

Real Estate

Contracts Are Hard To Break

By JAY ROMANO

There is one thing a real estate lawyer dreads, it is hearing a client under contract to buy or sell a house or apartment utter the words: "I've changed my mind. Get me out of this deal."

The reason for the discomfort is not that real estate lawyers are skittish about engaging in legal skirmishes, but that most are not inclined to fight battles they are likely to lose. And trying to get a client out of a well-drafted real estate contract, lawyers say, is often a losing battle.

"Whenever a client comes to me and says 'I can't go through with this deal,'" said Eric Gonchar, a Manhattan real estate lawyer, "the first thing I'll usually say is, 'This is not going to be easy.'"

Indeed, Mr. Gonchar said, since the primary goal of both buyers and sellers negotiating a real estate contract in good faith is to arrive at an agreement that neither party can break, a well-drafted contract will keep the parties in the deal until the property changes hands for the agreed-upon price.

Litigation for breach of a real-estate contract can take years to resolve," Mr. Gonchar said. "And it usually ends up costing both sides lots of money."

Felix Nihamin, a Manhattan real estate lawyer who also practices in New Jersey, said that in most cases, real estate contracts contain provisions — typically referred to as "contingencies" — that allow the party or the other to back out of the deal, usually without penalty, under certain circumstances. For example, he said, most contracts are contingent upon the purchaser obtaining a commitment for a mortgage within a specific period of time. If the buyer cannot obtain the commitment within that time — after having made a good faith effort to do so — then either party generally has the right to cancel the contract.

Another common contingency found in contracts for the sale of a home in New Jersey, Mr. Nihamin said, permits the buyer to have the house inspected to determine

whether it has any serious structural or mechanical defects. (In New York and Connecticut, such issues are often addressed before the contract is signed.) In most cases, the buyer will then be able to get out of the deal if the inspection reveals serious problems and the seller declines to either remedy them or adjust the price.

Yet another contingency — one commonly found in sales contracts for co-op apartments — is a provision that conditions the sale upon approval by the co-op's board. If the board does not give the approval, Mr. Nihamin said, both parties are relieved of their obligations under the contract.

In most cases, the only way out of a contract is if a contingency has not been met," Mr. Nihamin said, adding, however, that it may be possible for a party to get out of a contract if circumstances change significantly after a contingency has been met.

For example, he said, if a buyer loses a job — or a substantial portion of his or her income — after a mortgage commitment has been issued, the lender is likely to withdraw the commitment. And while the seller's lawyer could claim that once the commitment had been accepted by the buyer, the contingency had been satisfied, Mr. Nihamin said he believes the change in circumstances may provide a sufficient basis for the buyer to get out of the contract.

Within the past month alone, I've gotten three clients out of contracts because of a change in financial circumstances," Mr. Nihamin said, referring to clients who lost all or much of their income as a result of the World Trade Center disaster.

It might also be possible for a buyer to get out of a contract or at least renegotiate its terms if the amount the property is appraised for is reduced after the commitment has been issued and the commitment is conditioned on the original appraisal. "I had one deal where the appraisal on a property was reduced by 10 percent," he

said, adding that in this case, rather than attempt to cancel the deal, the buyer requested a reduced purchase price, and the seller agreed to it.

In most cases, however, buyers or sellers who try to wriggle their way out of a real estate sales contract want to do so for more practical reasons: the buyer has found a better house at a better price; the seller has found a buyer willing to pay more money; or one or the other has simply changed his or her mind.

Scott Konner, a Manhattan real estate lawyer, said that when a buyer or seller decides to back out of a contract for no legitimate reason, the terms of the contract itself generally dictate what happens next. And most real estate contracts used in New York usually treat defaulting buyers differently than defaulting sellers.

"In my opinion, Rule No. 1 is that every real estate contract should provide that the total liability of the buyer in the event of a default is the amount of the buyer's deposit," he said, referring to the 10 percent deposit typically paid at the time a contract is signed. Such a provision, also known as a "liquidated damages clause," basically specifies the amount of money that the seller is entitled to if the buyer defaults.

Mr. Konner explained that some contracts — particularly those used by developers marketing new properties — may contain a provision giving the seller the right to demand what is known as "specific performance" on the part of the buyer. This means that instead of keeping the buyer's deposit, the seller can instead insist the buyer "specifically perform" the contract by going through with the sale. Generally speaking, Mr. Konner said, if a buyer's lawyer insists that the specific performance provision be taken out of the contract, the seller will usually comply because the courts are quite reluctant to hold a buyer to specific performance.

On the other hand, Mr. Konner said, buyers generally want the right to demand specific performance from the seller and courts are typically inclined to grant it.

"When you're a seller, you can't just walk away from the deal," he said, explaining that under New York law a buyer is usually entitled to specific performance from the seller even if the contract does not explicitly provide for it. There are certain circumstances, however, where the seller may be able to get out of a contract. For example, Mr. Konner said, when there is a problem with the title to a property that the seller cannot resolve, most contracts allow him to back out of the deal.

Just being legally entitled to demand a defaulting buyer's deposit if you're a seller — or a defaulting seller's specific performance if you're a buyer — does not provide any guarantee that either will be easy to get.

Dennis Greenstein, a Manhattan real estate lawyer, said that regardless of whether it is the buyer or seller who is in breach of the contract, it is generally a court that will end up as the final arbiter of the dispute. And that, he said, often makes it more economical for the parties to work out their differences themselves.

"The time involved, the cost involved and the uncertainty of the outcome make settling a dispute in court a risky proposition for both parties," Mr. Greenstein said. "So if there is a way for the parties to come to an agreement both sides can live with, that's probably going to be the best possible outcome."