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Purchase and sale of real estate - Part 2: An intro. to causes of action - by Michael Brangwynne

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This is the ninth article in a series on the circumstances that can give rise to a civil lawsuit. Earlier articles in the series can be found on Fletcher Tilton's website under ARTICLES and on the NEREJ website.

Introduction: In the previous installment, we looked at the requirements for forming a contract for the sale of real estate. Under certain circumstances, an executed initial Offer to Purchase will satisfy all of those requirements and will be binding and enforceable. Once a subsequent Purchase and Sale Agreement has been executed, there is usually no longer any doubt that the parties have entered into a contractual agreement that gives rise to legal rights and obligations. What if one party fails to fulfill their part of the deal – or, in contract terms, fails to “perform”?

Excuse of Performance Compared to Breach

First, we must distinguish excuse of performance and breach. Under a contract for the purchase of real estate, there may be certain contingencies that must occur before a party is required to perform. For example, a purchaser may agree to buy a single-family residence for \$750,000, but this will be contingent upon the purchaser obtaining approval for a 30-year fixed mortgage loan prior to closing. If the purchaser's financing falls through, he will be excused from performance – i.e., he will not have to pay the purchase price at closing, and any deposits will be returned. All such contingencies must be specifically set forth in the parties' agreement. Breach, on the other hand, occurs when one party refuses to perform but does not have a legal basis for his refusal. For example, a seller might decide he wants to pull out of the deal because he has learned of another prospective purchaser who is willing to pay a much higher purchase price. This would almost certainly not be a permissible basis for terminating the transaction under the parties' agreement, and if the seller refused to go forward with the sale, he would be in breach of the parties' contract. On the other hand, a purchaser might decide that he had grossly overbid on a property and fail to show up on the date of closing. Absent a lawful basis that would excuse performance, that buyer would be in breach of the parties' agreement.

Remedies for Breach

The remedies for breach of a contract to purchase real estate usually will depend upon whether it is the buyer or seller who is in breach.

Most contracts for the purchase of real estate will provide for the buyer to tender a deposit. If the buyer fails to perform – that is, fails to show up on the date of closing and pay the agreed-upon closing price – the buyer forfeits that deposit as liquidated damages. Such provisions are standard practice because it is difficult for the seller to quantify the actual damages that he will suffer as a result of the buyer's breach, such as additional marketing costs, carrying costs, and a potential decrease in the ultimate sales price. Because of the nature of liquidated damages, these are typically the seller's only remedy for breach, and this will often be expressly provided in the parties' contract.

If the seller refuses to perform, the buyer's remedy will typically be specific performance. Specific performance is a contract remedy whereby the breaching party can be ordered to perform as agreed upon. The aggrieved would-be purchaser will need to file a complaint in court seeking an order that the seller convey the property to the buyer for the agreed-upon purchase price.

The purchaser would also seek a memorandum lis pendens from the court. This legal notice issued by the court is recorded at the registry of deeds and will serve as a cloud upon the title of the real estate until the parties' dispute concludes – in effect preventing a sale to any other potential purchasers.

Conclusion: Real estate transactions, particularly in today's market, can be fraught with traps for the unwary. A party entering into a potentially binding real estate transaction should do so with the advice of counsel and with an understanding of any contingencies and the consequences of breach.

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