to act thereon, if the statements, descriptions, or promises purport to be made or to be performed by either the licensee or his or her principal and the licensee then knew or, by the exercise of reasonable care and inquiry, could have known, of the falsity of the statements, descriptions or promises;

(3) Knowingly committing, or being a party to, any material fraud, misrepresentation, concealment, conspiracy, collusion, trick, scheme, or device whereby any other person lawfully relies upon the word, representation or conduct of the licensee;

(4) Accepting the services of, or continuing in a representative capacity, any broker or managing broker who has not been granted a license, or after his or her license has been revoked or during a suspension thereof;

(5) Conversion of any money, contract, deed, note, mortgage, or abstract or other evidence of title, to the person's own use or to the use of that person's principal or of any other person, when delivered in trust or on condition, in violation of the trust or before the happening of the condition; and failure to return any money or contract, deed, note, mortgage, abstract, or other evidence of title within thirty days after the owner thereof is entitled thereto, and makes demand therefor, is prima facie evidence of such conversion;

(6) Failing, upon demand, to disclose any information within the person's knowledge, or to produce any document, book, or record in the person's possession for

inspection by the director or the director's authorized representatives acting by authority of law;

(7) Continuing to sell any real estate, or operating according to a plan of selling, whereby the interests of the public are endangered, after the director has, by order in writing, stated objections thereto;

(8) Advertising in any manner without including the real estate firm's name or assumed name as licensed in a clear and conspicuous manner in the advertisement; except, that real estate brokers, managing brokers, or firms advertising their personally owned real property must only disclose that they hold a real estate license;

9) Accepting other than cash or its equivalent as earnest money unless that fact is communicated to the owner before the owner's acceptance of the offer to purchase, and such fact is shown in the purchase and sale agreement;

(10) Charging or accepting compensation from more than one party in any one transaction without first making full disclosure in writing of all the facts to all the parties interested in the transaction;

(11) Accepting, taking, or charging any undisclosed commission, rebate, or direct profit on expenditures made for the principal;

(12) Accepting employment or compensation for appraisal of real property contingent upon reporting a predetermined value;

(13) Issuing a report on any real property in which the broker, managing broker, or real estate firm has an interest unless that interest is clearly stated in the report;

(14) Misrepresentation of membership in any state or national real estate association;

(15) Discrimination against any person in hiring or in real estate brokerage service activity, on the basis of any of the provisions of any local, county, state, or federal antidiscrimination law;

(16) Failing to keep an escrow or trustee account of funds deposited relating to a real estate transaction, for a period of three years, showing to whom paid, and other pertinent information as the director may require, such records to be available to the director, or the director's representatives, on demand, or upon written notice given to the bank;

(17) In the case of a firm and its designated broker, failing to preserve records relating to any real estate transaction for three years following the submission of the records to the firm;

(18) Failing to furnish a copy of any listing, sale, lease, or other contract relevant to a real estate transaction to all signatories thereof within a reasonable time following execution;

(19) In the case of a broker or managing broker, acceptance of a commission or any valuable consideration for the performance of any acts specified in this chapter,

from any person, except the licensed real estate firm with whom the broker or managing broker is licensed;

(20) To direct any transaction involving his or her principal, to any lending institution for financing or to any escrow company, in expectation of receiving a kickback or rebate therefrom, without first disclosing the expectation to his or her principal;

(21) Buying, selling, or leasing directly, or through a third party, any interest in real property without disclosing in writing that the person is a real estate licensee;

(22) In the case of real estate firms, and managing and designated brokers, failing to exercise adequate supervision over the activities of their brokers and managing brokers within the scope of this chapter;

(23) Any conduct in a real estate transaction which demonstrates bad faith, dishonesty, untrustworthiness, or incompetence;

(24) Acting as a vehicle dealer, as defined in RCW [46.70.011](#), without having a license to do so; or

(25) Failing to ensure that the title is transferred under chapter [46.12](#) RCW when engaging in a transaction involving a mobile or manufactured home as a broker, managing or designated broker, or firm.

Properly Constructed PSA with Appropriate Addenda (to Address Needed Contingencies) Can Reduce the Risk of Default

Each real estate transaction is unique in its own way. There are so many variables to each transaction. Attaching addenda to a Purchase and Sale Agreement (PSA) can assist in tailoring your offer to meet the needs of your clients. Let's look at some further examples where you may want to use contingencies attached to contracts to reduce the risk of default by your client:

- Your client will not get the gift money from his parents for the purchase of his home for another five days and is signing a PSA today. He doesn't have the funds for earnest money (Promissory Note Addendum)
- Your client is making an offer on a home contingent upon selling her current residence (Contingent Upon the Sale of a Residence Addendum)
- Your clients are purchasing a home in Snohomish County (Smoke Detector Addendum required in this county)
- You are representing the buyer and you suspect that the seller may not have been paying their utility bills (Utility Addendum)
- You are representing the buyer or the seller who is a foreign person (FIRPTA Addendum)
- Your client is purchasing a vacation home in San Juan County (San Juan County Addendum required)

In the Event of a Default or Termination

There may be times in your real estate career where a contract may be terminated or the buyer or the seller may default on the agreement. Let's look at different scenarios and what, as a licensee, your obligations to protect your client might be:

Case Study: Implications to a Contract Because of a Contingency Notice not Given in a Timely Manner

In this case, a contingency in the contract was not met and the buyer has a legal excuse to terminate. As a buyer's broker or seller's broker, you may want to be sure that the notice of contingency that was not met was given in a timely manner.

As an example, the buyer had a structural contingency attached to the contract which stated that the buyer, at the buyer's expense, would perform a structural inspection on a property within 10 days of mutual acceptance, and that within that 10-day time frame would notify the seller if the structural inspection was accepted, rejected, or conditionally approved with the seller agreeing to do some repairs. The structural inspection addendum further stated that if the buyer did not notify the seller within the 10-day time frame that the buyer's silence would construe acceptance. The buyer performed the structural inspection on day 9, but did not submit the notice of conditional approval to the seller until day 11. On the notice, the buyer asked the seller to replace the roof. Because of the untimely notice from the buyer, his or her silence construed acceptance and the buyer was obligated to the contract and the seller was not obligated to replace the roof. The buyer's broker had the obligation to ensure that the buyers knew about the importance of the timing of the notice. The seller's broker performed his obligation by informing his clients that they were under no obligation to replace the roof, because the buyer had not acted in a timely manner.

Case Study: Contingency in a Contract not met and Termination is by Mutual Agreement

There was a contingency attached to the contract that the seller would provide clear title to the buyer. Upon obtaining a preliminary title report, there was a judgment attached to the property for \$95,000 of which the seller claims she had no prior knowledge. The seller wanted to rescind the contract and the buyer agreed. It is the obligation of both the buyer's broker and the seller's broker to make sure that the rescission agreement is signed by both parties and that the earnest money is returned to the buyer.

Case Study: Buyer Defaults on a PSA Without Legal Excuse

The buyer claims that he just “changed his mind” and does not want to go through with the PSA contract after all contingencies were already met. It is the buyer’s broker’s responsibility to inform her client that he may want to seek legal advice as to the implications of breaching the contract (examples might be forfeiture of earnest money as liquidated damages, specific performance, damages, etc.). The seller’s broker may want to do the same and should the seller wish to seek legal counsel, provide documentation to the seller’s attorney. The seller’s broker may also want to accompany the sellers to the meeting with their attorney.

Note: The seller’s broker may want to accompany their clients to a meeting with legal counsel, but the seller’s broker should in no way seek legal advice for their client by meeting with an attorney without their client being present. The seller’s agent should not put themselves in the position of interpreting legal advice for their client.

Case Study

Bob, a broker with XYZ Realty Investment LLC, has a listing with the Smiths. Janet, a broker with ABC Investments, procures a buyer. Both of the sellers have had a job transfer and any delay in closing a transaction would be very costly to them. Because of this, the listing broker asked the buyer’s broker for the following from her clients in an attempt to protect his clients from default:

- A large earnest money deposit in the event of default by the buyer
- A letter or prequalification and not just pre approval from the buyer’s lender
- A clause agreed to by the buyer and the seller which would cost the buyer \$100 for each day that the transaction failed to close after the mutually agreed upon date.

It would be the duty of the seller’s broker to explain the implications of each request to the sellers. It would be the duty of the buyer’s agent to explain the implications to the buyers of agreeing to the request.

The Level of Detail to Include in a Financing Contingency Clause

Most offers made for real estate contain a financing contingency. The buyers make their offer contingent upon obtaining financing within a given time frame. It is important for all licensees to understand that they fill in the blanks of standardized pre-printed forms approved by an attorney, and not draft addenda, such as a financing contingency, themselves. When a broker drafts his or her own contingencies, it could be considered

practicing law without a law degree. A financing addendum should be as detailed as possible and the following may be included in the blanks:

- Buyer and seller
- Property address
- Type of loan such as FHA, VA, conventional, rural development (RD), etc.
- Time allowed to obtain a commitment for financing
- Seller's contribution if the loan is a FHA or RD
- Seller's contribution if the loan is a VA loan or conventional loan
- Insurance contingency for homeowner's insurance
- Consequences when an appraisal is less than the agreed upon sale price

Note: Many financing addendum have a provision where the buyers must not change the type of loan or the lender without the prior written permission of the seller.

Typical Elements of a Property Management Agreement

The Property Management Agreement details the responsibilities and powers of the property manager versus what must be approved and/or authorized by the property owner, such as fees, commissions, maintenance, and repairs.

Property Management Agreement

According to the Washington Administrative Code [WAC 308-124D-215](#) -

Management agreements and disclosures.

(1) All properties managed by the firm must be supported by a written management agreement signed by the owner and designated broker and retained. The management agreement must state at a minimum:

- (a) The firm's compensation;
- (b) The type (i.e., apartments, industrial) and number of individual units in the project or square footage (if other than residential);
- (c) Whether or not the firm is authorized to collect funds and disburse funds and for what purposes;
- (d) Authorization, if any, to hold security deposits and the manner in which security deposits may be disbursed; and
- (e) The frequency of furnishing summary statements to the owner.

(2) All properties rented or leased by the firm must be supported by a written rental or lease agreement.

(3) Each owner of property managed by the firm must be provided a summary statement as provided in the property management agreement for each property managed showing: (The designated broker is to retain a true copy of this statement.)

(a) Balance carried forward from previous summary statement.

(b) Total rent receipts.

(c) Owner contributions.

(d) Other itemized receipts.

(e) Itemization of all expenses paid.

(f) Ending balance.

(g) Number of units rented or square footage if other than residential.

(4) The firm may provide other services to owners of properties managed provided full disclosure to the owner is provided in writing of the broker's relationship with any and all persons providing such services, prior disclosure of fees charged, and permission is granted by the owner.

(5) Any amendment or modification to the property management agreement must be made in written form and signed by the owner and the designated broker and retained.

The Unique Fiscal Responsibilities Associated with Property Management

There are unique fiscal responsibilities associated with property management, such as the duty to collect rents, funds management, accounting, and monthly income statements.

Property Management

The property manager acts as a liaison between the tenant and the landlord.

The duties of a property manager may include, but are not limited to:

- Collection of rents
- Maintenance of grounds
- Repairs
- Accounting to the landlord for all monies collected and disbursed
- Interviewing and securing tenants
- Showing property
- Evicting tenants
- Scheduling of contractors such as landscapers, painters, carpet installers, pest control companies, etc.
- Paying taxes and utilities
- Making mortgage payments on the property
- Setting rent rates
- Income tax accounting

- Budgeting
- Keeping operations running smoothly
- Dealing with tenant complaints and tenant satisfaction

The property manager has a duty to the landlord to maximize his or her profits, to manage the financial accounting of the operations, and to ensure that the operations are within the constraints of the law and the lease agreements.

The property manager also has a duty to the tenant to ensure that the tenant has a safe, habitable dwelling and that the terms of the lease or rental agreement are carried out.

The Typical Provisions of Leases

In a typical residential lease, leases for apartments may have some additional provisions. These might include:

- Parking and assigned spaces
- Rules about washing vehicles in carports or on the grounds
- Times that washing machines and dryers are prohibited from running
- Number, type, and size limits of pets
- If barbeques are allowed and what type (gas versus charcoal)
- Procedures for the use of the clubhouse
- Rules for the use of the swimming pool or hot tub
- House guests and rules on their length of staying
- Rules on the disposal and recycling of garbage
- Rules for picking up mail and parcels

The Appropriate Precautions and Procedures When Using Unfamiliar or Non-Standardized Forms of Contracts

Such forms may include bank contracts for the purpose of foreclosure properties (REOs) and contracts provided by developers for new home purchases.

When selling new construction homes and bank-owned REOs, it may be typical that the builder or the bank may have their own contracts and addenda.

Note: REO is an acronym for Real Estate Owned properties (bank owned).

Many of these internal contracts and addenda may be heavily weighted in favor of the seller and may compromise the buyer. Examples of this might include:

- A requirement that the buyer obtain a loan from the seller's "preferred" lender

- Non-refundable earnest money
- A penalty clause and per day fee if the transaction fails to close on the agreed upon date
- A requirement that the buyer waive a structural inspection
- A clause that the buyer agrees to waive their right to receive a seller's property disclosure statement
- Rules that prohibit a buyer from changing the terms and conditions on the PSA or any accompanying addenda

As a licensee, you should suggest, in writing, that your client seek independent legal advice, especially when these forms are unclear. Do not assume that these "internal forms" have been reviewed by an attorney prior to the builder or bank using them. Also, do not assume that the terms contained within some addenda are compatible with a standard PSA. As we discuss in the sections on voidable contracts, if the terms of a contract conflict, then the contract could become voidable at either party's discretion.

There may be times when not dealing with new construction or REOs where you may experience the use of internal forms. Certain real estate companies may have their own internal forms that they require their licensees use with all PSAs.

Again, the safe approach is to have your buyer client seek legal counsel. If the client prefers not to seek legal advice, their forms at the least should be VERY carefully read and each term should not conflict within another term contained within the contract. Advise your clients of the implications of giving up some of their rights if they are asked to do so through these internal forms.

Note: Do not assume that all branches of a franchise have the same exact forms or addenda.

Example: ABC Realty, Elm Street branch, has a financing addendum. Clients prior to your current clients had an attorney review this form and the attorney said that it was acceptable. In the current transaction, you're dealing with ABC Realty, State Street branch. Do not assume that these addenda are identical.