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Real Estate Contracts

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A. Definition of a "contract"

- A contract is a *voluntary* agreement or promise between legally competent parties, supported by legal consideration, to perform (or refrain from performing) some legal act.

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A contract must be:

- **Voluntary** – no one may be forced into a contract
- **An agreement or a promise** – a contract is essentially a legally enforceable promise
- **Made by legally competent parties** – the parties must be viewed by the law as capable of making a legally binding promise.....

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A contract must be:

- Supported by **legal consideration** – a contract must be supported by some valuable thing that induces a party to enter into the contract and that must be legally sufficient to support a contract
- **About a legal act** – no one may make a legal contract to do something illegal.

B. Legal Classifications of Contracts:

B. Express vs. Implied (depending on how it is created)

- **Express** contract exists when the parties state the terms and show their intentions in *words*. (can be oral or written)
- **EXAMPLE:** Harold approaches his neighbor, Bill, and says, "I will paint your house today for \$50." Bill replies, "If you paint my house today, I will pay you \$50." Harold and Bill have entered into an express contract.

Contracts – Classifications:

• Express vs. Implied (depending on how it is created)

- In an **Implied** contract the agreement of the parties is demonstrated by their *acts and conduct*.
- **EXAMPLE:** Karen goes into a restaurant and orders a meal. Karen has entered into an implied contract with the restaurant to pay for the meal, even though payment was not mentioned before the meal was ordered.
- Under the statute of frauds certain types of contracts must be in writing to be enforceable in a court of law such as those dealing with *real estate*.

Contracts – Classifications:

C. Unilateral vs. Bilateral

- A **unilateral contract** is a one-sided agreement. One party makes a promise to induce a second party to do something.
- **EXAMPLE:** Bill puts up a sign that says, "If you paint my house today, I will pay you \$500." If Harold paints Bill's house, Bill will be legally obligated to pay Harold. Bill and Harold have a *unilateral contract*. On the other hand, if Harold says to Bill, "I will paint your house for \$500," and Bill replies, "I will pay you \$500 for painting my house," they have a *bilateral contract*, a promise exchanged for a promise.

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Contracts – Classifications:

- Unilateral vs. Bilateral
 - In a **bilateral contract**, both parties promise to do something; one promise is given in exchange for another.
 - EXAMPLE: A listing agreement is a bilateral contract in which the broker promises to use his or her skills to produce a buyer and the seller promises to pay a commission or brokerage fee.

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Contracts – Classifications:

D. Executed vs. Executory

- An **executed contract** is one in which all parties have fulfilled their promises: The contract has been performed.
- An **executory contract** exists when one or both parties still have an act to perform.

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C. Legal Status of Contracts

- **Void** – when it has no legal force or effect because it lacks some or all of the essential elements of a contract.
- **Valid** – when it meets all the essential elements that make it legally sufficient, or enforceable.
- **Voidable** – when it appears on the surface to be valid but may be rescinded or disaffirmed by one or both parties based on some legal principle.

Legal Status of Contracts

- **Unenforceable** – also appears on the surface to be valid; however, neither party can sue the other to force performance.
- **EXAMPLE:** An oral agreement for the sale of a parcel of real estate would be unenforceable. Because the statute of frauds requires that real estate sales contracts be in writing, the defaulting party could not be taken to court and forced to perform.

D. Essential Elements of a VALID Contract

- **Legal Capacity** – A contract must be for a legal purpose. If the contract is to do something illegal, it is not a valid contract.
- **Legally Competent Parties** – All parties to the contract must have *legal capacity*, that is, they must be of legal age and have enough mental capacity to understand the nature or consequences of their actions in the contract.

Essential Elements of a VALID Contract

- **Mutual Consent**, Meeting of the Minds – there must be complete agreement between the parties about the purpose and terms of the contract. Usually evidenced by signatures.
- **Legal Purpose** – the agreement must be for a legal and lawful purpose.

Essential Elements of a VALID Contract

- **Consideration** – The contract must be based on consideration. (Consideration is something of legal value offered by one party and accepted by another as an inducement to perform or to refrain from some act)
Classified as either valuable consideration or good consideration.

Essential Elements of a VALID Contract

- **Capacity to Contract**
 - Contracts by minors are not void, but voidable
- *For Real Estate, it must include an enforceable legal description*

Offer and Acceptance

- **Offer** – when a prospective buyer is found, a broker helps prepare an offer to purchase. The offer is signed by the prospective buyer.
- **Acceptance** – when the seller agrees to an offer *as it was made* and signs the document, the offer has been accepted.
- **Counter Offer** – any change to the terms proposed creates a counteroffer.

Offer and Acceptance

- **Amendment** – a change to an accepted contract, that all parties agree to.
- **Addendum** – an addition to the contract prior to acceptance
- **Rejection** – when an offer is not accepted and no counter offer is given
 - NOTE: An offer or counteroffer may be revoked at anytime before it has been accepted- even if the contract stated it was open for a set period of time

E. Terminating a Contract

- A contract is discharged when the agreement is terminated. Can happen in one of several ways:
 - A. **Full Performance** of a contract – Each party has certain rights and duties to fulfill.
 - "Time is of the essence" – This means that the contract must be performed within the time limit specified. A party who fails to perform on time is liable for breach of contract.

Terminating a Contract

- B. **Agreement Between the Parties:**

Cancellation vs. withdrawal

Definitions

1. **Withdrawal** – the contract remains in full force and effect, but the property is no longer marketed or offered for sale by the broker.
2. **Cancellation** – the contract is fully terminated, either with or without the broker's consent and with or without "good cause" on the part of the seller.

Terminating a Contract

3. **Rescission** – mutual agreement between parties that effectively rescinds a contract would be as if it never existed in the first place.

Terminating a Contract

4. **Assignment** – is a transfer of rights or duties under a contract.

- o **EXAMPLE:** John enters into a contract to paint Tim's tool shed. Under the terms of the contract, John will be paid \$1,000 when the job is finished. John owes \$1,000 to Rob, and so John assigns to Rob the right to receive the payment. When the job is done, Tim will pay \$1,000 to Rob.....

Terminating a Contract

- On the other hand, suppose that the day after John contracts to paint Tim's tool shed for \$1,000, Ken offers John \$3,000 to paint a gazebo. John wants to take the better paying job but doesn't want to breach the contract with Tim. If the contract with Tim permits it, John may assign both the right to be paid and the duty to paint the tool shed to Peter, another painter. If Peter fails to paint the tool shed, however, John will be liable to Tim for breach of contract.

Terminating a Contract

5. **Novation** – A contract may be performed by novation, that is, the substitution of a new contract in place of the original.

Terminating a Contract

C. **Breach of contract**

A contract may be terminated if it is breached by one of the parties. A breach of contract is a violation of any of the terms or conditions of a contract without legal excuse.

Termination of a Contract

- 1. **Rescission** – court allows the contract to be treated as if it never existed
- 2. **Liquidated Damages** – true damages aren't apparent so court may determine a number
- 3. **Damages** – actual damages as evidenced by expenditures
- 4. **Specific Performance** – court enforces parties to perform to the terms of the agreed contract

Terminating a Contract

- D. **Partial Performance** – The parties could agree that the work is performed "close enough."
- E. **Substantial Performance** – EX: a newly constructed addition to the home is complete except for polishing the brass doorknobs. The contractor is entitled to the final payment.

Termination of a Contract

- F. **Impossibility of Performance** – when an act required by the contract cannot be legally accomplished.
- G. **Operation of Law** – voiding of a contract by a minor. as a result of fraud. Because a contract was altered...

F. Statute of Limitations

The law of every state limits the time within which parties to a contract may bring legal suit to enforce their rights. The statute of limitations varies for different legal actions, and any rights not enforced within the applicable time period are lost.

F. Time is of the Essence

Pay attention to deadlines!

Discharge of a Contract

• Statute of Limitations

Written Contract	5 Years
Judgment Lien	5 Years
Adverse Possession	20 Years
Easement by Prescription	20 Years
Verbal Contract	4 Years
Mechanics Lien	6 Months

G. Contracts used in Real Estate

A. Seller Representation Agreement

TYPES OF LISTING AGREEMENTS:

- **Open Listing** EX: "FSBO" - A seller may compensate any broker who brings in an offer or they may sell it themselves.
- **Exclusive-Agency (office) Listing** EX: FSBO & one Broker is the exclusive agent of the principal. (Seller retains the right to sell the property without obligation to the broker.)

Contracts used in Real Estate

Seller Representation Agreement

TYPES OF LISTING AGREEMENTS:

- **Exclusive-Right-to-Sell Listing**
 - If the property sells during the contract, the broker is entitled to a commission regardless of who sells the property.
- **Net Listing**
 - This type of listing is illegal in many states. In Idaho, while not illegal, it doesn't meet the statutory elements of a contract and therefore is not considered a valid contract.

Contracts used in Real Estate

B. Buyer Representation Agreement

TYPES OF LISTING AGREEMENTS:

- **Exclusive-Agency Buyer Agency agreement** - The broker is entitled to payment only if he or she locates the property ultimately purchases.
- **Exclusive Buyer Representation Agreement** - The broker is entitled to payment regardless of whether he or she locates the property. Even if the buyer finds the property independently, the agent is entitled to payment.

Contracts used in Real Estate

- Options
- Land Sales Contracts
 - The buyer agrees to give the seller a down payment and pay regular monthly installments of principal and interest over a number of years. Once it is paid off then the deed is transferred.
- Leases

Contracts used in Real Estate

- Escrow Agreements
 - Used when a party carries back a note and deed of trust
- Purchase & Sales Agreements (RE21) – Contracts created by attorneys so that real estate agents can “fill in the blanks” and assist in the purchase and sale of real estate.
- Purchase & Sales Agreement- New Construction (RE22)

H. Idaho Requirements for a Valid Real Estate Contract

1. Legally competent parties
2. An offer and acceptance or mutual assent that includes meeting of the minds
3. Legal objective
4. Legal consideration
5. An enforceable legal description
6. Written document, signed by all parties to the contract

Statute of Frauds in Idaho:

Defined by Idaho Supreme Court:
"Agreements for the sale of real property or of an interest therein and leases of real property for a period of more than one year are unenforceable unless the sale or lease agreement, or some note or memorandum thereof, is in writing and signed by both parties."

I. Interpleader Action

- Earnest Money in Dispute
