SECTION TWO

CONTRACT FORMATION & NEGOTIATION

Outline:
Introduction
Fundamental Contract Principles 101
Offer & Acceptance
Requisites of an Offer
Acceptance
Submitting Offers to Seller
Due Diligence Fee & Earnest Money Deposit
Negotiations - How Binding?
Hypotheticals & Discussion

Learning Objective: Upon completing this Section, brokers should have a much better understanding of how and when enforceable contracts for the purchase or sale of property are created, the effect of oral negotiations in the offer and acceptance process, and the scope of a broker's authority when acting as an agent for a buyer or seller.

INTRODUCTION

It really is quite astonishing the number of brokers who either don't understand or have forgotten the fundamentals of offer and acceptance and contract formation! At one time they knew it, because it was taught in the broker prelicensing course and tested on the state licensing examination, and most individuals acquiring a license since 2006 had to complete a thirty hour postlicensing course devoted to contracts and closing. So is it ignorance, or merely eagerness to believe that one has successfully negotiated an agreement that leads too many brokers to prematurely announce "we have a deal" only to later learn that, actually, we don't? But having announced that the parties *have* a contract establishes certain expectations that people often begin acting in reliance upon and when they learn that the assertion, i.e., we have a contract, is in fact false, they tend to be upset, both brokers and consumers. Arguably, brokers falsely proclaiming a

contract might be guilty of misrepresentation (whether negligent or willful) or being unworthy or incompetent to act as a real estate broker, both violations of License Law [G.S. 93A-6(a)(1) & (8).]

This Section will briefly review • the essential elements of a contract, • the concepts of offer and acceptance, • what constitutes acceptance, • the effect of negotiations, whether oral, written or electronic and by whom, • the scope of an agent's authority to bind his/her principal, and • comments regarding the payment of due diligence fees and earnest money. Hopefully by the end of this section, brokers' memories will be refreshed, confusion eliminated, and misrepresentations concerning whether there is a contract significantly reduced.

FUNDAMENTAL CONTRACT PRINCIPLES 101

Terminology

The law of contracts comes to us from English common law which, literally, is hundreds of years old and very well established. A "***contract***" may be defined as *a deliberate agreement between two or more competent parties supported by legal consideration to perform or abstain from performing some act*. If the agreement meets specific legal requirements, then it will be binding on the parties and enforceable in a court of law. The person extending the offer is called the ***offeror*** and the person receiving the offer is the ***offeree*** (analogous to donor who makes the gift and the donee who receives the gift). These roles may change several times during the course of the negotiations.

Generally, contracts may be *express*, i.e., stated in words whether orally or in writing, or *implied* from the conduct of the parties indicating their intent to be bound. However, within the real estate arena, *all* ***contracts*** *for the purchase and sale of real property and most contracts to lease real property* ***must be in writing*** *to be enforceable because of* a law known as *the* ***Statute of Frauds*** that comes to us from the English common law. In North Carolina, the Statute of Frauds is found in **General Statute §22-2** which states in relevant part:

> "All contracts to sell or convey any lands ... and all other *leases* and contracts for leasing land *exceeding in duration three years from the making thereof*, shall be void unless said contract, or some memorandum or note thereof, be put in writing and signed by the party to be charged therewith, or by some other person by him thereto lawfully authorized."

While the statute states that the attempted contract is "void" if not in writing, most courts today treat the oral agreement as voidable and unenforceable, rather than void from the outset. It is this statute that renders *oral agreements* relating to the transfer of a real property interest unenforceable, and thus *virtually meaningless*, absent voluntary performance. That is, if the parties choose to voluntarily perform their oral agreement, there is nothing that prevents the property interest from being transferred; it's just that if either party refuses to do what they orally agreed to do, the non-breaching party will not be able to enforce the oral agreement in a civil action. The purpose of the Statute of Frauds (which extends to certain contracts other than just those for the transfer of real property) is to prevent perjury, forgery, dishonest conduct and false testimony regarding the subject matter of the covered contracts.

Bilateral vs. Unilateral

Lastly, contracts may be *unilateral* or *bilateral* (*"lateral"* meaning *"side"*). In a *uni*lateral contract, only one side (party) has promised to do or not do something, whereas in a *bi*lateral contract, both sides have promised to do or not do something. Most real estate contracts are bilateral, i.e., the seller agrees to sell and the buyer agrees to purchase for a stated sum, or the owner agrees to lease the property and the tenant agrees to pay periodic rent. An example of a unilateral contract is the traditional option to purchase contract, as only the owner-optionor is bound; the optionor has promised not to sell to any other person during the prospective buyer-optionee's option period, but the optionee has *not* agreed or promised to purchase the property — just to consider it. If the optionee decides to purchase the property, then s/he must affirmatively notify the optionor of that election prior to the expiration of the option period and must sign the contract to purchase at that point, creating a *bilateral* contract to purchase.

What then, is the current Standard Form 2-T, Offer to Purchase & Contract, used in most residential sales transactions? Good question. Arguably, it is still a bilateral contract as the seller has promised to sell and the buyer has promised to purchase an identified property for a determined sum by a stated date with or without various other terms and conditions. However, since January 1, 2011, the standard form grants the buyer the unilateral right to terminate the contract for any or no reason during a stated period called the "due diligence period." This feature of the contract seems in essence to more closely resemble a traditional option to purchase contract; nonetheless, a distinguishing feature between the two is that the optionee has not promised to purchase and must take affirmative action before a stated date to exercise the right to purchase by entering into a purchase contract or s/he will lose that right, whereas a buyer under the standard form *has* promised to purchase and must take affirmative action by a stated date to cancel or avoid that promise and be relieved from the obligation to purchase.

Essential Contract Elements *[Editor's note: this section should be a **review** of the elements every contract must contain. Instructors may skim this section quickly or omit, if not necessary for a particular class.]*

Any agreement between two or more parties must meet certain minimum requirements in order to be a legally valid contract. The basic essentials for *any* contract (not just those for real property) are listed below and *briefly* discussed.

<u>Essential Elements of a Contract</u>

- Mutual assent (offer and acceptance)
- Consideration (the bargained for exchange)
- Legal contractual capacity of the parties
- Lawful objective (purpose) and means of accomplishing objective
- In writing* (*for certain types of contracts only*)

Mutual Assent: While parties generally are free to include virtually any terms or conditions in any contract they enter into ("freedom of contract"), at the end of all negotiations, each and every party must agree/assent to all the terms, provisions and conditions contained within the final resulting agreement, whether oral or in writing. If in writing, each party's assent

is evidenced by his/her signature and the date s/he signs. There must be this "meeting of the minds" where all parties understand and agree to all material terms of their negotiated agreement.

As stated in the *North Carolina Real Estate Manual*, 2013-2014 edition (p.363):

> ... Mutual assent is gathered from a reasonable meaning of the words and acts of the parties and not from their unexpressed intentions or understandings. *The parties' state of mind is not the controlling factor*. One who accepts or signs an instrument which on its face is a contract is deemed to assent to all of its terms and cannot escape liability on the ground that he or she has not read it. The terms of the written agreement will control unless there is a legally recognized mistake of fact or a person has been induced to sign an instrument because of undue influence, duress, overreaching, or an unfair or deceptive trade practice. Manifestation of mutual assent is usually accomplished through an *offer* communicated to a person and that person's *acceptance* communicated back to the person who made the offer.

Consideration: "Consideration" is the "bargained for exchange" forming the basis of the parties' agreement, i.e., what am I getting out of this and what are you getting out of this? There must be some "thing of value" passing between the parties that supports their agreement, because absent an exchange of value, one party would be acting gratuitously. In a bilateral contract, the exchange of promises typically is sufficient consideration — I promise to purchase and you promise to sell. Because only one promise is made in a *uni*lateral contract, such as the traditional option to purchase, the person receiving the benefit of the promise must give the promisor literally some thing of value, typically a sum of money, in exchange for the promisor's promise to do or not do some act. Courts rarely will review the sufficiency of the consideration, but will confirm its existence.

Legal Capacity: All parties to an agreement must be legally capable of entering into a contract. Conditions that will render a person incapable of contracting include: being a minor (less than 18 years of age); or being mentally incompetent at the time of signing the contract; or being so intoxicated that one does not know what s/he is doing (viewed as akin to mental incompetence if one can't understand the nature and consequences of one's acts). Related issues that may impact capacity and whether an agreement is set aside or enforced include fraud or misrepresentation, mutual mistake of material fact, undue influence, overreaching, duress or unfair and deceptive practices, but this is beyond the scope of our present focus. Suffice it to say that the presence of any of these factors may render the contract voidable by the party who lacked capacity.

Lawful Objective: To be enforceable in a court of law, agreements must be for a legally permissible purpose, rather than illegal, and each party must be able to accomplish that purpose. If the purpose of the agreement will cause any party to commit a crime, whether misdemeanor or felony, then that agreement/contract typically will not be enforced by the courts. Similarly, a contract to sell real property where the named seller doesn't hold legal title to the property may not be enforceable as the seller had no ability to accomplish the stated objective *unless* the purported seller was under contract to purchase that property and upon acquiring title would then convey it to the named buyer (which condition should be clearly stated in the contract with that buyer).

In Writing: While written agreements tend to diminish confusion regarding each party's rights and obligations under the contract and are always recommended, only those agreements relating to subject matter covered by the Statute of Frauds *must* be in writing to be enforceable. Thus, an agreement to *sell* real property must be in writing; an agreement to *lease* a single family home *for one year* is not required to be in writing to be enforceable in a court of law, because it concludes less than three years from its making.

OFFER & ACCEPTANCE

Requisites of an "Offer"

In essence, an offer is one party volunteering to promise some act or thing, coupled with a request for something from another party that is to be the agreed exchange for the promise or its performance, namely, the consideration. The "something" may be an act, a forbearance, a promise to act, or a promise to forbear acting in a particular way. An offer must be definite and certain in its terms; the intent underlying the offer must be that it will legally bind the offeror if it is accepted. *A valid offer must be an unequivocal promise, certain in its terms, that manifests a present, serious contractual intent, and if it pertains to real property, it must be in writing to comply with the Statute of Frauds.*

Where there is no act or thing requested in exchange (consideration) to support the offer, then the offer and any resulting "contract" may be held "*illusory*." From a legal standpoint, an illusory offer is no offer at all; one has the illusion of being under contract, but the contract is unenforceable because the essential contract law element of consideration/bargained for exchange is missing. An example is a traditional option to purchase contract with no option fee paid to the owner. If the owner is receiving nothing in exchange for promising not to sell this property to any other person for the next 90 days, then why should the owner be compelled to honor that gratuitous promise?

To comply with the *Statute of Frauds*, an offer and any resulting contract for the purchase of real estate must be *in writing* and:

- identify the parties to the contract by individual legal name;
- identify the subject matter of the contract;
- contain all material terms and conditions; and
- be signed by the party to be charged with performance.

Rule A.0112 - Offer & Sales Contracts

Parties to a contract (buyer/seller; owner/lessee) need only ensure that their contract to sell/purchase real property or lease real property for more than three years satisfies the Statute of Frauds requirements enumerated above. Licensees should recall, however, that in addition to complying with state law, they are subject to Commission **Rule A.0112**. The opening paragraph of this rule states:

> (a) A broker acting as an agent in a real estate transaction shall not use a preprinted offer or sales contract form unless the form describes or expressly requires the entry of the following information ....

The rule then lists 19 matters that must be addressed. Brokers are prohibited by Rule A.0111 from drafting legal instruments for others as to do so is the unauthorized practice of law, violating both state law and Commission rule and for which the broker could be disciplined. Thus, the compromise years ago with the North Carolina State Bar to devise preprinted forms that addressed most of the legal issues with relatively few blanks for real estate licensees to complete on behalf of a consumer *as instructed/directed by the consumer*. As a result, the Joint Forms Task Force created standard form offers to purchase and contract for use in residential (Form 2-T) and commercial (Form 510) transactions which forms incorporate all of the required Rule A.0112 information and address many additional issues.

Once an offer is prepared, *a licensee "...shall* ***immediately, but in no event later than five days from the date of execution deliver*** *to the parties thereto copies of any required ... contract, offer, lease or option affecting real property....*" pursuant to **REC Rule A.0106**. A licensee is also required to retain copies of all offers for three years under Rule A.0108. Thus, once an offer is prepared and signed by the offeror, there should be at least three people who have a copy of the signed offer (whether a hard copy or a faxed or electronically transmitted copy), namely: the licensee preparing the offer, the offeror, and the offeree or his/her agent. If the licensee preparing the offer is the listing agent working only as a seller agent, or possibly a dual agent, with the appropriate consent, then the completed offer would be provided to the buyer and seller with the licensee retaining a copy.

Acceptance

Upon presentment of an offer, the offeree has several choices: 1) s/he may reject the offer outright; 2) s/he may accept the offer as tendered without *any* modifications (other than the addition of all offerees' signatures and the dates thereof); 3) s/he may alter or change some of the terms of the tendered offer and return it to the original offeror; or 4) s/he may neither accept nor reject the offer and engage in oral negotiations with the offeror concerning terms the offeree would consider more favorably. **UNDERSTAND** that if the initial offeree alters any term in the offer extended, then the original offer is thereby ***rejected*** as a matter of law and cannot later be revived, absent mutual agreement. The original offeree has made a ***counteroffer***, i.e., a *new* offer, thereby becoming the offeror with the original offeror becoming the offeree. Must licensees really keep this terminology straight? Doubtfully critical, so long as licensees understand that altering any term of an offer creates a new offer that automatically terminates the original offer and reverses the parties' roles each time it occurs.

Query: If an owner receives an offer that meets or exceeds the desired terms, e.g., purchase price, time frame, etc., *must* the owner accept the offer? Yes? No?

> NO. An owner virtually never is obligated to accept any offer, even when it meets or exceeds his/her advertised wants. The owner may owe the listing company a fee under the terms of the listing contract, but s/he is not obligated to accept even the most perfect offer (with the possible exception of agreements with lienholders in short sale situations). Thus brokers should rarely, if ever, tell their owners that the owner *must* accept the offer.

Once an offeree receives an offer and agrees with all of the proposed terms and all offerees sign and date the offer without making any changes (mirror image acceptance), then the parties at

that point have a valid, enforceable contract, right? *Not yet*. Why not? Because the offer in virtually all real estate transactions is requesting a reciprocal *promise* from the offeree (rather than the performance of some act), acceptance of the offer is ***not complete*** upon all offerees signing the offer.

Both under contract law and pursuant to the provisions of the standard form contract, ***acceptance is not complete until the last offeree has actually* signed *the offer and that fact is communicated to the last offeror or his/her agent***. Once the offeree's written acceptance has been *communicated* to the last offeror, **then** the parties have an enforceable contract, but until acceptance is communicated to the last offeror or his/her agent, that offeror may still withdraw his/her offer *even though it has been signed by the offeree*. The contract itself defines "***Effective Date***" as "The date that: (1) the last one of Buyer and Seller has signed or initialed this offer or the final counteroffer, if any, ***and*** *(2) such signing or initialing is communicated to the party making the offer or counteroffer*, as the case may be." [Note that all changes should be initialed by both parties to confirm each party's awareness of and consent to that modified provision.]

This reality is also expressed in the Real Estate Commission's brochure on "***Offer & Acceptance***;" in response to the question: "*Once the seller has signed my offer, does it become a contract?*" {How many brokers would say "*yes*, you're under contract!"?}

> The stated answer is: "No. It does not become a binding contract until the seller (or the seller's agent) has notified you (or your agent) that the seller has signed it. If your agent informs you that the seller has "verbally" accepted or will accept your offer but has not yet signed it, *there is no enforceable contract*." (Italics added.)

Methods of Communicating Acceptance

The offeree's signing and acceptance of the offer may be communicated to the offeror by various methods unless the offer dictates how acceptance should be communicated, in which event the offeree must utilize the specified method(s). Otherwise, after all offerees have signed the offer, the offeree or his/her/their agent may communicate the offerees' acceptance by any of the following methods:

1. *Oral communication* by telephone or in person;
2. *Personal delivery* of the signed offer or other written notice of acceptance;
3. *Via mail** (traditional US Postal Service or special delivery);
4. *Facsimile* (fax) machine or *electronic mail* (email).

In the case of facsimile or email, delivery is deemed complete upon receipt of the communication by the recipient's equipment or server, not when the recipient actually reads it. A notable exception to the "upon receipt" rule, is when notice of acceptance is mailed via post to the last offeror, in which case the "***mailbox rule***" applies. In essence, it provides that so long as the envelope was properly and legibly addressed to the recipient and adequate postage prepaid, then notice is deemed "delivered" the moment the sender relinquishes control and deposits it with the mail service. The "Effective Date" of the contract would be the date of mailing and the offeror is precluded from retracting or withdrawing the offer once notice of acceptance has been deposited with the mail service. *The mailbox rule only operates within the context of communicating notice*

of acceptance of a contract. It is becoming of less relevance, given the immediacy afforded by electronic communications.

Lastly, brokers are reminded that under both the common law of agency, the terms of their written agency agreements with the consumer, and the terms of the standard form contracts, *notice* to a party (seller, buyer, lessor, lessee) may be accomplished by communicating that notice to that party's agent.

Submitting Offers to Seller

*Under the law of agency, a seller's agent (**listing** agent or **seller's subagent**) has a duty to communicate (present) all offers on a listed property to the seller (principal) as soon as possible and to disclose to the seller all information in the agent's possession that might affect the seller's decision to accept an offer.* In addition, Real Estate **Commission Rule 21 NCAC 58A.0106** requires all licensees to "*...immediately, but in no event later than five days from the date of execution,* ***deliver*** to the parties thereto copies of any contract, offer, lease or option affecting real property." It is important to note that this Commission rule *applies to all agents involved in a transaction regardless of whom they represent or from whom they will receive compensation.*

These requirements mean very simply that a *seller's* agent (or subagent) must *immediately* ***present*** all offers to the seller and must inform the seller of any matter that might affect the seller's decision. The agent cannot withhold or delay the delivery of offers or information. Understand as well that merely telling the client what the main terms of the offer are does not in any way excuse or delay the five day delivery requirement. *A copy of the document must be delivered to the client, whether personally, by electronic transfer, postal service or other means.*

> *Example:* Sally Seller lists her property with Bob Broker with an asking price of $319,500 and authorizes him to list the property with a multiple listing service. Bob finds a prospect who is fairly interested in the property and who probably will make an offer of $315,900 after checking with his father about helping out with a downpayment. In the meantime, Zippy Smith, a competing broker who is also a member of the multiple listing service, contacts Bob Broker and delivers to him an offer to purchase the property from a third party who is willing to pay $315,500 for the property. Because Bob does not want to split the commission with Zippy, he places the offer in his desk drawer and does not tell Seller about it. Bob hopes that his prospect will come through with an offer soon and that he won't have to present the offer from Zippy's prospect. Bob's action constitutes both a violation of agency principles and of Real Estate Commission Rule A.0106.

In addition to presenting signed offers, *a seller's agent (or subagent) also* ***must promptly inform the seller of any possible offers*** *that may be forthcoming*. Such information may be extremely important to the seller.

> *Example:* X has interested Smith in purchasing a residence listed with X's firm although Smith has not signed an offer to purchase the property yet. Y of another firm phones X and informs him that he has a prospect who is very interested in purchasing, and that he will be preparing an offer with the prospect that evening. After this phone call, X hurries over to Smith's house, convinces Smith to make a formal offer to purchase the property, and promptly delivers Smith's offer to the seller without informing the seller that another

offer probably will be submitted very shortly. X has breached his agency duty to disclose all relevant information to his principal. Even oral offers or expressions of strong interest by third persons should be disclosed.

The duty of a broker to deliver offers to a seller is quite clear where the broker is the *listing* agent, but what if the broker is a *buyer's* agent, or a broker proposing to act as a seller's subagent, but without an advance agreement with the listing firm to cooperate and share in the listing firm's commission? How does the Real Estate Commission's rule on delivery of instruments apply in these circumstances?

The Commission's delivery of instruments rule imposes an absolute requirement applicable to all brokers regardless of whom they represent or who will compensate them. If a buyer's agent or a broker proposing to act as a seller's subagent has a signed offer to purchase, the broker must deliver such offer to the seller (or seller's listing agent), *even if there is no agreement with the listing agent to cooperate with the listing firm and share the listing firm's brokerage commission.* As a practical matter, this means that any agent working with a buyer who wants to cooperate with a listing firm and share the listing firm's brokerage commission should have an *advance agreement* with the listing firm regarding cooperation and commission-splitting *prior to assisting a prospective buyer with preparing an offer on a property listed with the listing firm.* Understand that once an offer has been prepared and signed by the offeror, it must be promptly delivered to the offeree *unless* the broker is working with the consumer under an oral buyer agency agreement and the consumer refuses to sign a written buyer agency agreement of any type; in this case, the broker is precluded by Rule A.0104(a) from presenting the offer because s/he is prohibited from continuing to act as a buyer agent without a *written* agreement. This is why buyer agents are advised not to draft an offer until they first have a written buyer agency agreement to avoid any conflict between Rules A.0104(a) and A.0106.

A seller's agent has no authority to reject an offer on behalf of the seller, even if the offer is clearly disadvantageous to the seller. Rather, **all offers must be presented** ***and the broker should point out the disadvantages of any given offer***. If, for example, the seller's agent is aware that the prospective buyer (offeror) may be financially unqualified, this fact should be disclosed to the seller when the offer is presented.

Concurrent Multiple Offers

Where a broker receives multiple offers on a listed property about the same time, *all offers should be presented to the seller at the same time*. The broker should not present one offer to the seller and withhold a second offer until the seller makes a decision on the first offer. In this situation, it makes no difference which offer was received first, or which offers the highest price, or which company procured the offer. It also makes no difference whether the offer has been submitted through a seller's agent or subagent or a buyer's agent.

When a seller is considering several offers, may the listing agent disclose the terms of some offers to some of the competing buyers, but not to other competing buyers? No. The Commission has maintained for years that listing brokers who are in a multiple offer situation have a duty to treat all buyers fairly, honestly and equally. This duty arises out of the common law of agency and since July 1, 2008 has been reinforced by Commission Rule A.0115 that states:

> "A broker shall not disclose the price or other material terms contained in a party's offer to purchase, sell, lease, rent, or option real property to a competing party without the express authority of the offering party."

To disclose terms of an offer to one or two buyers, but not to other competing buyers, gives the first two buyers an advantage over the others. If the seller doesn't want to accept any of the offers as presented, s/he may instruct the listing broker to notify all buyers that the seller has received multiple offers and invite each buyer to submit his/her highest and best offer, if they have not done so already, by a certain time and date when the seller will reevaluate the offers received and make a decision. The *listing broker with the seller's permission may also outline any terms the seller might favorably consider,* ***so long as*** *the information is given to all*. Note that this rule is not limited to sales transactions, but applies to ANY offers received by a broker, including offers to lease, rent, exchange or option to purchase property.

Understand as well that the mere fact that the owner has received more than one offer is **not a material fact** that the listing broker must disclose to any of the prospective buyers. *A listing broker must first obtain the owner's consent before mentioning to anyone that the owner has received or is considering more than one offer*. In a seller's market, the owner may want this information disclosed so buyers are aware that there are several people who are interested in the property. However, in a buyer's market, where there are numerous available properties that satisfy a buyer's needs, a buyer may decide not to even make an offer on a property if s/he knows another offer is pending or is coming in, as s/he does not want any competition when negotiating a purchase or lease. Rather than assume s/he may disclose that there are multiple offers, the listing broker must obtain the owner's consent to share that information and should share the same information with everyone to treat all fairly, equally, and honestly.

Multiple Contracts?

Once an owner accepts an offer and enters into a contract, it generally is not a good idea for that owner to accept a later offer if the pending contract has not been terminated, unless the second acceptance is in a back-up or qualified capacity. Thus, in the past, it was rare for an owner to have multiple *contracts* — offers, yes; contracts, no. Brokers still should not commonly encounter multiple contract situations *unless* they are involved in short sale transactions. The Commission has long maintained that a listing broker in a short sale transaction must notify the lienholder upon the seller's receipt of any offer, even if the seller already has accepted an offer that is being reviewed by the lienholder. Different lienholders have different practices; apparently some are now instructing sellers to go ahead and sign any and all offers acceptable to the seller and send them to the lienholder for its consideration and approval. *It is absolutely critical, however, that the standard Short Sale Addendum (Form 2A14-T) be attached to these offers/contracts to protect both parties*. The short sale addendum has been substantially revised and Paragraph 6 has several provisions that address "Other Offers/Additional Contracts." The underlying theory is that the seller can't sell without the lienholder's consent and the lienholder will only approve one of the many contracts and reject all others, thus protecting the owner against liability that otherwise would attach for contracting to sell the same property to multiple buyers.

Due Diligence Fee & Earnest Money Deposit

In discussing a broker's receipt of trust monies belonging to others, it should be understood that the brokerage trust accounts typically will be in the name of the company and the broker-in-charge will be held strictly accountable for oversight and management of that account. Associated brokers usually will not have access to the trust account and must be instructed how they are to handle such funds under office policy while offers are being negotiated. It is not recommended that associated agents be allowed to retain the check in the transaction file during negotiations. Further, brokers-in-charge are reminded that *Commission rules require a* ***provisional broker*** *who receives trust monies to* ***deliver all such monies*** ***<u>upon receipt</u>*** ***to their broker-in-charge****, so provisional broker do not have the option of holding and safeguarding funds*.

Due Diligence Fees and Option Fees

Due diligence fees and option monies are similar; they are payable directly to the owner of the property to provide consideration for the period of time during which the buyer may decide to terminate the contract, i.e., the due diligence period, or during which the optionee may decide to purchase the property. As mentioned earlier in the discussion of consideration and unilateral, bilateral, and illusory contracts, most legal scholars agree that some option fee or other consideration must be paid to support a traditional option contract, and many believe the same logic applies to the payment of the due diligence fee under the current Standard Form 2-T. In part to address this concern, Standard Form 2-T expressly states that if the parties agree that no due diligence fee will be paid or only a nominal sum, e.g., $25.00, then all parties

> "... expressly waive any right that they may have to deny the right to conduct Due Diligence or to assert any defense as to the enforceability of this Contract based on the absence or alleged insufficiency of any Due Diligence Fee, it being the intent of the parties to create a legally binding contract for the purchase and sale of the Property without regard to the existence or amount of any Due Diligence Fee."

Thus, *must* a buyer offer to pay a due diligence fee to the owner-seller? Not according to the terms of the standard form. Can either party argue that the lack of a due diligence fee invalidates the contract? Supposedly not, since the contract states that each party has waived or relinquished the right to use the lack of a due diligence fee as an argument to avoid the contract. How a North Carolina court will interpret that clause and assess the element of consideration remains to be seen. Standard Form 2-T states that *$x of the purchase price will be paid "...BY DUE DILIGENCE FEE made payable to Seller by the Effective Date*."

<u>Brokers Handling Due Diligence Fees</u>

How is a broker supposed to handle due diligence fees? **Rule A.0116(a)(4)** states:

> (4) A broker may accept custody of a check or other *negotiable instrument made payable to the seller* of real property as payment for an option or due diligence fee, but only for the purpose of delivering the instrument to the seller. *While the instrument is in the custody of the broker, the broker shall, according to the instructions of the buyer, either deliver it to the seller or return it to the buyer*. The broker shall safeguard the instrument and be responsible to the parties on the instrument for its safe delivery as required by this Rule. A broker shall not retain such an instrument for more than three business days after the acceptance of the option or other sales contract.

A broker may accept possession of a ***check or other negotiable instrument*** made payable to the seller and safeguard and keep it until the "Effective Date," at which point it belongs to the seller pursuant to the terms of the standard form and, with the consent of the buyer, should be delivered to the seller or listing agent within three business days of contract formation. If a broker accepts a due diligence fee in ***cash***, then the cash must immediately be deposited into the broker's trust account within three banking days of receipt and may *not* be held pending contract formation. Once in the broker's trust account, the disputed funds rule would apply in the event of a dispute, rather than the exception above that requires a broker to obey the buyer's instructions regarding delivery of non-cash due diligence fees. The due diligence fee is the seller's to keep regardless of whether the transaction closes (unless the seller breaches) and may be the only monies the seller receives if the buyer exercises the right to terminate the contract prior to the expiration of the due diligence period.

Earnest Money Deposits

Many licensees labor under the misconception that the buyer *must* offer some amount of earnest money to support the contract. As discussed earlier, historically this has not been true, in that the consideration supporting a sales contract is the seller's promise to sell and the buyer's promise to purchase. Thus, payment of earnest money has never been required, but it is generally offered to show the buyer's good faith and some indication of financial ability. Listing agents, seller agents and owners should clearly understand two matters:

1) that the buyer will be entitled to a return of the earnest money if s/he timely terminates the contract prior to the expiration of his/her due diligence period; and

2) if after the expiration of the due diligence period, the buyer breaches the contract and fails to consummate the transaction, then the amount of the due diligence fee and earnest money deposit will be the only sums the seller receives as damages for buyer's breach.

A couple of years ago the Joint Forms Task Force revised the standard residential offer and sales contract form to provide an alternative for the payment of earnest monies. The present Standard Form 2-T states that any initial earnest money payable to the named escrow agent either is delivered "... with this offer OR delivered within five (5) days of the Effective Date of this Contract ..." and that any (additional) earnest money to be paid later is to be paid by cash, or other immediately available funds such as wire transfer or official bank check with time being of the essence as to that payment. If the buyer fails to deliver any fees or deposits by the due date or if any funds tendered by buyer are dishonored, then the seller may terminate the contract if buyer fails to deliver good funds within one banking day after seller provides written notice to Buyer of the default.

<u>Brokers Handling Earnest Money</u>

How is a broker to handle earnest money? **Rule A.0116(a)(3)** provides:

(3) Earnest money or tenant security deposits paid by means *other than currency* and received by a broker in connection with a pending offer to purchase or lease shall be deposited in a trust or escrow account no later than three days following acceptance of such

offer to purchase or lease; the date of such acceptance of such offer or lease shall be set forth in the purchase or lease agreement.

The rule allows but does not *require* a broker to hold and safeguard a ***check or other negotiable instrument*** for earnest money or tenant security deposit until the parties have actually entered into a contract, at which point the mandatory three banking day clock starts to tick. Earnest money received in the form of **cash** must immediately be deposited into a broker's trust account, as the three banking day clock for cash ***always*** begins to tick upon the broker's receipt, regardless of the purpose of the payment.

If the offer states that the earnest money is submitted with the offer, then the check or payment should be *with the offer*. If the buyer doesn't want to write a check for the earnest money initially and have some broker hold and safeguard it during negotiations, then the buyer might select the other alternative, which is to pay any initial earnest money deposit within five days of the Effective Date and not even worry about writing a check until the parties are successfully under contract. Another alternative would be to pay an "(additional) earnest money" payment (which may be the initial payment) at a later specified date. In any event, *an escrow agent should never sign acknowledging receipt of earnest money or any other monies until s/he either has received something s/he can deposit or verifies wire transfer of the amount into the escrow agent's trust account*. What about a back-up contract situation or multiple contract/short sale transaction? As in all contract cases, the parties will be bound by their agreement and if and when earnest money must be paid will depend on the terms of each contract. If the parties don't want to pay any deposits until sometime well after the Effective Date, such as when the contract becomes primary, then the contract needs to say that.

Three Banking Day Rule

How do these various payment options interface with a broker's obligation to deposit earnest money within three banking days of receipt or contract formation as required by Commission Rule A.0116? A broker's three banking day clock usually commences upon the broker's *receipt* of trust monies, as one cannot deposit what one does not possess. Thus, where the earnest money check is tendered with the offer and already in the broker-escrow agent's possession, that broker may safeguard the check pending contract formation, upon which event the broker's three banking day clock begins. If, however, the contract provides that the buyer will pay the earnest money within five days of the Effective Date, then the broker-escrow agent's three banking day clock will commence upon the broker's receipt of the funds, not the Effective Date.

Example: The seller accepts and signs the buyer's offer at 10pm on Wednesday, June 26, 2013 and the listing agent faxes a copy of the signed offer to the buyer's agent at 8:30am on Thursday, June 27. Earnest money is to be paid within five days of the Effective Date. (Is the Effective Date June 26 or 27?) Buyer writes a check payable to the listing company on Sunday, June 30, and gives it to his buyer agent who delivers it to the listing agent on Tuesday, July 2.

Queries: 1) Was the earnest money timely paid by the buyer?

2) When did the listing agent's three banking days begin and what is the final date by which the check must be deposited into the broker's trust account?

NEGOTIATIONS - HOW BINDING?

Brokers all too frequently tell their principals that the principal no longer is free to accept some other offer or do some other act because *the broker*, on behalf of the principal, has negotiated an agreement with the broker representing the other side. In fact there was an article in the January/February 2013 *REALTOR* magazine titled "E-mail Could Be Binding" that discussed a Massachusetts Superior Court ruling on a preliminary issue in *Feldberg, et.al. v. Coxall*. In discussing the issue in the case, the article commented (p. 37):

> ... *attorneys* representing the buyer and seller exchanged a series of emails about the deal, the last one attaching a revised, but unsigned, offer to purchase. When the seller pulled out of the deal, the buyer sued, claiming the deal had been sealed in the last e-mail. The seller argued that nothing had been signed, as required under ... the Statute of Frauds ... and sought dismissal of the claim. [Italics added.]

The series of email negotiations in the Feldberg case were between the seller-owner's corporation (unclear whether with Mr. Coxall himself or his corporation's attorney) and the attorney/ law firm representing the purchasers. Whether an attorney has the authority to bind his client to an agreement will be influenced by what authority the client-principal has conferred, which may or may not be in writing, the rules of the State Bar, and perhaps custom and practice. *The standards governing attorneys' conduct are completely distinct from those governing real estate brokers, and attorneys' ability, if any, to obligate their principals is not precedential for brokers*.

The other interesting note about the *Feldberg* case was that the Court was ruling on an exceptionally narrow preliminary issue as to whether the continued registration of a *lis pendens* notice/order was appropriate. The Court concluded that the plaintiffs had met their burden and were entitled to the lis pendens until the case could be heard on its merits, at which time seller's motion to dismiss for failure to satisfy the Statute of Frauds would be heard and interpreted in light of the Uniform Electronic Transactions Act (UETA). The Court commented:

> ...[Defendant's] arguments about the alleged insufficiency of the parties' e-mail communications to meet the Statute of Frauds and to show an intent to be bound are substantial and may well prevail .... There is some authority treating, as open, the question whether e-mails, coupled with an unsigned draft agreement, can satisfy the UCC requirement of a signed writing, although the Court in that case found that the particular e-mails from the defendant evidenced no intent to be bound to a contract with the plaintiff. See *May Trucking Co. v. Northwest Volvo Trucks, Inc.*, 238 Or.App. 21, 241 P. 3d 727 (2010), review denied, 350 Or.App. 130, 250 P.3d 922(2011)....
>
> In truth, the Courts have not yet set forth rules of the road for "the intersection between the seventeenth-century statute of frauds and twenty-first century electronic mail." [citing *May* supra.] ... The Uniform Electronic Transaction Act is one attempt to do so. It applies "to transactions between parties each of which has agreed to conduct transactions by electronic means."

The question was unanswered in this case, as the parties apparently reached an agreement resolving their dispute prior to a trial on the merits. However, in the 2001 case of *Shattuck v.*

Klotzbach a Massachusetts trial court held that a series of email exchanges *directly between the buyers and sellers* were sufficiently definite, addressed all material terms of the purchase, and were "signed" by the typed names of each party and could constitute a legally valid and binding contract. The buyers and sellers had been negotiating via email for months concerning the purchase of a $1.8 million residence and had worked out all the details. The seller's final email mentioned having the sales contract drafted, closing as soon as possible thereafter, and concluded by saying: "I'm looking forward to closing and seeing you as the owner of 5 Main Street, the prettiest spot in Marion village." The seller ultimately refused to sign the purchase contract and the buyer sued for specific performance relying on the email communications as the written evidence of the terms of the contract. The Court held that the series of emails between the parties and the typed signature of each party satisfied the Statute of Frauds requirement that the agreement be in writing and signed by the party to be charged.

Thus, parties may bind themselves in their own email communications with others, and attorneys may be able to bind their client-principals to an agreement or contract in some instances, but what about real estate brokers?

Manecke v. Kurtz

One needn't look to Massachusetts, however, for guidance, since as recently as August 2012, the North Carolina Court of Appeals in the case of *Manecke v. Kurtz*, (COA 11-1447, 2012 NC App. LEXIS 1017) ruled upon the issue of ***whether negotiations and email communications between real estate brokers was sufficient to bind or obligate each broker's principal***. The facts of the Manecke case, as found by the Court, follow.

Facts of the Case

In 2010, Mr. Manecke listed his property for sale in Cornelius with an agent named Linda. Mr. and Mrs. Kurtz were residents of New Jersey, but were looking to purchase real property in North Carolina and had hired a broker named Tom to be their buyer agent. On August 22, 2010, Tom sent Linda an email to which was attached the then Standard Form 2-T signed by the Kurtzes offering to purchase Mr. Manecke's property for $785,000. Linda then emailed Tom a counteroffer with a $845,000 purchase price and an $8,000 repair contingency apparently signed by the seller, to which Tom replied "[The Kurtzes] are really excited about their new home and agree to the counteroffer." The next day, August 23, Tom emailed Linda a copy of the $20,000 earnest money check and informed her that Mr. Kurtz was overnighting the check and that Tom "should also have the initialed changes to the contract tomorrow."

On August 25, Linda sent Tom an email inquiring about the deposit. Tom replied that he had received it and would deliver it to Linda's office the next morning and that he should have the initialed contract by then as well. The Kurtzes called Tom on August 26 and told him they had changed their minds, that they were not going to sign the counteroffer, and that he should destroy the earnest money check. Tom then called Linda and related this information. Mr. Manecke was particularly unhappy, as he had received another offer for $850,000 that he had rejected based on his negotiations/communications with the Kurtzes. The decision does not reflect whether Mr. Manecke attempted to contact buyer #2 and revive those negotiations; what is stated is that he filed suit in November 2010 against the Kurtzes for specific performance or, alternatively, breach of contract. The Kurtzes filed a Motion for Summary Judgement which was granted.

Ruling

A Motion for Summary Judgment is appropriate when there are no genuine issues of material fact for a fact-finder, whether judge or jury, to determine; in other words, the facts are undisputed and when the law is applied to those facts, then one party is entitled to judgment as a matter of law — the granting of a judgment summarily. Basically, the defendants' argument was that they never signed or initialed the counteroffer, and thus there was no writing signed by the party to be charged as required by the Statute of Frauds. Plaintiff attempted to argue that Tom's email assertion that the buyers were "excited about their new home and agree to the counteroffer" was a sufficient writing to satisfy the Statute of Frauds and thus obligate the buyers since Tom was their agent. Plaintiff argued that there were genuine questions of material fact as to whether: A) Tom acted with actual or apparent authority, B) there was a valid contract and C) the writings were sufficient to satisfy the Statute of Frauds.

In addressing Plaintiff's arguments, the Court, citing prior case law, noted that principals are only liable on contracts made by their agent with a third party in three instances, namely: when the agent is acting within the scope of his *actual* authority or within the scope of his/her *apparent* authority, or when the principal ratifies the agent's unauthorized act. Actual authority is that authority which the agent reasonably believes s/he has and may be implied from the words and acts of the parties. However, citing a 1981 North Carolina Supreme Court case, the Court stated the general rule that "A real estate agent in North Carolina, absent special authority, *does not have the power to bind his principal in a contract to convey real property*."

In the instant case, the Kurtzes had signed NCAR Form 201, "Exclusive Right to Represent Buyer." Mr. Kurtz testified that while he and his wife had authorized Tom to negotiate a contract, they had not conveyed any permission or authority to enter into a binding contract on their behalf. Such permission should be in the written agency agreement and most likely would require a formal Power of Attorney granting the broker the authority to accept contracts in the Kurtzes' stead, which Tom acknowledged he had not been given. Thus, there was no actual authority. The Court also held that there was no apparent authority either, as Tom's emails were "... no more than notifications ..." to seller/listing agent that the defendants had agreed to the counteroffer, that Tom had received a faxed copy of the check, and that he expected to receive the initialed offer shortly. Thus, the Court concluded that the trial court had properly granted summary judgment for the defendants.

Recommended Practice

In light of the foregoing, it would appear that absent express written permission from the principal, a real estate broker in North Carolina has no authority to actually enter into contracts on behalf of his/her principal. Nevertheless, as suggested in the Realtor article, ***brokers might consider including some type of disclaimer in the email or document basically stating that the content is for discussion or negotiating purposes only and that a contract will only be created once it has been signed and accepted by all the parties***. If the communications are electronic, the disclaimer might also include a statement that *permitting the agent to communicate via email should not be construed as consent by the principal to conduct the transaction electronically*.

What is a Valid Signature?

As can be surmised from the *Shattuck* case, while the Statute of Frauds requires that agreements/contracts be signed by the party to be charged, the law no longer necessarily requires the handwritten signature of a party. Since the adoption in North Carolina of the *Uniform Electronic Transaction Act* (UETA) in 2000, electronic signatures may be sufficient **if** the parties have agreed to conduct their transaction electronically. State law defines an "***electronic signature***" as "*an electronic sound, symbol or process attached to, or logically associated with, a record and executed or adopted by a person with the intent to sign the record*." (G.S. §66-312(9).)

More simply, an e-signature is any method that indicates that the person who claims to have written the message is actually the author and that the message received is in fact the one sent. Merely typing one's name at the end of an email constitutes a valid signature. Nonetheless, because anyone may type anyone's name, a *prudent brokerage practice is to require encrypted digital signatures*. This practice adds a security feature that helps verify that the person signing is who s/he claims to be and not an imposter just signing that person's name, although signatures are not required to be encrypted to be valid and binding.

HYPOTHETICALS & DISCUSSION

With the foregoing background, let us now consider different fact situations and apply the principles reviewed herein to the facts presented. The answers will be discussed on the following pages after hypothetical #3.

Case #1:

Buyer agent physically delivers an offer on behalf of his buyer client to the listing agent along with a $300 due diligence fee check payable to the seller and a $2000 earnest money check payable to the listing company. Buyer agent provides no other instructions to the listing agent. The listing agent reviews the offer and faxes it to her seller who has already relocated to Colorado for employment purposes. Believing the seller will view the offer favorably, the listing agent deposits the earnest money check into her trust account.

Two days later, buyer contacts his broker to learn the status of the pending offer and to inform his broker that he's found another property he likes better. Buyer agent telephones the listing agent and notifies her that the buyer has withdrawn his offer and would like his checks for the due diligence fee and earnest money back please.

1. May buyer withdraw his offer?

2. What if the seller had signed the offer without making any changes and had faxed it back to her listing broker?

3. May the listing broker refund the earnest money 48 hours after deposit? Did the listing broker violate the Commission's trust account rules?

Case #2:

Same facts as first paragraph in #1 above; however, ten minutes before the buyer contacts his agent 2 days later, the buyer agent receives a phone call from the listing agent informing him that the sellers have accepted the buyer's offer and the parties are under contract. Buyer agent

asks "has everyone *signed*?" The listing agent says yes and that she will fax the buyer agent a copy of the contract. No sooner does the buyer agent conclude the conversation with the listing agent, when he receives a call from the buyer inquiring about the status of the offer because the buyer has found a different property.

1. May the buyer withdraw his offer at this point? Why or why not?

2. What if buyer rushes to listing agent's office and demands the return of his due diligence fee check which the listing agent was on the verge of mailing to the seller. What should the listing agent do?

3. What if the buyer demands the return of the earnest money check?

4. What if the listing agent, when asked whether everyone had signed, had replied "Well, yes, we've already accepted and they're on their way into the office now to sign the papers." Would that affect any of the foregoing answers?

Case #3:

A new broker-in-charge is presented with the following situation. One of his listing agents received an offer emailed from a buyer agent to which the listing agent immediately responded "we've accepted your offer." The listing agent forwarded the offer to his sellers for their consideration and discussion. The sellers instructed their agent to inquire whether the buyer would be open to a few changes in the proposed terms. The listing agent and buyer agent had a series of conversations, some by telephone and others by email, and believed that they had finally negotiated terms of an agreement that would be acceptable to both parties. When the listing agent contacted the sellers, they informed him that they had received another offer for $30,000 more than offer #1 and they were inclined to accept it. When the listing broker told buyer agent #1 that the sellers had received a more favorable offer, the buyer agent vehemently insisted that they could not, as the owners were already under contract with his buyer client based on the brokers' conversations and emails.

Initially, the broker-in-charge and listing broker decided to resolve the situation by telling their sellers that they could accept Offer #2 only in a back-up capacity, because they were under contract with buyer #1.

1. Did the brokers correctly assess the sellers' situation? What is the single most important question one must ask to determine the answer?

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Discussion of the foregoing fact situations continues on the following pages. Do NOT read the answers until you've considered the facts and arrived at your own conclusions.

Discussion

Case #1

1) *May the buyer withdraw his offer?*

Yes, because neither the buyer nor his buyer agent have been notified by the seller or listing agent that the seller has accepted.

2) *What if the seller had signed the offer without making any changes and had faxed it back to her listing broker?*

Even under this scenario, the buyer *could still withdraw his offer* because neither he nor his agent were notified of the seller's acceptance prior to them telling the listing agent of buyer's decision. The last offeror virtually always has the right to withdraw or retract an offer so long as s/he communicates the withdrawal to the offeree or the offeree's agent *before* the offeree notifies the offeror that they have accepted the offer by signing it. The seller returning the signed offer to her agent does not constitute notice to the buyer or his agent. Had the seller faxed or emailed copies of the signed offer to both her listing agent and the buyer's agent (assuming facsimile and email are authorized means of communicating notices pursuant to the final page of the parties' contract), then the buyer would not have been able to withdraw the offer, even if neither he nor his agent had yet retrieved the fax or email, so long as it had been received by buyer broker's equipment or server.

3) *May the listing broker refund the earnest money 48 hours after deposit? Did the listing agent violate the Commission's trust account rules?*

The listing agent did *not* violate any Commission rule; since she had not received any instructions from the buyer or buyer agent regarding either deposit/fee, she was free to apply her own judgment. Recall, Rule A.0116(a)(3) *allows* a broker-escrow agent to hold a non-cash earnest money deposit pending contract formation for exactly this reason, *but it does not* ***require*** *the broker to wait until a contract is successfully negotiated*.

It would **not** be prudent for the broker to refund the earnest money upon notice that the buyer has retracted the offer, since she only deposited the check into the brokerage trust account two days earlier. Obviously the broker has the physical ability to write a check and refund the deposit, but until the broker knows that the buyer's check has been honored, she should not refund monies until she can verify that the funds actually were deposited into the broker's trust account. Otherwise, she runs the risk of refunding the deposit, only to learn that the buyer's original check was dishonored, leaving her with a trust account shortage.

Case #2

1) *May the buyer withdraw his offer at this point (following listing agent's telephone call to buyer agent)?*

No, the buyer's right to withdraw or retract his offer only exists until the point that the buyer or his agent receives notice of the seller's acceptance. The moment that the buyer agent was notified of seller's written acceptance, the buyer's right to withdraw the offer was extinguished.

2) *What must the listing agent do if the buyer rushes to the listing agent's office and demands the return of the check for the due diligence fee?*

So long as a due diligence fee check or other negotiable instrument is in the possession of any broker, the broker is to obey the buyer's directives. Thus, even though the buyer and seller are now under contract and the seller is legally entitled to the due diligence fee, the listing agent nonetheless is supposed to *return the buyer's original check or negotiable instrument to the buyer*. ***Really***? **Yes.** Isn't the buyer in breach of contract? Yes. Could the seller sue the buyer for the amount of the due diligence fee? Yes, and most likely claim their court costs and a portion of the seller's attorney fees, if any. Nonetheless, the broker need not be involved in the dispute of right and wrong; the broker merely needs to follow the buyer's directive so long as the check or negotiable instrument for the due diligence fee is in a broker's possession.

Understand that if a broker accepts *cash* for a due diligence fee then that cash must be deposited immediately into the broker's trust account and once in a broker's trust account, the disputed funds rule applies, rather than the exception in Rule A.0116(a)(4), as there is no piece of paper (i.e., check) to merely hand back to the buyer.

3) *What if the buyer demands the return of the earnest money check?*

The broker is *not* obligated to return the earnest money and in fact should not, as the parties are legally under contract and the check is already in the broker-escrow agent's possession, so the three banking day clock starts ticking immediately. The exception discussed in #2 above is limited only to checks for due diligence fees or option fees.

4) *What if the listing agent, when asked whether everyone had signed, had replied "Well, yes, they've already accepted and they're on their way into the office now to sign the papers." Would that affect any of the foregoing answers?*

Yes – it changes all of the last three answers, as the situation is identical to Case #1. There is no enforceable contract at the time the buyer notifies his agent that he wants to withdraw his offer because the sellers have not yet signed the offer and may still change their minds. Notice of alleged acceptance prior to actual signatures from/by all necessary parties negates the purported acceptance because it has not yet occurred. Notice of acceptance must ***follow*** signing of the offer by the last party.

THE FIRST QUESTION TO ASK when told "we have a deal" or something similar SHOULD BE "HAS EVERYBODY SIGNED?" If the answer is "not yet," then we DON'T have a deal!

How might the buyer agent assist in this situation if in fact the sellers had signed and there was a valid contract at the time the listing agent telephoned the buyer agent? The buyer agent may wish to educate his buyer-consumer to the reality that the buyer does appear to be under contract and the seller thus is entitled to the due diligence fee and could sue the buyer for the amount, plus additional costs that only make it more expensive for the buyer. If the buyer doesn't want to purchase the property, he still has the right to terminate the contract so long as his due diligence period hasn't expired. Thus, the buyer should be encouraged to allow the buyer agent to return the due diligence fee check to the listing agent to send to the seller, along with a notice informing the listing agent that the buyer is exercising his right to terminate the contract. Buyer

no longer is obligated to purchase, seller has the due diligence fee to which she is entitled, and the buyer's earnest money deposit will be refunded to him.

Case #3

Now that brokers are aware of the holding in the *Manecke* case previously discussed, it should be easier to answer the question in Case #3, namely, did the brokers correctly advise their seller-clients that they could only accept offer #2 as a back-up? The answer is, *it depends*. What is the one critical question that must be asked before one can definitively answer the question? It is, did all the sellers ever sign offer #1? The broker-in-charge wasn't sure of the answer to that question. **Understand** that until one knows the answer to that question, one cannot say whether the advice was correct or incorrect. If the sellers never actually signed offer #1, even if they had said they would, then it would seem that they were at liberty to accept offer #2 outright, and the listing brokers would have advised the sellers incorrectly. If the sellers had in fact signed offer #1 and that fact had been communicated to the buyer's agent, then the listing brokers correctly advised their sellers that they could only accept offer #2 in a back-up position.

The fact that the listing broker acknowledged receipt of the initial email with the attached offer by stating "We've accepted your offer" is not controlling, unless the sellers had in fact already signed the offer, which is unlikely within minutes of its receipt. The listing broker clearly meant to say that the offer had been *received*, rather than accepted; yet another example, however, of how words have meaning and should be chosen carefully.